

LogMeIn, Inc.  
Form 10-Q  
July 25, 2014  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended June 30, 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: 001-34391**

**LOGMEIN, INC.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**20-1515952**  
**(I.R.S. Employer**  
**Identification No.)**

**320 Summer Street, Suite 100**

**Boston, Massachusetts**  
**(Address of principal executive offices)**

**02210**  
**(Zip Code)**

**781-638-9050**

**(Registrant's telephone number, including area code)**

**(Former name, former address and former fiscal year, if changed since last report)**

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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  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

As of July 18, 2014, there were 24,617,804 shares of the registrant's Common Stock, par value \$0.01 per share, outstanding.



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**Table of Contents****Part I. Financial Information****Item 1. Financial Statements****LogMeIn, Inc.****Condensed Consolidated Balance Sheets****(In thousands, except share and per share data)**

	<b>December 31, 2013</b>	<b>June 30, 2014</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 89,257	\$ 120,828
Marketable securities	100,299	100,170
Accounts receivable (net of allowance for doubtful accounts of \$269 and \$279 as of December 31, 2013 and June 30, 2014, respectively)	12,957	10,601
Prepaid expenses and other current assets	6,508	7,537
Restricted cash, current portion	23	1,492
Deferred income tax assets	3,053	3,053
Total current assets	212,097	243,681
Property and equipment, net	13,198	13,661
Restricted cash, net of current portion	3,902	2,584
Intangibles, net	16,886	17,476
Goodwill	18,712	25,007
Other assets	5,348	5,231
Deferred income tax assets	9,470	9,218
Total assets	\$ 279,613	\$ 316,858
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 6,390	\$ 5,958
Accrued liabilities	20,110	19,023
Deferred revenue, current portion	82,496	106,496
Total current liabilities	108,996	131,477
Deferred revenue, net of current portion	2,667	1,845
Other long-term liabilities	611	2,022
Total liabilities	112,274	135,344

Commitments and contingencies (Note 10)

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Preferred stock, \$0.01 par value - 5,000,000 shares authorized, 0 shares outstanding as of December 31, 2013 and June 30, 2014		
Equity:		
Common stock, \$0.01 par value - 75,000,000 shares authorized as of December 31, 2013 and June 30, 2014; 25,371,844 and 26,092,834 shares issued as of December 31, 2013 and June 30, 2014, respectively; 24,103,201 and 24,629,180 outstanding as of December 31, 2013 and June 30, 2014, respectively	254	262
Additional paid-in capital	200,235	219,127
(Accumulated deficit) retained earnings	(1,439)	895
Accumulated other comprehensive loss	(1,186)	(1,296)
Treasury stock, at cost - 1,268,643 and 1,463,654 shares as of December 31, 2013 and June 30, 2014, respectively	(30,525)	(37,474)
Total equity	167,339	181,514
Total liabilities and equity	\$ 279,613	\$ 316,858

See notes to condensed consolidated financial statements.

**Table of Contents****LogMeIn, Inc.****Condensed Consolidated Statements of Operations****(In thousands, except share and per share data)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
Revenue	\$ 40,670	\$ 54,975	\$ 78,107	\$ 103,995
Cost of revenue	4,776	7,397	9,185	13,517
Gross profit	35,894	47,578	68,922	90,478
Operating expenses				
Research and development	6,918	7,973	14,309	14,685
Sales and marketing	22,567	31,053	43,135	58,763
General and administrative	6,352	7,448	17,872	14,125
Amortization of acquired intangibles	180	322	359	525
Total operating expenses	36,017	46,796	75,675	88,098
(Loss) income from operations	(123)	782	(6,753)	2,380
Interest income, net	155	149	320	260
Other (expense) income	(198)	224	454	196
(Loss) income before income taxes	(166)	1,155	(5,979)	2,836
(Provision for) benefit from income taxes	(1,194)	175	(1,188)	(502)
Net (loss) income	\$ (1,360)	\$ 1,330	\$ (7,167)	\$ 2,334
Net (loss) income per share:				
Basic	\$ (0.06)	\$ 0.05	\$ (0.29)	\$ 0.10
Diluted	\$ (0.06)	\$ 0.05	\$ (0.29)	\$ 0.09
Weighted average shares outstanding:				
Basic	24,262,417	24,425,081	24,485,429	24,134,686
Diluted	24,262,417	25,159,340	24,485,429	24,889,730

See notes to condensed consolidated financial statements.

Table of Contents**LogMeIn, Inc.****Condensed Consolidated Statements of Comprehensive (Loss) Income****(In thousands)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
Net (loss) income	\$ (1,360)	\$ 1,330	\$ (7,167)	\$ 2,334
Other comprehensive income (loss):				
Net unrealized (losses) gains on marketable securities, net of tax	(49)	(15)	(68)	6
Net translation gains (losses)	318	19	(1,196)	(116)
Total other comprehensive income (loss)	269	4	(1,264)	(110)
Comprehensive (loss) income	\$ (1,091)	\$ 1,334	\$ (8,431)	\$ 2,224

See notes to condensed consolidated financial statements.



**Table of Contents****LogMeIn, Inc.****Condensed Consolidated Statements of Cash Flows****(In thousands)**

	<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>
<b>Cash flows from operating activities</b>		
Net (loss) income	\$ (7,167)	\$ 2,334
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Depreciation and amortization	3,596	5,499
Amortization of premium on investments	77	122
Provision for bad debts	41	32
Provision for deferred income taxes	198	268
Stock-based compensation	10,282	12,151
Gain on disposal of equipment	(1)	(1)
Changes in assets and liabilities:		
Accounts receivable	3,601	2,575
Prepaid expenses and other current assets	(3,388)	(1,009)
Other assets	(1,794)	210
Accounts payable	(2,409)	433
Accrued liabilities	1,997	(1,327)
Deferred revenue	8,052	23,394
Other long-term liabilities	(174)	721
Net cash provided by operating activities	12,911	45,402
<b>Cash flows from investing activities</b>		
Purchases of marketable securities	(60,381)	(19,984)
Proceeds from sale or disposal of marketable securities	60,000	20,000
Purchases of property and equipment	(6,456)	(4,348)
Intangible asset additions	(915)	(1,322)
Cash paid for acquisition, net of cash acquired		(7,434)
Decrease (increase) in restricted cash and deposits	125	(200)
Net cash used in investing activities	(7,627)	(13,288)
<b>Cash flows from financing activities</b>		
Proceeds from issuance of common stock upon option exercises	267	10,306
Income tax benefit from the exercise of stock options	2	
Common stock withheld to satisfy income tax withholdings for restricted stock unit vesting	(917)	(3,557)
Purchase of treasury stock	(14,607)	(6,949)
Net cash used in financing activities	(15,255)	(200)

Effect of exchange rate changes on cash and cash equivalents and restricted cash	(883)	(343)
Net (decrease) increase in cash and cash equivalents	(10,854)	31,571
Cash and cash equivalents, beginning of period	111,932	89,257
Cash and cash equivalents, end of period	\$ 101,078	\$ 120,828
<b>Supplemental disclosure of cash flow information</b>		
Cash paid for interest	\$	\$ 2
Cash paid for income taxes	\$ 6,287	\$ 568
<b>Noncash investing and financing activities</b>		
Purchases of property and equipment included in accounts payable and accrued liabilities	\$ 1,515	\$ 687
Fair value of contingent consideration in connection with acquisition included in accrued liabilities and other long term liabilities	\$ 176	\$
See notes to condensed consolidated financial statements.		

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**Table of Contents****LogMeIn, Inc.****Notes to Condensed Consolidated Financial Statements****1. Nature of the Business**

LogMeIn, Inc. (the Company) provides a portfolio of secure, easy-to-use cloud-based offerings aimed at transforming the way people work and live through secure connections to the computers, devices, data and people that make up their digital world. The Company's product line includes AppGuru, BoldChatCubby, join.me, LogMeIn Pro®, LogMeIn® Central, LogMeIn Rescue®, LogMeIn® Rescue+Mobile, LogMeIn Backup®, LogMeIn for iOS, LogMeIn Hamachi®, Xively and RemotelyAnywhere®. The Company is headquartered in Boston, Massachusetts with wholly-owned subsidiaries in Hungary, The Netherlands, Australia, the United Kingdom, Brazil, Japan, Ireland, and India.

**2. Summary of Significant Accounting Policies**

*Principles of Consolidation* The accompanying condensed consolidated financial statements include the results of operations of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. The Company has prepared the accompanying condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP).

*Unaudited Interim Condensed Consolidated Financial Statements* The accompanying condensed consolidated financial statements and the related interim information contained within the notes to the condensed consolidated financial statements are unaudited and have been prepared in accordance with GAAP and applicable rules and regulations of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. The accompanying unaudited condensed consolidated financial statements should be read along with the Company's audited financial statements included in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on March 10, 2014. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited condensed consolidated financial statements and in the opinion of management, reflect all adjustments, consisting of normal and recurring adjustments, necessary for the fair presentation of the Company's financial position, results of operations and cash flows for the interim periods presented. The results for the interim periods presented are not necessarily indicative of future results. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

*Use of Estimates* The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. By their nature, estimates are subject to an inherent degree of uncertainty. Actual results could differ from those estimates.

*Marketable Securities* The Company's marketable securities are classified as available-for-sale and are carried at fair value with the unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive income in equity. Realized gains and losses and declines in value judged to be other than temporary are included as a component of earnings based on the specific identification method. Fair value is determined based on quoted market prices. At December 31, 2013 and June 30, 2014, marketable securities consisted of U.S. government agency securities that have remaining maturities within two years and have an aggregate amortized cost of approximately

\$100.3 million and \$100.1 million and an aggregate fair value of approximately \$100.3 million and \$100.2 million, including approximately \$67,000 and \$59,000 of unrealized gains and approximately \$28,000 and \$10,000 of unrealized losses, respectively.

*Revenue Recognition* The Company derives revenue primarily from subscription fees related to its LogMeIn premium services and the delivery of professional services, primarily related to its Xively business.

Revenue from the Company's LogMeIn premium services is recognized on a daily basis over the subscription term as the services are delivered, provided that there is persuasive evidence of an arrangement, the fee is fixed or determinable and collectability is deemed reasonably assured. Subscription periods range from monthly to five years, but are generally one year in duration. The Company's software cannot be run on another entity's hardware nor do customers have the right to take possession of the software and use it on their own or another entity's hardware.

The Company's multi-element arrangements typically include subscription and professional services, which may include development services. The Company evaluates each element within the arrangement to determine if they can be accounted for as separate units of accounting. If the delivered item or items have value to the customer on a standalone basis, either because they are sold separately by any vendor or the customer could resell the delivered item or items on a standalone basis, the Company has determined that the deliverables within these arrangements qualify for treatment as separate units of accounting. Accordingly, the Company recognizes revenue for each delivered item or items as a separate earnings process commencing when all of the significant performance obligations have been performed and when all of the revenue recognition criteria have been met. Professional services revenue recognized as a separate earnings process under multi-element arrangements has been immaterial to date. In cases where the Company has determined that the delivered items within its multi-element arrangements do not have value to the customer on a stand-alone basis, the arrangement is accounted for as a single unit of accounting and the related consideration is recognized ratably over the estimated customer life, commencing when all of the significant performance obligations have been delivered and when all of the revenue recognition criteria have been met.

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The Company currently only offers free versions of its iPhone, iPad and Android software products. The Company had formerly sold these iPhone, iPad and Android software products as perpetually licensed software, the revenue from which was recognized when there was persuasive evidence of an arrangement, the product had been provided to the customer, the collection of the fee was probable, and the amount of fees to be paid by the customer was fixed or determinable.

Revenues are reported net of applicable sales and use tax, value-added tax, and other transaction taxes imposed on the related transaction.

*Concentrations of Credit Risk and Significant Customers* The Company's principal credit risk relates to its cash, cash equivalents, marketable securities, restricted cash, and accounts receivable. Cash, cash equivalents, and restricted cash are deposited primarily with financial institutions that management believes to be of high-credit quality and custody of its marketable securities is with an accredited financial institution. To manage accounts receivable credit risk, the Company regularly evaluates the creditworthiness of its customers and maintains allowances for potential credit losses. To date, losses resulting from uncollected receivables have not exceeded management's expectations.

As of December 31, 2013, no customers accounted for 10% or more of accounts receivable and no customers accounted for 10% or more of revenue for the three and six months ended June 30, 2013 or 2014. As of June 30, 2014, one customer accounted for 10% of accounts receivable.

*Goodwill* Goodwill is the excess of the acquisition price over the fair value of the tangible and identifiable intangible net assets acquired. The Company does not amortize goodwill, but performs an annual impairment test of goodwill on the last day of its fiscal year and whenever events and circumstances indicate that the carrying amount of goodwill may exceed its fair value. The Company operates as a single operating segment with one reporting unit and consequently evaluates goodwill for impairment based on an evaluation of the fair value of the Company as a whole. Through June 30, 2014, no impairments have occurred.

*Long-Lived Assets and Intangible Assets* The Company records intangible assets at their estimated fair values at the date of acquisition. Intangible assets are amortized based upon the pattern in which their economic benefit will be realized, or if this pattern cannot be reliably determined, using the straight-line method over their estimated useful lives. The Company's intangible assets have estimated useful lives which range from four months to seven years.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, including intangible assets, may not be recoverable. When such events occur, the Company compares the carrying amounts of the assets to their undiscounted expected future cash flows. If this comparison indicates that there is impairment, the amount of the impairment is calculated as the difference between the carrying value and fair value. Through June 30, 2014, no impairments have occurred.

*Foreign Currency Translation* The functional currency of operations outside the United States of America is deemed to be the currency of the local country, unless otherwise determined that the United States dollar would serve as a more appropriate functional currency given the economic operations of the entity. Accordingly, the assets and liabilities of the Company's foreign subsidiaries are translated into United States dollars using the period-end exchange rate, and income and expense items are translated using the average exchange rate during the period. Cumulative translation adjustments are reflected as a separate component of equity. Foreign currency transaction gains and losses are charged to operations. The Company had foreign currency losses of approximately \$199,000 for the three months ended June 30, 2013 and foreign currency gains of approximately \$454,000 for the six months ended June 30, 2013, respectively, and foreign currency gains of approximately \$224,000 and \$197,000 for the three and six months ended June 30, 2014, respectively.

*Stock-Based Compensation* Stock-based compensation is measured based upon the grant date fair value and recognized as an expense on a straight-line basis in the financial statements over the vesting period of the award for those awards expected to vest. The Company uses the Black-Scholes option pricing model to estimate the grant date fair value of stock awards. The Company uses the with-or-without method to determine when it will realize excess tax benefits from stock based compensation. Under this method, the Company will realize these excess tax benefits only after it realizes the tax benefits of net operating losses from operations.

*Income Taxes* Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction.

The Company evaluates its uncertain tax positions based on a determination of whether and how much of a tax benefit taken by the Company in its tax filings or positions is more likely than not to be realized. Potential interest and penalties associated with any uncertain tax positions are recorded as a component of income tax expense. As of December 31, 2013 and June 30, 2014, the Company has provided a liability for approximately \$304,000 and \$484,000 for uncertain tax positions, respectively. These uncertain tax positions would impact the Company's effective tax rate if recognized.

*Segment Data* Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision-maker, or decision making group, in making decisions regarding resource allocation and assessing performance. The Company, which uses consolidated financial information in determining how to allocate resources and assess performance, has determined that it operates in one segment.

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The Company's revenue by geography (based on customer address) is as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2014	2013	2014
Revenues:				
United States	\$ 26,695	\$ 36,465	\$ 51,483	\$ 68,870
United Kingdom	3,643	4,918	7,106	9,325
International - all other	10,332	13,592	19,518	25,800
<b>Total revenue</b>	<b>\$ 40,670</b>	<b>\$ 54,975</b>	<b>\$ 78,107</b>	<b>\$ 103,995</b>

**Guarantees and Indemnification Obligations** As permitted under Delaware law, the Company has agreements whereby the Company indemnifies certain of its officers and directors for certain events or occurrences while the officer or director is, or was, serving at the Company's request in such capacity. The term of the indemnification period is for the officer's or director's lifetime. As permitted under Delaware law, the Company also has similar indemnification obligations under its certificate of incorporation and by-laws. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has director's and officer's insurance coverage that the Company believes limits its exposure and enables it to recover a portion of any future amounts paid.

The Company has entered into agreements with certain customers that contractually obligate the Company to indemnify the customer from certain claims, including claims alleging that the Company's products infringe third-party patents, copyrights, or trademarks. The term of these indemnification obligations is generally perpetual. The maximum potential amount of future payments the Company could be required to make under these indemnification obligations is unlimited. Through June 30, 2014, the Company has not experienced any losses related to these indemnification obligations.

In November 2012, the Company filed suit against Pragmatius Telecom LLC (Pragmatius), seeking declaratory judgment after certain of the Company's customers received letters from Pragmatius claiming that their use of certain LogMeIn services infringed upon three patents allegedly owned by Pragmatius. On March 29, 2013, the Company and Pragmatius entered into a License Agreement, which granted the Company a fully-paid license covering the patents at issue. The Company paid Pragmatius a one-time licensing fee in April 2013, after a portion of the fee was reimbursed in March 2013 from a designated escrow arrangement associated with a prior acquisition. The Company recorded approximately \$1.2 million of expense related to this matter in general and administrative expenses in March 2013. As a result, the Company's declaratory judgment action against Pragmatius was dismissed by the court on May 3, 2013.

**Net (Loss) Income Per Share** Basic net (loss) income per share is computed by dividing net (loss) income by the weighted average number of common shares outstanding for the period. Diluted net (loss) income per share is computed by dividing net (loss) income by the sum of the weighted average number of common shares outstanding during the period and the weighted average number of potential common shares outstanding from the assumed exercise of stock options and the vesting of restricted stock units. For the three and six months ended June 30, 2013, the Company incurred a net loss and therefore, the effect of the Company's outstanding common stock equivalents were not included in the calculation of diluted loss per share as they were anti-dilutive. Accordingly, basic and dilutive net loss per share for the period were identical.

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

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
Options to purchase common shares	2,947	50	2,947	457
Restricted stock units	1,134	71	1,134	408
<b>Total options and restricted stock units</b>	<b>4,081</b>	<b>121</b>	<b>4,081</b>	<b>865</b>



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Basic and diluted net (loss) income per share was calculated as follows (in thousands, except share and per share data):

	<b>Three Months Ended June 30, 2013</b>	<b>Six Months Ended June 30, 2013</b>
<b>Basic and diluted net loss per share:</b>		
Net loss	\$ (1,360)	\$ (7,167)
<b>Weighted average common shares outstanding</b>		
	24,262,417	24,485,429
Basic and diluted net loss per share	\$ (0.06)	\$ (0.29)
<b>Basic:</b>		
<b>Three Months Ended June 30, 2014</b>		
<b>Six Months Ended June 30, 2014</b>		
Net income	\$ 1,330	\$ 2,334
<b>Weighted average common shares outstanding, basic</b>		
	24,425,081	24,134,686
Net income per share, basic	\$ 0.05	\$ 0.10
<b>Diluted:</b>		
Net income	\$ 1,330	\$ 2,334
<b>Weighted average common shares outstanding</b>		
	24,425,081	24,134,686
Add: Options to purchase common shares and restricted stock units	734,259	755,044
<b>Weighted average common shares outstanding, diluted</b>		
	25,159,340	24,889,730
Net income per share, diluted	\$ 0.05	\$ 0.09

*Recently Issued Accounting Pronouncements* On May 28, 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers ( ASU 2014-09 ) its final standard on revenue from contracts with customers. ASU 2014-9 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core

principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the revenue model to contracts within its scope, an entity identifies the contract(s) with a customer, identifies the performance obligations in the contract, determines the transaction price, allocates the transaction price to the performance obligations in the contract and recognizes revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 applies to all contracts with customers that are within the scope of other topics in the FASB Accounting Standards Codification. Certain of ASU 2014-09's provisions also apply to transfers of nonfinancial assets, including in-substance nonfinancial assets that are not an output of an entity's ordinary activities (i.e., property plant and equipment; real estate; or intangible assets). Existing accounting guidance applicable to these transfers has been amended or superseded. ASU 2014-09 also requires significantly expanded disclosures about revenue recognition. ASU 2014-09 is effective for the Company on January 1, 2017. The Company is currently assessing the potential impact of the adoption of ASU 2014-09 on its condensed consolidated financial statements.

### **3. Fair Value of Financial Instruments**

The carrying value of the Company's financial instruments, including cash equivalents, restricted cash, accounts receivable, and accounts payable, approximate their fair values due to their short maturities. The Company's financial assets and liabilities are measured using inputs from the three levels of the fair value hierarchy. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement. The three levels are as follows:

Level 1: Unadjusted quoted prices for identical assets or liabilities in active markets accessible by the Company at the measurement date.

Level 2: Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Unobservable inputs that reflect the Company's assumptions about the assumptions that market participants would use in pricing the asset or liability.

The following table summarizes the basis used to measure certain of the Company's financial assets that are carried at fair value (in thousands):

		<b>Basis of Fair Value Measurements</b>			
			<b>Quoted Prices in Active Markets for Identical Items (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
	<b>Balance</b>				
<b>Balance at December 31, 2013</b>					
Cash equivalents - money market funds	\$ 28,210	\$ 28,210			\$
Cash equivalents - bank deposits	5,001			5,001	
Short-term marketable securities					
U.S. government agency securities	100,299	75,288		25,011	
<b>Balance at June 30, 2014</b>					
Cash equivalents - money market funds	27,504	27,504			
Cash equivalents - bank deposits	5,021			5,021	
Short-term marketable securities - U.S. government agency securities	100,170	95,168		5,002	

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Bank deposits and certain U.S. government agency securities are classified within the second level of the fair value hierarchy as the fair value of those assets are determined based upon quoted prices for similar assets.

**4. Acquisitions**

On March 7, 2014, the Company acquired all of the outstanding capital stock of Ionia Corporation, or Ionia, a Boston, Massachusetts based systems integrator, for a cash purchase price of \$7.5 million plus contingent retention-based bonuses totaling up to \$4.0 million, which are expected to be paid over a two-year period from the date of acquisition. The operating results, which are comprised of approximately \$0.6 million and \$0.8 million of revenue for the three and six months ended June 30, 2014, respectively, as well as \$1.6 million and \$2.1 million of expenses during the three and six months ended June 30, 2014, are included in the condensed consolidated financial statements beginning on the acquisition date.

The acquisition has been accounted for as a business combination. The assets acquired and the liabilities assumed were recorded at their estimated fair values as of the acquisition date. The Company retained an independent third party valuation firm to calculate the fair value of the intangible assets with estimates and assumptions provided by Company management. The excess of the purchase price over the tangible net assets and identifiable intangible assets was recorded as goodwill.

The purchase price was allocated as follows (in thousands):

	<b>Amount</b>
Cash	\$ 67
Current assets	296
Other assets	26
Deferred revenue	(70)
Other liabilities	(864)
Customer backlog	120
Trade name and trademark	10
Customer relationships	1,340
Documented know-how	280
Goodwill	6,295
<b>Total purchase price</b>	<b>\$ 7,500</b>

The pro forma results of operations for the quarter ended June 30, 2013 and 2014 assuming the Company had acquired Ionia on January 1, 2013, do not differ materially from those reported in the Company's condensed consolidated statement of income for that quarter.

The stock purchase agreement included a contingent, retention-based bonus program provision requiring the Company to make additional payments to employees, including former Ionia stockholders now employed by the Company, on the first and second anniversaries of the acquisition, contingent upon their continued employment and achievement of certain bookings goals. The range of the contingent, retention-based bonus payments that the Company could pay is between \$0 to \$4.0 million. The Company has concluded that the arrangement is a compensation arrangement and is accruing the maximum payout ratably over the performance period, as it believes it is probable that the criteria will be

met.

The goodwill recorded in connection with this transaction is primarily related to the expected synergies to be achieved related to the Company's ability to leverage its Xively platform, customer base, sales force and Internet of Things business plan with Ionia's technical expertise and customer base. All goodwill and intangibles acquired are not deductible for income tax purposes.

The Company incurred approximately \$100,000 of acquisition-related costs which are included in general and administrative expense for the three and six months ended June 30, 2014.

During the second quarter of 2014, the Company finalized its purchase price accounting related to the Ionia acquisition and recorded both a deferred tax liability and a corresponding increase in goodwill of approximately \$0.7 million related to the amortization of intangible assets which cannot be deducted for income tax purposes.

### 5. Goodwill and Intangible Assets

The changes in the carry amounts of goodwill for the six months ended June 30, 2014 are due to the addition of goodwill resulting from the acquisition of Ionia (See Note 4 to the Condensed Consolidated Financial Statements).

Changes in goodwill for the six months ended June 30, 2014, are as follows (in thousands):

Balance, December 31, 2013	\$ 18,712
Goodwill related to the acquisition of Ionia	6,295
Balance, June 30, 2014	\$ 25,007

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Intangible assets consist of the following (in thousands):

	Estimated Useful Life	December 31, 2013			June 30, 2014		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Trade names	1-5 years	\$ 666	\$ 666	\$	\$ 676	\$ 670	\$ 6
Customer base	5-7 years	3,789	1,901	1,888	5,129	2,199	2,930
Customer backlog	4 months				120	120	
Domain names	5 years	894	341	553	908	425	483
Software	4 years	299	299		299	299	
Technology	3-6 years	13,963	1,835	12,128	14,363	2,856	11,507
Technology and know-how	3 years	3,176	2,597	579	3,176	3,125	51
Documented know-how	4 years				280	22	258
Non-compete agreements	5 years	162	34	128	162	53	109
Internally developed software	3 years	2,485	875	1,610	3,390	1,258	2,132
		\$ 25,434	\$ 8,548	\$ 16,886	\$ 28,503	\$ 11,027	\$ 17,476

As a result of the acquisition of Ionia, the Company capitalized \$120,000 of customer backlog, \$280,000 of documented know-how, \$10,000 of trade names, and \$1.3 million of customer relationships as intangible assets. The Company is amortizing the intangible assets based upon the pattern in which their economic benefit will be realized, or if this pattern cannot be reliably determined, using the straight-line method over their estimated useful lives. The intangible assets have estimated useful lives which range from four months to seven years.

On November 6, 2013, the Company purchased a software asset for \$11.5 million. This software asset is recorded as an intangible asset and classified as technology and will be amortized using the straight-line method over an estimated useful life of five years, beginning in February 2014 when the product was made available to customers. In May 2014, the Company paid the remaining \$0.5 million for the statement of work in accordance with the agreement. The Company capitalized \$0.4 million as completed technology and \$0.1 million was expensed as consulting work.

The Company capitalized \$317,000 and \$413,000 during the three months ended June 30, 2013 and 2014, respectively, and \$556,000 and \$905,000 during the six months ended June 30, 2013 and 2014, respectively, of costs related to internally developed computer software to be sold as a service incurred during the application development stage and is amortizing these costs over the expected lives of the related services.

The Company is amortizing its intangible assets over the estimated lives noted above. Amortization expense for intangible assets was \$633,000 and \$1.5 million for the three months ended June 30, 2013 and 2014, respectively, and \$1.2 million and \$2.5 million for the six months ended June 30, 2013 and 2014, respectively. Amortization relating to software, technology and know-how, documented know-how, and internally developed software is recorded within cost of revenues and the amortization of trade name and trademark, customer base, customer backlog, domain names, and non-compete agreements is recorded within operating expenses. Future estimated amortization expense for intangible assets is as follows at June 30, 2014 (in thousands):

<b>Amortization Expense (Years Ending December 31)</b>	<b>Amount</b>
2014 (Six months ending December 31)	2,346
2015	4,485
2016	3,939
2017	3,339
2018	2,863
Thereafter	504
<b>Total</b>	<b>\$ 17,476</b>

**6. Accrued Liabilities**

Accrued liabilities consisted of the following (in thousands):

	<b>December 31, 2013</b>	<b>June 30, 2014</b>
Marketing programs	\$ 4,631	\$ 5,651
Payroll and payroll related	9,719	7,419
Professional fees	1,064	1,036
Other accrued liabilities	4,696	4,917
<b>Total accrued liabilities</b>	<b>\$ 20,110</b>	<b>\$ 19,023</b>



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The Company recorded a provision for federal, state and foreign income taxes of approximately \$1.2 million and a benefit of \$175,000 for the three months ended June 30, 2013 and 2014, respectively, and a provision for federal, state and foreign income taxes of approximately \$1.2 million and \$502,000 for the six months ended June 30, 2013 and 2014, respectively. The tax provision for the three and six months ended June 30, 2014, decreased compared to the prior comparable periods as a result of a loss before income taxes incurred in the United States which offset increased profitability in certain foreign jurisdictions, primarily our Irish subsidiaries, which have significantly lower tax rates than the U.S. statutory rate.

Deferred income taxes are provided for the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and operating loss carry-forwards and credits using enacted tax rates expected to be in effect in the years in which the differences are expected to reverse. At each balance sheet date, the Company assesses the likelihood that deferred tax assets will be realized, and recognizes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company's income tax returns since inception are open to examination by federal, state, and foreign tax authorities. The Company has recorded a liability related to uncertain tax provisions of approximately \$304,000 and \$484,000 as of December 31, 2013 and June 30, 2014, respectively. The Company's policy is to record estimated interest and penalty related to the underpayment of income taxes or unrecognized tax benefits as a component of its income tax provision. The Company did not recognize any interest or penalties in its statement of operations during the three or six months ended June 30, 2013. The Company recognized approximately \$5,000 of interest expense for the three months ended June 30, 2014.

**8. Common Stock and Equity**

In February 2013, the Company's board of directors approved a \$25 million share repurchase program. On August 13, 2013, the board of directors approved a new \$50 million share repurchase program, which replaced the previous \$25 million share repurchase program. Share repurchases are made from time-to-time in the open market, in privately negotiated transactions or otherwise, in accordance with applicable securities laws and regulations. The timing and amount of any share repurchases are determined by the Company's management based on its evaluation of market conditions, the trading price of the stock, regulatory requirements and other factors. The share repurchase program may be suspended, modified or discontinued at any time at the Company's discretion without prior notice.

For the three months ended June 30, 2013 and 2014, the Company repurchased 258,663 and 46,511 shares of its common stock at an average price of \$21.76 and \$43.86 per share for a total cost of approximately \$5.6 million and \$2.0 million, respectively. For the six months ended June 30, 2013 and 2014, the Company repurchased 760,485 and 195,011 shares of its common stock at an average price of \$19.21 and \$35.63 per share for a total cost of approximately \$14.6 million and \$6.9 million, respectively. At June 30, 2014, approximately \$29.0 million remained available under the Company's share repurchase program.

**9. Stock Incentive Plan**

The Company's 2009 Stock Incentive Plan ( 2009 Plan ) is administered by the Board of Directors and Compensation Committee, which have the authority to designate participants and determine the number and type of awards to be

granted and any other terms or conditions of the awards. Options generally vest over a four-year period and expire ten years from the date of grant. Restricted stock units with service-based vesting conditions generally vest over a three-year period while restricted stock units with market-based vesting conditions generally vest over two or three-year periods. Certain stock-based awards provide for accelerated vesting if there is a change in control. On May 22, 2014, the Company's stockholders approved an amendment to the 2009 Plan that increased the shares available to grant under the plan by 1,200,000 shares. There were 2,072,394 shares available for grant under the 2009 Plan as of June 30, 2014.

The Company uses the Black-Scholes option-pricing model to estimate the grant date fair value of stock options. The Company estimates the expected volatility of its common stock at the date of grant based on the historical volatility of comparable public companies over the option's expected term as well as its own stock price volatility since the Company's IPO. The Company estimates expected term based on historical exercise activity and giving consideration to the contractual term of the options, vesting schedules, employee turnover, and expectation of employee exercise behavior. The assumed dividend yield is based upon the Company's expectation of not paying dividends in the foreseeable future. The risk-free rate for periods within the estimated life of the stock option is based on the U.S. Treasury yield curve in effect at the time of grant. Historical employee turnover data is used to estimate pre-vesting stock option forfeiture rates. The compensation expense is amortized on a straight-line basis over the requisite service period of the stock award, which is generally four years.

The Company used the following assumptions to apply the Black-Scholes option-pricing model:

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014(1)</b>	<b>2013</b>	<b>2014</b>
Expected dividend yield	0.00%	%	0.00%	0.00%
Risk-free interest rate	0.89%	%	0.87% - 0.89%	1.48%
Expected term (in years)	6.25		6.25	6.25
Volatility	55%	%	55%	55%

(1) There were no stock options granted during the three months ended June 30, 2014.

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The following table summarizes stock option activity, including performance-based options (shares and intrinsic value in thousands):

	<b>Number of shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (Years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at January 1, 2014	2,389	\$ 26.85	6.4	\$ 22,330
Granted	35	41.03		
Exercised	(500)	20.62		\$ 11,037
Forfeited	(75)	33.36		
Outstanding at June 30, 2014	1,849	\$ 28.54	6.3	\$ 33,444
Exercisable at December 31, 2013	1,451	\$ 23.45	5.4	\$ 17,855
Exercisable at June 30, 2014	1,332	\$ 26.72	5.7	\$ 26,522

The aggregate intrinsic value was calculated based on the positive differences between the fair value of the Company's common stock of \$33.55 on December 31, 2013 and \$46.62 per share on June 30, 2014, or at time of exercise, and the exercise price of the options.

The weighted average grant date fair value of stock options issued was \$11.60 per share for the year ended December 31, 2013, and \$21.78 for the six months ended June 30, 2014.

During the three and six months ended June 30, 2014, the Company granted 436,110 and 539,396 restricted stock units, respectively, containing time-based vesting conditions which generally lapse over a three year period.

In August 2013 and May 2014, the Company granted 74,000 and 71,000 restricted stock units with market-based vesting conditions, respectively, which were tied to the Company's achievement of a relative total shareholder return target measured over an applicable performance period which ranges from two to three years (the "TSR Units"). The number of shares underlying these TSR Units that will vest upon the conclusion of the applicable performance periods can range from 0% of the shares awarded to 200% of the shares awarded, or up to 148,000 shares or 142,000 shares for the August 2013 grant and May 2014 grant, respectively. Vesting of such shares is also contingent upon the continued employment of the participant throughout the vesting period. All TSR Units granted by the Company are valued using a Monte Carlo simulation model. The number of awards expected to be earned is factored into the grant date Monte Carlo valuation for the TSR Unit. Compensation cost is recognized regardless of the actual number of awards that are earned based on the market condition. Expected volatility is based on the Company's historical volatility. The risk-free interest rate is based upon U.S. Treasury securities with a term similar to the vesting term of the TSR Units.

The assumptions used in the Monte Carlo simulation model include (but are not limited to) the following:

	<b>August 2013 Grant</b>	<b>May 2014 Grant</b>
Risk-free interest rate	0.62%	0.78%
Volatility	54%	54%

Compensation cost is recognized on a straight-line basis over the requisite service period. At June 30, 2014, all of the TSR Units granted in August 2013 and May 2014 remain outstanding.

The following table summarizes restricted stock unit activity (shares in thousands):

	<b>Number of shares Underlying Restricted Stock Units</b>	<b>Weighted Average Grant Date Fair Value</b>
Unvested as of January 1, 2014	1,192	\$ 28.47
Restricted stock units granted	610	44.38
Restricted stock units vested	(303)	26.88
Restricted stock units forfeited	(101)	26.46
Unvested as of June 30, 2014	1,398	\$ 35.90

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The Company recognized stock based compensation expense within the accompanying condensed consolidated statements of operations as summarized in the following table (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2014	2013	2014
Cost of revenue	\$ 181	\$ 274	\$ 384	\$ 509
Research and development	1,045	1,008	2,062	1,784
Sales and marketing	2,146	2,796	4,227	4,857
General and administrative	1,745	2,635	3,609	5,001
	\$ 5,117	\$ 6,713	\$ 10,282	\$ 12,151

As of June 30, 2014, there was approximately \$47.7 million of total unrecognized share-based compensation cost, net of estimated forfeitures, related to unvested stock awards which are expected to be recognized over a weighted average period of 2.2 years. The total unrecognized share-based compensation cost will be adjusted for future changes in estimated forfeitures.

**10. Commitments and Contingencies**

*Operating Leases* The Company has operating lease agreements for offices in Massachusetts, Hungary, Australia, the United Kingdom, Ireland and India that expire through 2023.

In April 2014, the Company amended its current lease for its Budapest, Hungary office space to provide for an expansion of leased space and to extend the term of the lease. The term of the amended lease began in July 2014 and will extend through June 2019. The aggregate amount of minimum lease payments to be made over the term of the lease is approximately \$7.8 million (EUR 5.7 million). The amended lease agreement required a bank guarantee of approximately \$483,000 (EUR 354,000). The bank guarantee is classified as restricted cash.

Rent expense under all leases was approximately \$1.6 million and \$1.7 million for the three months ended June 30, 2013 and 2014, respectively, and \$2.7 million and \$3.4 million for the six month ended June 30, 2013 and 2014, respectively. The Company records rent expense on a straight-line basis for leases with scheduled escalation clauses or free rent periods.

The Company also enters into hosting services agreements with third-party data centers and internet service providers that are subject to annual renewal. Hosting fees incurred under these arrangements aggregated approximately \$1.3 million and \$1.2 million for the three months ended June 30, 2013 and 2014, respectively, and \$2.3 million and \$2.4 million for the six months ended June 30, 2013 and 2014, respectively.

Future minimum lease payments under non-cancelable operating leases including one year commitments associated with the Company's hosting services arrangements are approximately as follows at June 30, 2014 (in thousands):

**Years Ending December 31**

2014 (Six months ending December 31)	\$ 4,959
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2015	7,377
2016	6,083
2017	5,629
2018	5,930
Thereafter	21,494
<b>Total minimum lease payments</b>	<b>\$ 51,472</b>



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*Litigation* On September 8, 2010, 01 Communique Laboratory, Inc., or 01, filed a complaint that named the Company as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Virginia (Civil Action No. 1:10cv1007) alleging that the Company infringed U.S. Patent No. 6,928,479, or the 479 Patent, which is owned by 01 and has claims directed to a particular application or system for providing a private communication portal from one computer to a second computer. The complaint sought damages in an unspecified amount and injunctive relief. On April 1, 2011, the U.S. District Court for the Eastern District of Virginia granted the Company's motion for summary judgment of non-infringement. The court issued a written order regarding this decision on May 4, 2011. On May 13, 2011, 01 filed a notice of appeal appealing the court's ruling granting summary judgment. On July 31, 2012, the U.S. Court of Appeals for the Federal Circuit vacated the lower court's summary judgment of non-infringement ruling and remanded the case back to the U.S. District Court for the Eastern District of Virginia with revised claim construction. The trial commenced on March 18, 2013 and on March 26, 2013, a jury in the Eastern District of Virginia found that the Company's products do not infringe the 479 Patent as previously asserted by 01. The court issued a written order regarding this decision on April 2, 2013. On June 26, 2013, the court issued a written opinion denying all pending post-trial motions, thereby preserving the jury's non-infringement verdict. On June 26, 2013, 01 filed a notice of appeal seeking to appeal the jury's non-infringement verdict and on July 18, 2013, the Company filed a notice of cross appeal seeking to appeal the jury's decisions regarding invalidity and inequitable conduct. Oral arguments were heard on June 3, 2014 and on June 9, 2014, the U.S. Court of Appeals for the Federal Circuit affirmed the jury's non-infringement verdict. At this time the Company does not believe that a loss is probable and remains unable to reasonably estimate a possible loss or range of loss associated with this litigation.

On November 21, 2012, the Company filed suit against Pragmatius Telecom LLC, or Pragmatius, in the U.S. District Court for the District of Delaware (Civil Action No. 12-1507) seeking a declaratory judgment that the Company's products do not infringe three patents allegedly owned by Pragmatius after certain of the Company's customers received letters from Pragmatius claiming that their use of certain LogMeIn services infringed upon those patents. On March 29, 2013, the Company and Pragmatius entered into a License Agreement, which granted the Company a fully-paid license covering the patents at issue. The Company paid Pragmatius a one-time license fee in connection with the License Agreement in April 2013. As a result, the Company's declaratory judgment action was dismissed by the court on May 3, 2013.

The Company is from time to time subject to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. The Company routinely assesses its current litigation and/or threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss in situations where the Company assesses the likelihood of loss as probable. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on the Company's condensed consolidated financial statements.

**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 unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and the audited condensed 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 SEC, on March 10, 2014. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. 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. 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 discussed in the section titled Risk Factors, set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this Report. The forward-looking statements in this Quarterly Report on Form 10-Q represent our views as of the date of this Quarterly Report on Form 10-Q. We anticipate that subsequent events and developments will cause our views to change. However, while we may elect to update these forward-looking statements at some point in the future, we have no current intention of doing so except to the extent required by applicable law. You should, therefore, not rely on these forward-looking statements as representing our views as of any date subsequent to the date of this Quarterly Report on Form 10-Q.*

## **Overview**

LogMeIn provides a portfolio of secure, easy-to-use cloud-based offerings aimed at transforming the way people work and live through secure connections to the computers, devices, data and people that make up their digital world. We believe our cloud-based services, which are deployed and accessed from anywhere with an Internet connection, are used to connect more Internet-enabled devices worldwide than any other connectivity platform on the market. Our solutions are used by tens of millions of professionals to work from virtually anywhere on virtually any Internet-enabled device. Hundreds of thousands of small and medium businesses, or SMBs, use our solutions to manage distributed work environments, embrace employee-owned technology in the workplace and facilitate collaboration across distributed teams. Thousands of service providers, including many of the world's largest hardware and software companies, web hosting providers, retailers and telecommunications providers, use our solutions to service and support their customers across mobile, social and online channels.

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We offer both free and fee based, or premium, services. Sales of our premium services are generated through word-of-mouth referrals, web-based advertising, online search, the conversion of free users and expiring free trials to paid subscriptions and direct marketing to new and existing customers.

We derive our revenue principally from subscription fees from SMBs, IT service providers, mobile carriers, customer service centers, original equipment manufacturers, or OEMs, and consumers and to a lesser extent, from the delivery of professional services primarily related to our Xively business. The majority of our customers subscribe to our services on an annual basis. Our revenue is driven primarily by the number and type of our premium services for which our paying customers subscribe. For the six months ended June 30, 2013, we generated revenues of \$78.1 million, compared to \$104.0 million for the six months ended June 30, 2014, an increase of approximately 33%. In the fiscal year 2013, we generated revenues of \$166.3 million.

## **Certain Trends and Uncertainties**

The following represents a summary of certain trends and uncertainties, which could have a significant impact on our financial condition and results of operations. This summary is not intended to be a complete list of potential trends and uncertainties that could impact our business in the long or short term. The summary, however, should be considered along with the factors identified in the section titled **Risk Factors** of this Quarterly Report on Form 10-Q and elsewhere in this report.

There is frequent litigation in the software and technology industries based on allegations of infringement or other violations of intellectual property rights. We have been, and may in the future be, subject to third party patent infringement or other intellectual property-related lawsuits as we face increasing competition and become increasingly visible. Any adverse determination related to intellectual property claims or litigation could adversely affect our business, financial condition and operating results.

The risk of a data security breach or service disruption caused by computer hackers and cyber criminals has increased as the frequency, intensity and sophistication of attempted attacks and intrusions from around the world have increased. Our services and systems have been, and may in the future be, the target of various forms of cyber-attacks. While we make significant efforts to maintain the security and integrity of our services and computer systems, our cybersecurity measures and the cybersecurity measures taken by our third-party data center facilities may be unable to anticipate, detect or prevent all attempts to compromise our systems. Any security breach, whether successful or not, could harm our reputation, subject us to lawsuits and other potential liabilities and ultimately could result in the loss of customers.

We continue to closely monitor current adverse economic conditions, particularly as they impact SMBs, IT service providers and consumers. We are unable to predict the likely duration and severity of the current adverse economic conditions in the United States and other countries, but the longer the duration the greater risks we face in operating our business.

We believe that competition will continue to increase. Increased competition could result from existing competitors or new competitors that enter the market because of the potential opportunity. We will continue to closely monitor competitive activity and respond accordingly. Increased competition could have an adverse effect on our financial condition and results of operations.

We believe that as we continue to grow revenue at expected rates, our cost of revenue and operating expenses, including sales and marketing, research and development and general and administrative expenses will increase in absolute dollar amounts. For a description of the general trends we anticipate in various expense categories, see [Cost of Revenue and Operating Expenses](#) below.

### **Sources of Revenue**

We derive our revenue primarily from subscription fees for our premium services from SMBs, IT service providers, mobile carriers, customer service centers, original equipment manufacturers, or OEMs, and consumers and to a lesser extent, from the delivery of professional services primarily related to our Xively business. The majority of our customers subscribe to our services on an annual basis and pay in advance, typically with a credit card, for their subscription. A smaller percentage of our customers subscribe to our services on a monthly basis through either month-to-month commitments or annual commitments that are then paid monthly with a credit card. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period. Typically, a subscription automatically renews at the end of a subscription period unless the customer specifically terminates it prior to the end of the period.

## **Employees**

We have increased our number of full-time employees to 748 at June 30, 2014 as compared to 613 at December 31, 2013 and 589 at June 30, 2013.

## **Cost of Revenue and Operating Expenses**

We allocate certain overhead expenses, such as rent and utilities, to expense categories based on the headcount in or office space occupied by personnel in that expense category as a percentage of our total headcount or office space. As a result, an overhead allocation associated with these costs is reflected in the cost of revenue and each operating expense category.

*Cost of Revenue.* Cost of revenue consists primarily of costs associated with our data center operations, customer support centers and our Xively professional services team. Included in these costs are: wages and benefits for personnel, telecommunication and hosting fees associated with managing our data centers and the hosting of our services, contingent bonus expense related to the Ionia acquisition (see Note 4 to the Condensed Consolidated Financial Statements), hardware and software maintenance costs and depreciation. Additionally, amortization expense associated with the acquired software, technology and documented

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know-how, as well as internally developed software is included in cost of revenue. The expenses related to hosting our services and supporting our free and premium customers are related to the number of customers who subscribe to our services and the complexity and redundancy of our services and hosting infrastructure. The expenses related to our professional services team are driven by our investment and efforts to support the growth of our Xively business. We expect cost of revenue expenses to increase in absolute dollars but remain relatively constant as a percentage of revenue as we continue to invest in and expand our professional services team to support the growth of our Xively business and we continue to increase our number of customers over time.

*Research and Development.* Research and development expenses consist primarily of wages and benefits for development personnel, professional fees associated with outsourced development projects and depreciation associated with assets used in development. We have focused our research and development efforts on both improving ease of use and functionality of our existing services, as well as developing new offerings. The majority of our research and development employees are located in our development centers in Europe. Therefore, a majority of research and development expense is subject to fluctuations in foreign exchange rates. We capitalized approximately \$0.6 million and \$0.9 million for the six months ended June 30, 2013 and 2014, respectively, of costs related to internally developed computer software to be sold as a service, which was incurred during the application development stage. The majority of research and development costs have been expensed as incurred. We expect that research and development expenses will increase in absolute dollars as we continue to enhance and expand our services but will remain relatively constant as a percentage of revenue.

*Sales and Marketing.* Sales and marketing expenses consist primarily of online search and advertising costs, wages, commissions and benefits for sales and marketing personnel, offline marketing costs such as media advertising and trade shows, professional fees and credit card processing fees. Online search and advertising costs consist primarily of pay-per-click payments to search engines and other online advertising media such as banner ads. Offline marketing costs include radio and print advertisements as well as the costs to create and produce these advertisements, and tradeshows, including the costs of space at tradeshows and costs to design and construct tradeshow booths. Advertising costs are expensed as incurred. In order to continue to grow our business and awareness of our services, we expect that we will continue to commit resources to our sales and marketing efforts. We expect that sales and marketing expenses will increase in absolute dollars but remain relatively constant as a percentage of revenue.

*General and Administrative.* General and administrative expenses consist primarily of wages and benefits for management, human resources, internal IT support, legal, finance and accounting personnel, professional fees, insurance and other corporate expenses. We expect general and administrative expenses related to personnel, recruiting, internal information systems, audit, accounting and insurance costs will increase in absolute dollars but remain relatively constant as a percentage of revenue as we continue to support the growth of our business. Assuming that there are no adverse changes in the status of the 01 Communique litigation (see Note 10 to the Condensed Consolidated Financial Statements), we expect associated legal costs, which are included in general and administrative expenses, to remain relatively constant.

**Critical Accounting Policies**

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, or GAAP. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates under different assumptions and conditions. Our most critical accounting policies are listed below:

Revenue recognition;

Income taxes;

Goodwill and acquired intangible assets;

Stock-based compensation; and

Loss contingencies.

**Table of Contents****Results of Consolidated Operations**

The following table sets forth selected consolidated statements of operations data for each of the periods indicated as a percentage of total revenue.

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
Revenue	100%	100%	100%	100%
Cost of revenue	12	13	12	13
<b>Gross profit</b>	<b>88</b>	<b>87</b>	<b>88</b>	<b>87</b>
Operating expenses:				
Research and development	17	15	18	14
Sales and marketing	55	56	55	57
General and administrative	16	14	23	14
Legal settlements			1	
Amortization of acquired intangibles				
<b>Total operating expenses</b>	<b>88</b>	<b>85</b>	<b>97</b>	<b>85</b>
<b>(Loss) income from operations</b>		<b>2</b>	<b>(9)</b>	<b>2</b>
Interest and other expense, net			1	
<b>(Loss) income before for income taxes</b>		<b>2</b>	<b>(8)</b>	<b>2</b>
(Provision for) benefit from income taxes	(3)		(1)	
<b>Net (loss) income</b>	<b>(3)%</b>	<b>2%</b>	<b>(9)%</b>	<b>2%</b>

**Three Months Ended June 30, 2013 and 2014**

*Revenue.* Revenue increased \$14.3 million, or 35%, from \$40.7 million for the three months ended June 30, 2013 to \$55.0 million for the three months ended June 30, 2014. The majority of the increase was attributable to an increase in revenue from new customers, as our total number of subscribers increased significantly during the period. The increase in revenue from new customers and in our total number of subscribers was attributable to continued increased sales of join.me pro, our premium collaboration service, and our strategic decision to discontinue offering LogMeIn Free, our free remote access service, to instead focus our marketing spend and efforts on our faster growing free services, specifically join.me. As a result of this change, we experienced significant growth in total sales and total subscribers as former LogMeIn Free users transitioned to either our premium remote access service, LogMeIn Pro, or our premium IT management product, LogMeIn Central. We believe that the majority of LogMeIn Free users that will convert to LogMeIn Pro or LogMeIn Central subscribers converted during the three months ended March 31, 2014.



*Cost of Revenue.* Cost of revenue increased \$2.6 million, or 55%, from \$4.8 million for the three months ended June 30, 2013 to \$7.4 million for the three months ended June 30, 2014. As a percentage of revenue, cost of revenue was 12% and 13% for the three months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily a result of a \$0.8 million increase in contingent retention-based bonuses incurred in connection with the Ionia acquisition (see Note 4 to the Condensed Consolidated Financial Statements), and a \$0.7 million increase in amortization expense of intangible assets primarily related to a software asset purchased in November 2013. The increase was also due to a \$0.5 million increase in personnel-related costs associated with the hiring of additional customer support employees to support our overall growth and the retention of the professional services employees from the Ionia acquisition, a \$0.3 million increase in hosting costs associated with managing our data centers and hosting of our services as a result of an increase in both the number of customers using our services and the total number of devices that connected to our services and a \$0.3 million increase in external professional fees.

*Research and Development Expenses.* Research and development expenses increased \$1.1 million, or 15%, from \$6.9 million for the three months ended June 30, 2013 to \$8.0 million for the three months ended June 30, 2014. As a percentage of revenue, research and development expenses were 17% and 15% for the three months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$1.1 million increase in personnel-related costs, a \$0.2 million increase in hardware and software maintenance costs, a \$0.1 million increase in travel-related costs, a \$0.1 million increase in employee training expenses, and a \$0.1 million increase in rent expense. These were offset by a \$0.5 million decrease in contingent bonus expense related to the Xively and Bold acquisitions, which were accrued for and paid prior to the three months ended June 30, 2014.

*Sales and Marketing Expenses.* Sales and marketing expenses increased \$8.5 million, or 38%, from \$22.6 million for the three months ended June 30, 2013 to \$31.1 million for the three months ended June 30, 2014. As a percentage of revenue, sales and marketing expenses were 55% and 56% for the three months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$3.5 million increase in marketing program costs and a \$3.4 million increase in personnel-related and recruiting costs, including salary, wages, commissions, bonus and benefits and tax expense costs, from the hiring of additional employees to support our growth in sales and expand our marketing efforts. The total increase in sales and marketing expense was also due to a \$0.6 million increase in external professional fees, a \$0.5 million increase in credit card transaction fees primarily related to an increase in e-commerce orders, a \$0.2 million increase in travel-related costs, a \$0.1 million increase in rent expense, a \$0.1 million increase in hardware and software maintenance costs, and a \$0.1 million increase in depreciation expense. Included in the personnel-related and recruiting costs is a \$0.6 million increase in stock compensation expense.

*General and Administrative Expenses.* General and administrative expenses increased \$1.1 million, or 17%, from \$6.4 million for the three months ended June 30, 2013 to \$7.4 million for the three months ended June 30, 2014. As a percentage of revenue, general and administrative expenses were 16% and 14% for the three months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$1.3 million increase in personnel-related and recruiting costs, including salary, wages, bonus and benefits and tax expense, as we increased the number of general and administrative employees to support our overall growth as well as a \$0.3 million increase in legal fees associated with general corporate-related matters. Included in the increase in personnel-related and recruiting costs is a \$0.9 million increase in stock-based compensation expense. These costs were offset by a \$0.4 million decrease in legal fees associated with the current status of the 01 Communique litigation as well as a \$0.1 million decrease in acquisition-related legal fees.

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*Amortization of Intangibles.* Amortization of intangibles was \$0.2 million and \$0.3 million for the three months ended June 30, 2013 and 2014, respectively. The increase in amortization of intangibles for the three months ended June 30, 2014 is related to the intangible assets acquired in the Ionia acquisition in March 2014.

*Interest and Other Income, (Expense) Net.* Interest and other income, (expense) net was expense of approximately \$43,000 and income of \$0.4 million for the three months ended June 30, 2013 and 2014, respectively. The increase was primarily related to a \$0.4 million increase in foreign currency gains.

*Income Taxes.* We recorded a provision for federal, state and foreign income taxes of approximately \$1.2 million and a benefit of \$0.2 million for the three months ended June 30, 2013 and 2014, respectively. We recorded a benefit as a result of a loss before income taxes incurred by the Company in the United States which offset profits generated in certain foreign jurisdictions, primarily our Irish subsidiaries, which are subject to significantly lower tax rates than the U.S. statutory rate. At each balance sheet date, we assess the likelihood that deferred tax assets will be realized, and recognize a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2013 and June 30, 2014, we maintained a full valuation allowance related to the deferred tax assets of our Hungarian subsidiary. This entity has historical losses and we concluded it was not more likely than not that these deferred tax assets are realizable.

*Net (Loss) Income.* We recognized a net loss of \$1.4 million for the three months ended June 30, 2013 compared to net income of \$1.3 million for the three months ended June 30, 2014.

For the three months ended June 30, 2014, revenue increased \$14.3 million while cost of revenue increased \$2.6 million, operating expenses increased \$10.8 million, other income increased \$0.4 million, and our tax provision decreased \$1.4 million, resulting in approximately a \$2.7 million increase in net income.

The \$14.3 million increase in revenue is primarily due to an increase in revenue from new customers and add-on revenues from our existing customer base. For the three months ended June 30, 2014, we experienced significant growth in total sales and total subscribers attributable to continued increased sales of join.me pro, our premium collaboration service, and our strategic decision to discontinue offering LogMeIn Free, our free remote access service, which caused former LogMeIn Free users to transition to either our premium remote access service, LogMeIn Pro, or our premium IT management product, LogMeIn Central.

The \$2.6 million increase in cost of revenue is primarily due to a \$0.8 million increase in contingent bonus expense, related to the Ionia acquisition, a \$0.7 million increase in amortization expense, primarily related to a software asset purchased in November 2013, a \$0.4 million increase in personnel-related costs, including salary, wages, bonus, benefits and tax expense primarily related to the Ionia acquisition, a \$0.3 million increase in costs to manage our data centers and the hosting of our services and a \$0.3 million increase in external professional fees.

The \$10.8 million increase in operating expenses is primarily due to a \$5.2 million increase in personnel-related costs, including a \$1.5 million increase in stock-based compensation, a \$3.5 million increase in marketing programs, a \$0.6 million increase in external professional fees, a \$0.5 million increase in credit card transaction fees, a \$0.3 million increase in travel-related costs, a \$0.3 million increase in hardware and software maintenance costs, a \$0.3 million increase in legal fees associated with general corporate-related matters, a \$0.2 million increase in rent expense, a \$0.1 million increase in depreciation and a \$0.1 million increase in amortization expense related to the Ionia acquisition. These costs were offset by a \$0.4 million decrease in legal fees due to the current status of the 01 Communique litigation.

The \$1.4 million decrease in our tax provision is primarily due to losses before taxes incurred in the United States which offset increased profitability in certain foreign jurisdictions, primarily our Irish subsidiaries, which are subject to significantly lower tax rates than the U.S. statutory rate.

#### **Six Months Ended June 30, 2013 and 2014**

*Revenue.* Revenue increased \$25.9 million, or 33%, from \$78.1 million for the six months ended June 30, 2013 to \$104.0 million for the six months ended June 30, 2014. The majority of the increase was attributable to an increase in revenue from new customers, as our total number of subscribers increased significantly during the period. The increase in revenue from new customers and in our total number of subscribers was attributable to continued increased sales of join.me pro, our premium collaboration service, and our strategic decision to discontinue offering LogMeIn Free, our free remote access service, to instead focus our marketing spend and efforts on our faster growing free services, specifically join.me. As a result of this change, we experienced significant growth in total sales and total subscribers as former LogMeIn Free users transitioned to either our premium remote access service, LogMeIn Pro, or our premium IT management product, LogMeIn Central. We believe that the majority of LogMeIn Free users that will convert to LogMeIn Pro or LogMeIn Central subscribers converted during the three months ended March 31, 2014.

*Cost of Revenue.* Cost of revenue increased \$4.3 million, or 47%, from \$9.2 million for the six months ended June 30, 2013 to \$13.5 million for the six months ended June 30, 2014. As a percentage of revenue, cost of revenue was 12% and 13% for the six months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$1.1 million increase in amortization expense related to a software asset purchased in November 2013, as well as a \$1.0 million increase in hosting costs associated with managing our data centers and hosting our services as a result of an increase in both the number of customers using our services and the total number of devices that connected to our services.

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The increase was also due to a \$0.9 million increase in contingent retention-based bonuses incurred in connection with the Ionia acquisition (see Note 4 to the Condensed Consolidated Financial Statements), a \$0.7 million increase in personnel-related costs, including salary, wages, bonus and benefits and tax, recruiting and relocation expense, as we increased the number of customer support employees to support our overall growth and retained professional services employees from the Ionia acquisition, a \$0.4 million increase in external professional fees, a \$0.1 million increase in rent expense and a \$0.1 million increase in hardware and software maintenance costs. Included in the increase in personnel-related costs is a \$0.1 million increase in stock-based compensation expense.

*Research and Development Expenses.* Research and development expenses increased \$0.4 million, or 3%, from \$14.3 million for the six months ended June 30, 2013 to \$14.7 million for the six months ended June 30, 2014. As a percentage of revenue, research and development expenses were 18% and 14% for the six months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$1.3 million increase in personnel-related costs, including salary, wages, bonus and benefits and tax, recruiting and relocation expense, a \$0.2 million increase in travel-related costs, a \$0.2 million increase in hardware and software maintenance costs, a \$0.1 million increase in rent expense and a \$0.1 million increase in employee training expense. These costs were offset by a \$0.9 million decrease in contingent bonus expense related to the Xively and Bold acquisitions, which were accrued for and paid in their entirety prior to February 2014, a \$0.3 million increase in costs related to internally developed computer software to be sold as a service which was incurred during the application development stage and therefore capitalized rather than expensed, as well as a \$0.3 million decrease in stock-based compensation expense.

*Sales and Marketing Expenses.* Sales and marketing expenses increased \$15.6 million, or 36%, from \$43.1 million for the six months ended June 30, 2013 to \$58.8 million for the six months ended June 30, 2014. As a percentage of revenue, sales and marketing expenses were 55% and 57% for the six months ended June 30, 2013 and 2014, respectively. The increase in absolute dollars was primarily due to a \$6.0 million increase in marketing program costs and a \$5.6 million increase in personnel-related costs, including salary, wages, commissions, recruiting and relocation, bonus and benefits and tax expense costs, from the hiring of additional employees to support our growth in sales and expand our marketing efforts. The total increase in sales and marketing expense was also due to a \$1.4 million increase in credit card transaction fees primarily related to an increase in e-commerce orders, a \$0.8 million increase in external professional fees, a \$0.5 million increase in rent expense, a \$0.4 million increase in travel-related costs, a \$0.3 million increase in hardware and software maintenance costs, a \$0.2 million increase in telecom expense, a \$0.2 million increase in depreciation expense and a \$0.1 million increase in employee training expense.

*General and Administrative Expenses.* General and administrative expenses decreased \$3.7 million, or 21%, from \$17.9 million for the six months ended June 30, 2013 to \$14.1 million for the six months ended June 30, 2014. As a percentage of revenue, general and administrative expenses were 23% and 14% for the six months ended June 30, 2013 and 2014, respectively. The decrease in absolute dollars was primarily due to a \$5.2 million decrease in legal fees associated with the current status of the 01 Communique litigation and the \$1.2 million expense associated with the Pragmatius License Agreement in April 2013. These were offset by a \$1.8 million increase in personnel-related and recruiting costs, including salary, wages, bonus and benefits and tax expense, as we increased the number of general and administrative employees to support our overall growth, a \$0.3 million increase in legal fees associated with general corporate-related matters, a \$0.1 million increase in external professional fees, a \$0.1 million increase in rent expense, a \$0.1 million increase in audit and tax fees, a \$0.1 million increase in hardware and software maintenance costs and \$0.1 million increase in travel and employee training expense. Included in the increase in personnel-related and recruiting costs is a \$1.4 million increase in stock-based compensation expense.

*Amortization of Intangibles.* Amortization of intangibles was \$0.4 million and \$0.5 million for the six months ended June 30, 2013 and 2014, respectively. The increase in amortization of intangibles for the six months ended June 30, 2014 is primarily related to intangible assets acquired in the Ionia acquisition in March 2014.

*Interest and Other Income, (Expense) Net.* Interest and other income, (expense) net was income of approximately \$0.8 million and \$0.5 million for the six months ended June 30, 2013 and 2014, respectively. The decrease was primarily related to a \$0.3 million decrease in foreign currency gains.

*Income Taxes.* We recorded a provision for federal, state and foreign income taxes of approximately \$1.2 million for the six months ended June 30, 2013, on a loss before income taxes of \$5.9 million. We recorded a provision as a result of income generated in the United States for which federal and state taxes were recorded. In addition, we incurred losses in certain foreign jurisdictions where there was no corresponding benefit. We recorded a provision for federal, state, and foreign income taxes of approximately \$0.5 million for the six months ended June 30, 2014 on income before taxes of \$2.8 million resulting in an effective tax rate of approximately 18%. Our effective tax rate is lower than the U.S. federal statutory rate of 35% primarily due to losses before taxes incurred in the United States as well as by earnings in certain foreign jurisdictions, primarily our Irish subsidiaries, which are subject to significantly lower tax rates than the U.S. statutory rate. At each balance sheet date, we assess the likelihood that deferred tax assets will be realized, and recognize a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. This assessment requires judgment as to the likelihood and amounts of future taxable income by tax jurisdiction. As of December 31, 2013 and June 30, 2014, we maintained a full valuation allowance related to the deferred tax assets of our Hungarian subsidiary. This entity has historical losses and we concluded it was not more likely than not that these deferred tax assets are realizable.

*Net (Loss) Income.* We recognized a net loss of \$7.2 million for the six months ended June 30, 2013 compared to net income of \$2.3 million for the six months ended June 30, 2014.

For the six months ended June 30, 2014, revenue increased \$25.9 million while cost of revenue increased \$4.3 million, operating expenses increased \$12.4 million, other income decreased \$0.3 million, and our tax provision decreased \$0.7 million, resulting in approximately a \$9.5 million increase in net income.

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The \$25.9 million increase in revenue is primarily due to an increase in revenue from new customers and add-on revenues from our existing customer base. For the six months ended June 30, 2014, we experienced significant growth in total sales and total subscribers attributable to continued increased sales of join.me pro, our premium collaboration service, and our strategic decision to discontinue offering LogMeIn Free, our free remote access service, which caused former LogMeIn Free users to transition to either our premium remote access service, LogMeIn Pro, or our premium IT management product, LogMeIn Central.

The \$4.3 million increase in cost of revenue is primarily due to a \$1.1 million increase in amortization expense related to a software asset purchased in November 2013, a \$1.0 million increase in costs to manage our data centers and the hosting of our services, a \$0.9 million increase in contingent bonus payments related to the Ionia acquisition and a \$0.7 million increase in personnel-related costs, including salary, wages, bonus, benefits and tax expense primarily related to the Ionia acquisition. Additionally, increases in cost of revenue were related to a \$0.4 million increase in external professional fees, a \$0.1 million increase in rent expense and a \$0.1 million increase in hardware and software maintenance costs.

The \$12.2 million increase in operating expenses is primarily due to a \$7.2 million increase in personnel-related costs, including a \$1.7 million increase in stock-based compensation, a \$6.0 million increase in marketing programs, a \$1.4 million increase in credit card transaction fees, a \$0.9 million increase in external professional fees, a \$0.7 million increase in rent expense, a \$0.7 million increase in travel-related costs, a \$0.6 million increase in hardware and software maintenance costs, a \$0.3 million increase in employee training expense, \$0.3 million legal fees associated with general corporate-related matters, a \$0.2 million increase in telecom related costs associated with the increase in personnel, a \$0.2 million increase in depreciation expense, a \$0.2 million increase in amortization expense primarily related to the intangible assets acquired in the Ionia acquisition in March 2014 and a \$0.1 million increase in accounting and tax fees. These were offset by a \$5.2 million decrease in litigation-related fees and a \$1.2 million expense associated with the Pragmatius License Agreement in April 2013.

The \$0.7 million decrease in our tax provision is primarily due to losses before taxes incurred in the United States which offset increased profitability in certain foreign jurisdictions, primarily our Irish subsidiaries, which are subject to significantly lower tax rates than the U.S. statutory rate.

**Liquidity and Capital Resources**

The following table sets forth the major sources and uses of cash for each of the periods set forth below (in thousands):

	<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2014</b>
Net cash provided by operations	\$ 12,911	\$ 45,402
Net cash used in investing activities	(7,627)	(13,288)
Net cash used in financing activities	(15,255)	(200)
Effect of exchange rate changes	(883)	(343)
Net (decrease) increase in cash	\$ (10,854)	\$ 31,571

At June 30, 2014, our principal source of liquidity was cash and cash equivalents and short-term marketable securities totaling \$221.0 million.

***Cash Flows From Operating Activities***

Net cash inflows from operating activities during the six months ended June 30, 2013 were primarily attributable to non-cash operating expenses, including \$10.3 million for stock compensation and \$3.6 million for depreciation and amortization. The net cash inflows from operating activities were also attributable to a \$8.1 million increase in deferred revenue associated with the increase in subscription sales orders and customer growth, a \$3.6 million decrease in accounts receivable and a \$0.4 million increase in accounts payable and accrued liabilities. These were offset by a \$3.4 million increase in prepaid expenses and other current assets, and a \$1.8 million increase in other assets. The increase in prepaid expenses and other current assets is associated with a \$4.3 million increase in prepaid taxes offset by a \$0.4 million decrease in prepaid rent for our Boston office and a \$0.4 million decrease in other prepaid expenses. The increase in other assets is attributable to a \$1.8 million increase in long-term prepaid rent for our Boston office.



Net cash inflows from operating activities during the six months ended June 30, 2014 were attributable to a \$23.4 million increase in deferred revenue associated with upfront payments primarily received from our customers. The increase in net cash inflows from operating activities was also attributable to a \$2.6 million decrease in accounts receivable, a \$0.7 million increase in other long-term liabilities and a \$0.4 million increase in accounts payable. These were offset by a \$1.3 million decrease in accrued liabilities and a \$1.0 million increase in prepaid expenses and other current assets. Included in the increase in other long-term liabilities is a \$0.3 million increase in accrued rent related to the expansion of the leased space and extension of the term of the lease for our Budapest, Hungary office space, a \$0.2 million increase in contingent bonus payments associated with the Ionia acquisition as well as a \$0.2 million increase in uncertain tax positions. The decrease in accrued liabilities is primarily due to a \$2.7 million decrease in accrued bonuses related to the payment of fiscal 2013 management plan bonuses in January 2014, offset by a \$1.0 million increase in accrued marketing spend and a \$0.4 million increase in accrued vacation. The \$1.0 million increase in prepaid expenses and other current assets is primarily related to the reclassification of a portion of the security deposit for our Boston, Massachusetts office space, which will be returned to us in April 2015 from long-term restricted cash to short-term restricted cash. Additionally, included in cash inflows from operating activities are add-backs of non-cash expense items, including \$12.2 million for stock compensation and \$5.5 million for depreciation and amortization. We expect that our future cash flows from operating activities will be impacted by the contingent payments associated with the Ionia acquisition.

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***Cash Flows From Investing Activities***

Net cash used in investing activities for the six months ended June 30, 2013 was primarily related to payments of \$6.5 million for property and equipment primarily related to the expansion and upgrade of our data center capacity, the expansion and upgrade of our internal IT infrastructure and the relocation of our corporate headquarters to Boston. Net cash used in investing activities also related to \$0.9 million in intangible asset additions related to internally developed software and the purchase of domain names and trademarks as well as the purchase of \$60.4 million of marketable securities offset by proceeds of \$60.0 million from redemption and maturity of marketable securities.

Net cash used in investing for the six months ended June 30, 2014 was primarily related to a \$7.4 million payment to acquire Ionia in March 2014 and \$4.3 million of payments to purchase property and equipment primarily related to the expansion and upgrade of our data center capacity, the expansion and upgrade of our internal IT infrastructure and expansion of our offices. Net cash used in investing activities also related to \$1.3 million in intangible asset additions related to internally developed software.

***Cash Flows From Financing Activities***

Net cash used in financing activities for the six months ended June 30, 2013 was primarily related to \$14.6 million for the purchase of treasury stock as well as \$0.9 million for payroll taxes paid related to vesting of restricted stock units, offset by \$0.3 million in proceeds received from the issuance of common stock upon exercise of stock options.

Net cash used in financing activities for the six months ended June 30, 2014 was primarily related to \$6.9 million for the purchase of treasury stock as well as \$3.6 million for payroll taxes paid related to vesting of restricted stock units, offset by \$10.3 million in proceeds received from the issuance of common stock upon exercise of stock options.

While we believe that our current cash and cash equivalents will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months, we may elect to raise additional capital through the sale of additional equity or debt securities or obtain a credit facility to develop or enhance our services, to fund expansion, to respond to competitive pressures or to acquire complementary products, businesses or technologies. If we elect, additional financing may not be available in amounts or on terms that are favorable to us, if at all. If we raise additional funds through the issuance of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock.

During the last three years, inflation and changing prices have not had a material effect on our business and we do not expect that inflation or changing prices will materially affect our business in the foreseeable future.

**Key Non-GAAP Financial Measures**

Regulation S-K Item 10(e), Use of Non-GAAP Financial Measures in Commission Filings, defines and prescribes the condition for use of non-GAAP financial information. We have presented the following non-GAAP measures in accordance with this standard. We believe that these non-GAAP measures of financial results provide useful information to management and investors regarding certain financial and business trends relating to our financial condition and results of operations. Management uses these non-GAAP measures to compare our performance to that of prior periods and uses these measures in financial reports prepared for management and our board of directors. We believe that the use of these non-GAAP financial measures provides an additional tool for investors to use in evaluating ongoing operating results and trends and in comparing our financial measures with other software-as-a-service companies, many of which present similar non-GAAP financial measures to investors.

In addition to our condensed consolidated financial statements prepared in accordance with GAAP, to date, we have considered the following non-GAAP financial measures to be key indicators of our financial performance:

Non-GAAP Operating Income, which we define as GAAP operating income less acquisition related costs and amortization, stock compensation expense, and patent litigation related expenses;

Adjusted EBITDA, which we define as GAAP income, less interest income and other expense (net), provision for income taxes, depreciation and amortization expenses, acquisition related costs, stock compensation expense, and patent litigation related expenses;

Non-GAAP Provision for income taxes, which we define as GAAP provision for income taxes less the tax impact from acquisition related costs amortization, stock compensation expense, patent litigation related expenses, and tax benefits associated with the reversal of a valuation allowance;

Non-GAAP Net income, which we define as Non-GAAP income before provision for income taxes less Non-GAAP provision for income taxes; and

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Non-GAAP Diluted net income per share, which we define as Non-GAAP net income divided by diluted average weighted shares outstanding.

The expenses described below have been excluded from our GAAP results to arrive at our non-GAAP measures, as outlined above:

*Acquisition related costs and amortization* relate to costs associated with acquisitions of intellectual property and businesses and include legal costs, contingent retention bonuses and the amortization of intangible assets.

*Acquisition related costs* relate to costs associated with the acquisitions of intellectual property and businesses and include legal costs and contingent retention bonuses.

*Stock compensation expense* relates to stock-based compensation awards granted to our executive officers, employees, and outside directors.

*Patent litigation related expenses* relate to costs associated with the defense and settlement of patent infringement claims brought against us (see Note 10 to the Condensed Consolidated Financial Statements).

*Tax benefits related to the reversal of a valuation allowance* relate to the reversal of a valuation allowance against certain foreign deferred tax assets (see Note 7 to the Condensed Consolidated Financial Statements).

*Depreciation and amortization expenses* relate to costs associated with the depreciation and amortization of fixed and intangible assets.

*Interest income and other expense (income), net* relates to the interest earned on outstanding cash balances during the period as well as foreign currency, realized and unrealized, gains and losses as a result of multi-currency settlements occurring during the period and period end translation adjustments.

*Income tax (benefit) expense* relates to the total income tax levied based on GAAP income during the period.

We consider our non-GAAP financial measures and these certain financial and operating metrics important to understanding our historical results, improving our business, benchmarking our performance against peer companies, and identifying current and future trends impacting our business.

The exclusion of certain expenses in the calculation of non-GAAP financial measures should not be construed as an inference that these costs are unusual or infrequent. We anticipate excluding these expenses in future presentations of our non-GAAP financial measures. We believe that these non-GAAP measures of financial results provide useful information to management and investors regarding certain financial and business trends related to our financial condition and results of operations.

We do not consider these non-GAAP measures in isolation or as an alternative to financial measures determined in accordance with GAAP. The principal limitation of these non-GAAP financial measures is that they exclude significant elements that are required to be recorded in our financial statements pursuant to GAAP. In addition, they are subject to inherent limitations as they reflect the exercise of judgments by management in determining these non-GAAP financial measures. In order to compensate for these limitations, management presents our non-GAAP financial measures in connection with our GAAP results. We urge investors to review the reconciliation of our non-GAAP financial measures to the comparable GAAP financial measures, which we have included in this Form 10-Q and in our press releases announcing our quarterly financial results, and not to rely on any single financial measure to evaluate our business.

Reconciliation tables of the most comparable GAAP financial measures to the non-GAAP measures are presented as follows (in thousands, except share and per share data):

<b>Non-GAAP Income from Operations</b>	<b>For the Three Months Ended</b>		<b>For the Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
GAAP (Loss) Income from Operations	\$ (123)	\$ 782	\$ (6,753)	\$ 2,380
Add Back:				
Stock-based compensation expense	5,117	6,713	10,282	12,151
Patent litigation related expenses	569	181	6,634	244
Acquisition related costs and amortization	1,141	2,012	2,211	3,152
Non-GAAP Operating Income	\$ 6,704	\$ 9,688	\$ 12,374	\$ 17,927

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	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
<b>Adjusted EBITDA</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
GAAP Net (Loss) Income	\$ (1,360)	\$ 1,330	\$ (7,167)	\$ 2,334
Add Back:				
Stock-based compensation expense	5,117	6,713	10,282	12,151
Patent litigation related expenses	569	181	6,634	244
Acquisition related costs	632	756	1,194	1,055
Interest income and other expense (income), net	43	(373)	(774)	(456)
Income tax (benefit) expense	1,194	(175)	1,188	502
Depreciation and Amortization expense	1,892	3,027	3,596	5,499
<b>Adjusted EBITDA</b>	<b>\$ 8,087</b>	<b>\$ 11,459</b>	<b>\$ 14,953</b>	<b>\$ 21,329</b>

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
<b>Non-GAAP Net Income</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
GAAP Net (Loss) Income	\$ (1,360)	\$ 1,330	\$ (7,167)	\$ 2,334
Add Back:				
Stock-based compensation expense	5,117	6,713	10,282	12,151
Patent litigation related expenses	569	181	6,634	244
Acquisition related costs and amortization	1,141	2,012	2,211	3,152
Less:				
Income Tax Effect of Non-GAAP items	(2,201)	(2,924)	(5,565)	(5,072)
<b>Non-GAAP Net Income</b>	<b>\$ 3,266</b>	<b>\$ 7,312</b>	<b>\$ 6,395</b>	<b>\$ 12,809</b>

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
<b>Non-GAAP earnings per share</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>
GAAP diluted (loss) earnings per share	\$ (0.05)	\$ 0.05	\$ (0.29)	\$ 0.09
Add Back:				
Stock-based compensation expense	0.21	0.27	0.41	0.49
Patent litigation related expenses	0.02	0.01	0.27	0.01
Acquisition related costs and amortization	0.04	0.08	0.09	0.13
Less:				
Income Tax Effect of Non-GAAP items	(0.09)	(0.12)	(0.22)	(0.21)
<b>Non-GAAP earnings per share</b>	<b>0.13</b>	<b>0.29</b>	<b>0.26</b>	<b>0.51</b>
	24,867,371	25,159,340	25,028,953	24,889,730

Shares used in computing diluted net income  
per share

**Off-Balance Sheet Arrangements**

We do not engage in any off-balance sheet financing activities, nor do we have any interest in entities referred to as variable interest entities.

**Table of Contents****Contractual Obligations**

The following table summarizes our contractual obligations at June 30, 2014 and the effect such obligations are expected to have on our liquidity and cash flow in future periods.

	<b>Payments Due by Period(in thousands)(1)</b>				
	<b>Total</b>	<b>Less Than 1 Year</b>	<b>1-3 Years</b>	<b>3-5 Years</b>	<b>More Than 5 Years</b>
Operating lease obligations	\$ 48,420	\$ 6,228	\$ 12,020	\$ 11,681	\$ 18,491
Hosting service agreements	3,052	2,949	103		
<b>Total</b>	<b>\$ 51,472</b>	<b>\$ 9,177</b>	<b>\$ 12,123</b>	<b>\$ 11,681</b>	<b>\$ 18,491</b>

(1) Excluded from the table above is \$484,000 related to uncertain tax positions as we are uncertain as to when a cash settlement for these liabilities will occur.

The commitments under our operating leases shown above consist primarily of lease payments for our corporate headquarters located in Boston, Massachusetts (see Note 10 to the Condensed Consolidated Financial Statements), our international sales and marketing offices located in Australia, the United Kingdom, Ireland, India and our research and development offices in Hungary as well as our contractual obligations related to our data centers.

In April 2014, we amended our current lease for our Budapest, Hungary office space to provide for an expansion of leased space and to extend the term of the lease. The term of the amended lease will begin in July 2014 and extend through June 2019. The aggregate amount of minimum lease payments to be made over the term of the lease is approximately \$7.8 million (EUR 5.7 million). The amended lease agreement required a bank guarantee of approximately \$483,000 (EUR 354,000). The bank guarantee is classified as restricted cash.

**Recent Accounting Pronouncements**

On May 28, 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers ( ASU 2014-09 ) its final standard on revenue from contracts with customers. ASU 2014-9 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the revenue model to contracts within its scope, an entity identifies the contract(s) with a customer, identifies the performance obligations in the contract, determines the transaction price, allocates the transaction price to the performance obligations in the contract and recognizes revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 applies to all contracts with customers that are within the scope of other topics in the FASB Accounting Standards Codification. Certain of ASU 2014-09's provisions also apply to transfers of nonfinancial assets, including in-substance nonfinancial assets that are not an output of an entity's ordinary activities (i.e., property plant and equipment; real estate; or intangible assets). Existing accounting guidance applicable to these transfers has been amended or superseded. ASU 2014-09 also requires significantly expanded disclosures about revenue recognition. ASU 2014-09 is effective for us on January 1, 2017. We are currently assessing the potential impact of the adoption of ASU 2014-09 on our condensed



consolidated financial statements.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

*Foreign Currency Exchange Risk* . Our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates as a result of the majority of our research and development expenditures being made from our Hungarian research and development facilities, and in our international sales and marketing offices in the United Kingdom, Australia, Ireland, Brazil and India. In the six months ended June 30, 2014, approximately 12%, 7%, 7%, 3%, 1%, of our operating expenses occurred in our operations in Hungary, Ireland, the United Kingdom, Australia, India, respectively, and less than 1% occurred in Brazil. In the six months ended June 30, 2013, approximately 12%, 7%, 3%, 2% of our operating expenses occurred in our operations in Hungary, the United Kingdom, Ireland, Australia, respectively, and less than 1% each in India and Brazil, respectively.

Additionally, an increasing percentage of our sales outside the United States are denominated in local currencies and, thus, also subject to fluctuations due to changes in foreign currency exchange rates. To date, changes in foreign currency exchange rates have not had a material impact on our operations, and a future change of 20% or less in foreign currency exchange rates would not materially affect our operations. At this time we do not, but may in the future, enter into any foreign currency hedging programs or instruments that would hedge or help offset such foreign currency exchange rate risk.

*Interest Rate Sensitivity*. Interest income is sensitive to changes in the general level of U.S. interest rates. However, based on the nature and current level of our cash and cash equivalents and short-term marketable securities, which are primarily consisted of cash, money market instruments, government securities and agency bonds, we believe there is no material risk of exposure to changes in the fair value of our cash and cash equivalents and marketable securities as a result of changes in interest rates.

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**Table of Contents****ITEM 4. CONTROLS AND PROCEDURES**

*Evaluation of Disclosure Controls and Procedures.* Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2014. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of June 30, 2014, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

*Changes in Internal Controls.* No changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the quarter ended June 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

On September 8, 2010, 01 Communique Laboratory, Inc., or 01, filed a complaint that named us as a defendant in a lawsuit in the U.S. District Court for the Eastern District of Virginia (Civil Action No. 1:10cv1007) alleging that we infringed U.S. Patent No. 6,928,479, or the 479 Patent, which is owned by 01 and has claims directed to a particular application or system for providing a private communication portal from one computer to a second computer. The complaint sought damages in an unspecified amount and injunctive relief. On April 1, 2011, the U.S. District Court for the Eastern District of Virginia granted our motion for summary judgment of non-infringement. The court issued a written order regarding this decision on May 4, 2011. On May 13, 2011, 01 filed a notice of appeal appealing the court's ruling granting summary judgment. On July 31, 2012, the U.S. Court of Appeals for the Federal Circuit vacated the lower court's summary judgment of non-infringement ruling and remanded the case back to the U.S. District Court for the Eastern District of Virginia with revised claim construction. The trial commenced on March 18, 2013 and on March 26, 2013, a jury in the Eastern District of Virginia found that our products do not infringe the 479 Patent as previously asserted by 01. The court issued a written order regarding this decision on April 2, 2013. On June 26, 2013, the court issued a written opinion denying all pending post-trial motions, thereby preserving the jury's non-infringement verdict. On June 26, 2013, 01 filed a notice of appeal seeking to appeal the jury's non-infringement verdict and on July 18, 2013, we filed a notice of cross appeal seeking to appeal the jury's decisions regarding invalidity and inequitable conduct. Oral arguments were heard on June 3, 2014 and on June 9, 2014, the U.S. Court of Appeals for the Federal Circuit affirmed the jury's non-infringement verdict.

We are from time to time subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these other claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on our consolidated financial statements.

## Item 1A. Risk Factors

*Our business is subject to numerous risks. We caution you that the following important factors, among others, could cause our actual results to differ materially from those expressed in forward-looking statements made by us or on our behalf in filings with the SEC, press releases, communications with investors and oral statements. Any or all of our forward-looking statements in this Quarterly Report on Form 10-Q and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. Many factors mentioned in the discussion below will be important in determining future results. Consequently, no forward-looking statement can be guaranteed. Actual future results may differ materially from those anticipated in forward-looking statements. We undertake no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosure we make in our reports filed with the SEC.*

### **RISKS RELATED TO OUR BUSINESS**

#### ***We may be unable to maintain profitability.***

We reported a net loss of \$7.7 million for fiscal 2013, primarily due to patent litigation related expenses. For the six months ended June 30, 2014, we reported net income of \$2.3 million. However, given our operating history, we cannot be certain that we will be able to maintain this profitability in the future. Our growth in revenue and customer base may not be sustainable, and we may not achieve sufficient revenue to achieve or maintain profitability. We may incur significant losses in the future for a number of reasons, including, but not limited to, unforeseen expenses, operating difficulties, complications and delays or due to the other risks described in this report. Accordingly, we may not be able to maintain our profitability, and we may incur significant losses for the foreseeable future.

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***Assertions by a third party that our services and solutions infringe its intellectual property, whether or not correct, could subject us to costly and time-consuming litigation or expensive licenses.***

There is frequent litigation in the software and technology industries based on allegations of infringement or other violations of intellectual property rights. We have been, and may in the future be, subject to third party patent infringement or other intellectual property-related lawsuits as we face increasing competition and become increasingly visible. Regardless of the merit of these claims, they can be time-consuming, result in costly litigation and diversion of technical and management personnel or require us to develop a non-infringing technology or enter into license agreements. There can be no assurance that such licenses will be available on acceptable terms and conditions, if at all, and although we have previously licensed proprietary technology, we cannot be certain that the owners' rights in such technology will not be challenged, invalidated or circumvented. For these reasons and because of the potential for court awards that are difficult to predict, it is not unusual to find even arguably unmeritorious claims settled for significant amounts. In addition, many of our service agreements require us to indemnify our customers from certain third-party intellectual property infringement claims, which could increase our costs as a result of defending such claims and may require that we pay damages if there were an adverse ruling related to any such claims. These types of claims could harm our relationships with our customers, deter future customers from subscribing to our services or expose us to further litigation. These costs, monetary or otherwise, associated with defending against third party allegations of infringement could have negative effects on our business, financial condition and operating results.

For additional information please refer to Part II, Item 1 entitled "Legal Proceedings" and Note 10 of the Condensed Consolidated Financial Statements.

***A reversal of the non-infringement verdict rendered in our patent infringement dispute with 01 Communique Laboratory, Inc. could have an adverse impact on our business, financial condition and operating results.***

We have been defending against a patent infringement claim brought against us by 01 Communique Laboratory, Inc., or 01, in the Eastern District of Virginia since September 2010. A jury in the Eastern District of Virginia has found that our products do not infringe U.S. Patent No 6,928,479 and on June 9, 2014, the U.S. Court of Appeals for the Federal Circuit affirmed the jury's non-infringement verdict. At this time, we do not believe that a loss is probable and we remain unable to reasonably estimate our potential liability, if any, in connection with this matter. However, any reversal of the non-infringement verdict or any continuation of this matter could have a material adverse effect on our business, financial condition and results of operations.

***If the security of our customers' confidential information stored in our systems is breached or otherwise subjected to unauthorized access, our reputation may be harmed, and we may be exposed to liability and a loss of customers.***

Our systems store our customers' confidential information, which may include credit card information, account and device information and other critical data. Any accidental or willful security breaches or other unauthorized access could expose us to liability for the loss of such information, time consuming and expensive litigation and other potential liabilities, as well as negative publicity. Many states have also enacted laws requiring companies to notify individuals of data security breaches involving their personal data. These mandatory disclosures regarding a security breach often lead to widespread negative publicity, which may cause our customers to lose confidence in the effectiveness of our data security measures.

Additionally, techniques used by computer hackers and cyber criminals to obtain unauthorized access or to sabotage systems change frequently and generally are difficult to recognize and react to. Our services and systems, including the systems of our outsourced service providers, have been and may in the future continue to be the target of various forms of cyber-attacks such as DNS attacks, wireless network attacks, viruses and worms, malicious software,

application centric attacks, peer-to-peer attacks, phishing attempts, backdoor trojans and distributed denial of service (DDoS) attacks. While we make significant efforts to maintain the security and integrity of our services and computer systems, our cybersecurity measures and the cybersecurity measures taken by our third-party data center facilities may be unable to anticipate, detect or prevent all attempts to compromise our systems. Any security breach, whether successful or not, could harm our reputation, subject us to lawsuits and other potential liabilities and ultimately could result in the loss of customers.

***If our services are used to commit fraud or other similar intentional or illegal acts, we may incur significant liabilities, our services may be perceived as not secure and customers may curtail or stop using our services.***

Certain services we provide enable direct remote access to third-party computer systems. We do not control the use or content of information accessed by our customers through our services. If our services are used to commit fraud or other bad or illegal acts, including, but not limited to, posting, distributing or transmitting any software or other computer files that contain a virus or other harmful component, interfering or disrupting third-party networks, infringing any third party's copyright, patent, trademark, trade secret or other proprietary rights or rights of publicity or privacy, transmitting any unlawful, harassing, libelous, abusive, threatening, vulgar or otherwise objectionable

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material, or accessing unauthorized third-party data, we may become subject to claims for defamation, negligence or intellectual property infringement and subject to other potential liabilities. As a result, defending such claims could be expensive and time-consuming, and we could incur significant liability to our customers and to individuals or businesses who were the targets of such acts. As a result, our business may suffer and our reputation may be damaged.

***We depend on search engines to attract a significant percentage of our customers, and if those search engines change their listings or increase their pricing, it would limit our ability to attract new customers.***

Many of our customers locate our website through search engines, such as Google. Search engines typically provide two types of search results, algorithmic and purchased listings, and we rely on both types. Algorithmic listings cannot be purchased and are determined and displayed solely by a set of formulas designed by the search engine. Search engines revise their algorithms from time to time in an attempt to optimize search result listings. If the search engines on which we rely for algorithmic listings modify their algorithms in a manner that reduces the prominence of our listing, fewer potential customers may click through to our website, requiring us to resort to other costly resources to replace this traffic. Any failure to replace this traffic could reduce our revenue and increase our costs. In addition, costs for purchased listings have increased in the past and may increase in the future, and further increases could have negative effects on our financial condition.

***If we are unable to attract new customers to our services on a cost-effective basis, our revenue and results of operations will be adversely affected.***

We must continue to attract a large number of customers on a cost-effective basis, many of whom have not previously used cloud-based, remote-connectivity solutions. We rely on a variety of marketing methods to attract new customers to our services, such as paying providers of online services and search engines for advertising space and priority placement of our website in response to Internet searches. Our ability to attract new customers also depends on the competitiveness of the pricing of our services. If our current marketing initiatives are not successful or become unavailable, if the cost of such initiatives were to significantly increase, or if our competitors offer similar services at lower prices, we may not be able to attract new customers on a cost-effective basis and, as a result, our revenue and results of operations would be adversely affected.

***If we are unable to retain our existing customers, our revenue and results of operations would be adversely affected.***

We sell our services pursuant to agreements that are generally one year in duration. Our customers have no obligation to renew their subscriptions after their subscription period expires, and these subscriptions may not be renewed on the same or on more profitable terms. As a result, our ability to grow depends in part on subscription renewals. We may not be able to accurately predict future trends in customer renewals, and our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, the prices of services offered by our competitors or reductions in our customers' spending levels. If our customers do not renew their subscriptions for our services, renew on less favorable terms, or do not purchase additional functionality or subscriptions, our revenue may grow more slowly than expected or decline, and our profitability and gross margins may be harmed.

***If we fail to convert our free users to paying customers, our revenue and financial results will be harmed.***

A significant portion of our user base utilizes our services free of charge through our free services or free trials of our premium services. We seek to convert these free and trial users to paying customers of our premium services. If our rate of conversion suffers for any reason, our revenue may decline and our business may suffer.

***If our efforts to build a strong brand identity are not successful, we may not be able to attract or retain subscribers and our operating results may be adversely affected.***

We believe that building and maintaining a strong brand identity plays an important role in attracting and retaining subscribers to our services, who may have other options from which to obtain their remote connectivity services. In order to build a strong brand, we believe that we must continue to offer innovative remote connectivity services that our subscribers value and enjoy using, and also market and promote those services through effective marketing campaigns, promotions and communications with our user base. From time-to-time, subscribers may express dissatisfaction with our services or react negatively to our strategic business decisions, such as changes that we make in pricing, features or service offerings, including the discontinuance of our free services. To the extent that user dissatisfaction with our services or strategic business decisions is widespread or not adequately addressed, our overall brand identity may suffer and as a result our ability to attract and retain subscribers may be adversely affected, which could adversely affect our operating results.

***Our business strategy includes acquiring or investing in other companies, which may divert our management's attention, result in additional dilution to our stockholders and consume resources that are necessary to sustain our business.***

Our business strategy includes acquiring complementary services, technologies or businesses. We also may enter into relationships with other businesses to expand our portfolio of services or our ability to provide our services in foreign jurisdictions, which could involve preferred or exclusive licenses, additional channels of distribution, discount pricing or investments in other companies. Negotiating these transactions can be time-consuming, difficult and expensive, and our ability to close these transactions may often be subject to conditions or approvals that are beyond our control. Consequently, these transactions, even if undertaken and announced, may not close.

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An acquisition, investment or new business relationship may result in unforeseen operating difficulties and expenditures. In particular, we may encounter difficulties assimilating or integrating the businesses, technologies, products, personnel or operations of the acquired companies, particularly if the key personnel of the acquired company choose not to work for us, the company's software is not easily adapted to work with ours or we have difficulty retaining the customers of any acquired business due to changes in management or otherwise. Acquisitions may also disrupt our business, divert our resources and require significant management attention that would otherwise be available for development of our business. Moreover, the anticipated benefits of any acquisition, investment or business relationship may not be realized or we may be exposed to unknown liabilities. For one or more of those transactions, we may:

issue additional equity securities that would dilute our stockholders;

use cash that we may need in the future to operate our business;

incur debt on terms unfavorable to us or that we are unable to repay;

incur large charges or substantial liabilities;

encounter difficulties retaining key employees of the acquired company or integrating diverse software codes or business cultures; and

become subject to adverse tax consequences, substantial depreciation or deferred compensation charges.

Any of these risks could harm our business and operating results.

***We expect that integrating an acquired company's operations may present challenges.***

The integration of an acquired company requires, among other things, coordination of administrative, sales and marketing, accounting and finance functions and expansion of information and management systems. Integration may prove to be difficult initially due to the necessity of coordinating geographically separate organizations and integrating personnel with disparate business backgrounds and corporate cultures. We may not be able to retain key employees of an acquired company. Additionally, the process of integrating a new product or service may require a disproportionate amount of time and attention of our management and financial and other resources. Any difficulties or problems encountered in the integration of a new product or service could have a material adverse effect on our business.

The integration of an acquired company may cost more than we anticipate, and it is possible that we will incur significant additional unforeseen costs in connection with the integration that may negatively impact our earnings.

In addition, we may only be able to conduct limited due diligence on an acquired company's operations. Following an acquisition, we may be subject to unforeseen liabilities arising from an acquired company's past or present operations. These liabilities may be greater than the warranty and indemnity limitations we negotiate. Any unforeseen liability



that is greater than these warranty and indemnity limitations could have a negative impact on our financial condition.

Even if successfully integrated, there can be no assurance that our operating performance after an acquisition will be successful or will fulfill management's objectives.

***We use a limited number of data centers to deliver our services. Any disruption of service at these facilities could harm our business.***

We host our services and serve all of our customers from seven third-party data center facilities located throughout the world. We do not control the operation of these facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, we may be required to transfer to new data center facilities, and we may incur significant costs and possible service interruption in connection with doing so.

Any changes in third-party service levels at our data centers or any errors, defects, disruptions or other performance problems with our services could harm our reputation and may damage our customers' businesses. Interruptions in our services might reduce our revenue, cause us to issue credits to customers, subject us to potential liability, cause customers to terminate their subscriptions or harm our renewal rates.

Our data centers are vulnerable to damage or interruption from human error, intentional bad acts, pandemics, earthquakes, hurricanes, floods, fires, war, terrorist attacks, power losses, hardware failures, systems failures, telecommunications failures and similar events. At least one of our data facilities is located in an area known for seismic activity, increasing our susceptibility to the risk that an earthquake could significantly harm the operations of these facilities. The occurrence of a natural disaster or an act of terrorism, or vandalism or other misconduct, a decision to close the facilities without adequate notice or other unanticipated problems could result in lengthy interruptions in our services.

***Failure to comply with data protection standards may cause us to lose the ability to offer our customers a credit card payment option which would increase our costs of processing customer orders and make our services less attractive to our customers, the majority of which purchase our services with a credit card.***

Major credit card issuers have adopted data protection standards and have incorporated these standards into their contracts with us. If we fail to maintain our compliance with the data protection and documentation standards adopted by the major credit card issuers and applicable to

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us, these issuers could terminate their agreements with us, and we could lose our ability to offer our customers a credit card payment option. Most of our individual and SMB customers purchase our services online with a credit card, and our business depends substantially upon our ability to offer the credit card payment option. Any loss of our ability to offer our customers a credit card payment option would make our services less attractive to them and hurt our business. Our administrative costs related to customer payment processing would also increase significantly if we were not able to accept credit card payments for our services.

***Failure to effectively and efficiently service SMBs would adversely affect our ability to increase our revenue.***

We market and sell a significant amount of our services to SMBs. SMBs are challenging to reach, acquire and retain in a cost-effective manner. To grow our revenue quickly, we must add new customers, sell additional services to existing customers and encourage existing customers to renew their subscriptions. Selling to and retaining SMBs is more difficult than selling to and retaining large enterprise customers because SMB customers generally:

have high failure rates;

are price sensitive;

are difficult to reach with targeted sales campaigns;

have high churn rates in part because of the scale of their businesses and the ease of switching services; and

generate less revenues per customer and per transaction.

In addition, SMBs frequently have limited budgets and may choose to spend funds on items other than our services. Moreover, SMBs are more likely to be significantly affected by economic downturns than larger, more established companies, and if these organizations experience economic hardship, they may be unwilling or unable to expend resources on IT.

If we are unable to market and sell our services to SMBs with competitive pricing and in a cost-effective manner, our ability to grow our revenue quickly and become profitable will be harmed.

***We may not be able to respond to rapid technological changes with new services, which could have a material adverse effect on our sales and profitability.***

The cloud-based, remote-connectivity services market is characterized by rapid technological change, frequent new service introductions and evolving industry standards. Our ability to attract new customers and increase revenue from existing customers will depend in large part on our ability to enhance and improve our existing services, introduce new services and sell into new markets. To achieve market acceptance for our services, we must effectively anticipate and offer services that meet changing customer demands in a timely manner. Customers may require features and capabilities that our current services do not have. If we fail to develop services that satisfy customer preferences in a timely and cost-effective manner, our ability to renew our services with existing customers and our ability to create or

increase demand for our services will be harmed.

We may experience difficulties with software development, industry standards, design or marketing that could delay or prevent our development, introduction or implementation of new services and enhancements. The introduction of new services by competitors, the emergence of new industry standards or the development of entirely new technologies to replace existing service offerings could render our existing or future services obsolete. If our services become obsolete due to wide-spread adoption of alternative connectivity technologies our ability to generate revenue may be impaired. In addition, any new markets into which we attempt to sell our services, including new countries or regions, may not be receptive.

If we are unable to successfully develop or acquire new services, enhance our existing services to anticipate and meet customer preferences or sell our services into new markets, our revenue and results of operations would be adversely affected.

***The markets in which we participate are competitive, with low barriers to entry, and if we do not compete effectively, our operating results may be harmed.***

The markets for remote-connectivity solutions are competitive and rapidly changing, with relatively low barriers to entry. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. In addition, pricing pressures and increased competition generally could result in reduced sales, reduced margins or the failure of our services to achieve or maintain widespread market acceptance. Often we compete against existing services that our potential customers have already made significant expenditures to acquire and implement.

Certain of our competitors offer, or may in the future offer, lower priced, or free, products or services that compete with our services. This competition may result in reduced prices and a substantial loss of customers for our services or a reduction in our revenue.

Our services compete with large, established competitors like Citrix Systems, WebEx (a division of Cisco Systems), Microsoft, IBM, Apple, Google and Adobe. Certain of our services also compete with smaller competitors such as NTRglobal, TeamViewer, Splashtop, Bomgar, LivePerson, Dropbox, BOX and SugarSync. Many of our actual and potential competitors enjoy competitive advantages over us, such as greater name recognition, longer operating histories, more varied services and larger marketing budgets, as well as greater financial, technical and other resources. In addition, many of our competitors have established marketing relationships and access to larger customer bases, and have major distribution agreements with consultants, system integrators and resellers. If we are not able to compete effectively, our operating results will be harmed.

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***Industry consolidation may result in increased competition.***

Some of our competitors have made or may make acquisitions or may enter into partnerships or other strategic relationships to offer a more comprehensive service than they individually had offered. In addition, new entrants not currently considered to be competitors may enter the market through acquisitions, partnerships or strategic relationships. We expect these trends to continue as companies attempt to strengthen or maintain their market positions. Many of the companies driving this trend have significantly greater financial, technical and other resources than we do and may be better positioned to acquire and offer complementary services and technologies. The companies resulting from such combinations may create more compelling service offerings and may offer greater pricing flexibility than we can or may engage in business practices that make it more difficult for us to compete effectively, including on the basis of price, sales and marketing programs, technology or service functionality. These pressures could result in a substantial loss of customers or a reduction in our revenues.

***Original equipment manufacturers may adopt solutions provided by our competitors.***

Original equipment manufacturers may in the future seek to build the capability for remote-connectivity solutions into their products. We may compete with our competitors to sell our services to, or partner with, these manufacturers. Our ability to attract and partner with these manufacturers will, in large part, depend on the competitiveness of our services. If we fail to attract or partner with, or our competitors are successful in attracting or partnering with, these manufacturers, our revenue and results of operations would be affected adversely.

***Our quarterly operating results may fluctuate in the future. As a result, we may fail to meet or exceed the expectations of research analysts or investors, which could cause our stock price to decline.***

Our quarterly operating results may fluctuate as a result of a variety of factors, many of which are outside of our control. If our quarterly operating results or guidance fall below the expectations of research analysts or investors, the price of our common stock could decline substantially. Fluctuations in our quarterly operating results or guidance may be due to a number of factors, including, but not limited to, those listed below:

our ability to renew existing customers, increase sales to existing customers and attract new customers;

the amount and timing of operating costs and capital expenditures related to the operation, maintenance and expansion of our business;

service outages or security breaches;

whether we meet the service level commitments in our agreements with our customers;

changes in our pricing policies or those of our competitors;

our ability to successfully implement strategic business model changes;

the timing and success of new application and service introductions and upgrades by us or our competitors;

changes in sales compensation plans or organizational structure;

the timing of costs related to the development or acquisition of technologies, services or businesses;

seasonal variations or other cyclicalities in the demand for our services;

general economic, industry and market conditions and those conditions specific to Internet usage and online businesses;

litigation, including class action litigation, involving our company, our services, or our general industry;

the purchasing and budgeting cycles of our customers;

the financial condition of our customers; and

geopolitical events such as war, threat of war or terrorist acts.

We believe that our quarterly revenue and operating results may vary significantly in the future and that period-to-period comparisons of our operating results may not be meaningful. You should not rely on past results as an indication of future performance.

***If we fail to maintain proper and effective internal controls, our ability to produce accurate and timely financial statements could be impaired, which could harm our operating results, our ability to operate our business and investors' views of us.***

Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort. Our internal controls over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles in the United States of America. In addition, Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, requires an annual management assessment of the effectiveness of our internal controls over financial reporting and a

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report from our independent registered public accounting firm addressing the effectiveness of our internal controls over financial reporting. We have documented, tested and improved, to the extent necessary, our internal controls over financial reporting for the year ended December 31, 2013. If in the future we are not able to comply with the requirements of Section 404 of the Sarbanes-Oxley Act in a timely manner, or if as part of our process of documenting and testing our internal controls over financial reporting, we or our independent registered public accounting firm identify deficiencies or areas for further attention and improvement, implementing appropriate changes to our internal controls may distract our officers and employees, entail substantial costs to modify our existing processes and take significant time to complete. These changes may not, however, be effective in maintaining the adequacy of our internal controls, and any failure to maintain that adequacy, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and harm our business. In addition, investors' perceptions that our internal controls are inadequate or that we are unable to produce accurate financial statements on a timely basis may harm our stock price and make it more difficult for us to effectively market and sell our services to new and existing customers.

***We provide minimum service level commitments to some of our customers, the failure of which to meet could cause us to issue credits for future services or pay penalties, which could significantly harm our revenue.***

Some of our customer agreements now, and may in the future, provide minimum service level commitments regarding items such as uptime, functionality or performance. If we are unable to meet the stated service level commitments for these customers or our services suffer extended periods of unavailability, we are or may be contractually obligated to provide these customers with credits for future services or pay other penalties. Our revenue could be significantly impacted if we are unable to meet our service level commitments and are required to provide a significant amount of our services at no cost or pay other penalties. We do not currently have any reserves on our balance sheet for these commitments.

***If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service or address competitive challenges adequately.***

For the last three fiscal years, our revenue has grown from \$119.5 million in 2011 to \$138.8 million in 2012 and to \$166.3 million in 2013. For the six months ended June 30, 2014, we reported revenue of \$104.0 million. Our growth has placed, and may continue to place, a significant strain on our managerial, administrative, operational, financial and other resources. We intend to further expand our overall business, customer base, headcount and operations both domestically and internationally. Creating a global organization and managing a geographically dispersed workforce will require substantial management effort and significant additional investment in our infrastructure. We will be required to continue to improve our operational, financial and management controls and our reporting procedures and we may not be able to do so effectively. As such, we may be unable to manage our expenses effectively in the future, which may negatively impact our gross profit or operating expenses in any particular quarter.

***If we do not effectively expand and train our work force, our future operating results will suffer.***

We plan to continue to expand our work force both domestically and internationally to increase our customer base and revenue. We believe that there is significant competition for qualified personnel with the skills and technical knowledge that we require. Our ability to achieve significant revenue growth will depend, in large part, on our success in recruiting, training and retaining sufficient numbers of personnel to support our growth. New hires require significant training and, in most cases, take significant time before they achieve full productivity. Our recent hires and planned hires may not become as productive as we expect, and we may be unable to hire or retain sufficient numbers of qualified individuals. If our recruiting, training and retention efforts are not successful or do not generate a corresponding increase in revenue, our business will be harmed.

***Our sales cycles for enterprise customers can be long, unpredictable and require considerable time and expense, which may cause our operating results to fluctuate.***

The timing of our revenue from sales to enterprise customers is difficult to predict. These efforts require us to educate our customers about the use and benefit of our services, including the technical capabilities and potential cost savings to an organization. Enterprise customers typically undertake a significant evaluation process that has in the past resulted in a lengthy sales cycle, typically several months. We spend substantial time, effort and money on our enterprise sales efforts without any assurance that our efforts will produce any sales. In addition, service subscriptions are frequently subject to budget constraints and unplanned administrative, processing and other delays. If sales expected from a specific customer for a particular quarter are not realized in that quarter or at all, our results could fall short of public expectations and our business, operating results and financial condition could be adversely affected.

***Our long-term success depends, in part, on our ability to expand the sales of our services to customers located outside of the United States, and thus our business is susceptible to risks associated with international sales and operations.***

We currently maintain offices and have sales personnel outside of the United States and are expanding our international operations. Our international expansion efforts may not be successful. In addition, conducting international operations subjects us to new risks that we have not generally faced in the United States. These risks include:

localization of our services, including translation into foreign languages and adaptation for local practices and regulatory requirements;

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lack of familiarity with and unexpected changes in foreign regulatory requirements;

longer accounts receivable payment cycles and difficulties in collecting accounts receivable;

difficulties in managing and staffing international operations;

fluctuations in currency exchange rates;

potentially adverse tax consequences, including the complexities of foreign value added or other tax systems and restrictions on the repatriation of earnings;

dependence on certain third parties, including channel partners with whom we do not have extensive experience;

the burdens of complying with a wide variety of foreign laws and legal standards;

increased financial accounting and reporting burdens and complexities;

political, social and economic instability abroad, terrorist attacks and security concerns in general; and

reduced or varied protection for intellectual property rights in some countries.

Operating in international markets also requires significant management attention and financial resources. The investment and additional resources required to establish operations and manage growth in other countries may not produce desired levels of revenue or profitability.

***Adverse economic conditions or reduced IT spending may adversely impact our revenues and profitability.***

Our business depends on the overall demand for IT and on the economic health of our current and prospective customers. The use of our service is often discretionary and may involve a commitment of capital and other resources. Weak economic conditions in the United States, European Union and other key international economies may affect the rate of IT spending and could adversely impact our customers' ability or willingness to purchase our services, delay prospective customers' purchasing decisions, reduce the value or duration of their subscription contracts, or affect renewal rates, all of which could have an adverse effect on our business, operating results and financial condition.

***Our success depends in large part on our ability to protect and enforce our intellectual property rights.***

We rely on a combination of copyright, service mark, trademark and trade secret laws, as well as confidentiality procedures and contractual restrictions, to establish and protect our proprietary rights, all of which provide only limited protection. In addition, we have six issued patents and eleven patents pending, and we are in the process of



filing additional patents. We cannot assure you that any patents will issue from our currently pending patent applications in a manner that gives us the protection that we seek, if at all, or that any future patents issued to us will not be challenged, invalidated or circumvented. Any patents that may issue in the future from pending or future patent applications may not provide sufficiently broad protection or they may not prove to be enforceable in actions against alleged infringers. Also, we cannot assure you that any future service mark or trademark registrations will be issued for pending or future applications or that any registered service marks or trademarks will be enforceable or provide adequate protection of our proprietary rights.

We endeavor to enter into agreements with our employees and contractors and agreements with parties with whom we do business to limit access to and disclosure of our proprietary information. The steps we have taken, however, may not prevent unauthorized use or the reverse engineering of our technology. Moreover, others may independently develop technologies that are competitive to ours or infringe our intellectual property. Enforcement of our intellectual property rights also depends on our successful legal actions against these infringers, but these actions may not be successful, even when our rights have been infringed.

Furthermore, effective patent, trademark, service mark, copyright and trade secret protection may not be available in every country in which our services are available. In addition, the legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in Internet-related industries are uncertain and still evolving.

***Our use of open source software could negatively affect our ability to sell our services and subject us to possible litigation.***

A portion of the technologies we license incorporate so-called open source software, and we may incorporate additional open source software in the future. Open source software is generally licensed by its authors or other third parties under open source licenses. If we fail to comply with these licenses, we may be subject to certain conditions, including requirements that we offer our services that incorporate the open source software for no cost, that we make available source code for modifications or derivative works we create based upon, incorporating or using the open source software and/or that we license such modifications or derivative works under the terms of the particular open source license. If an author or other third party that distributes such open source software were to allege that we had not complied with the conditions of one or more of these licenses, we could be required to incur significant legal expenses defending against such allegations and could be subject to significant damages, enjoined from the sale of our services that contained the open source software and required to comply with the foregoing conditions, which could disrupt the distribution and sale of some of our services.

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***We rely on third-party software, including server software and licenses from third parties to use patented intellectual property that is required for the development of our services, which may be difficult to obtain or which could cause errors or failures of our services.***

We rely on software licensed from third parties to offer our services, including server software from Microsoft and patented third-party technology. In addition, we may need to obtain future licenses from third parties to use intellectual property associated with the development of our services, which might not be available to us on acceptable terms, or at all. Any loss of the right to use any software required for the development and maintenance of our services could result in delays in the provision of our services until equivalent technology is either developed by us, or, if available, is identified, obtained and integrated, which could harm our business. Any errors or defects in third-party software could result in errors or a failure of our services which could harm our business.

***Material defects or errors in the software we use to deliver our services could harm our reputation, result in significant costs to us and impair our ability to sell our services.***

The software applications underlying our services are inherently complex and may contain material defects or errors, particularly when first introduced or when new versions or enhancements are released. We have from time to time found defects in our services, and new errors in our existing services may be detected in the future. Any defects that cause interruptions to the availability of our services could result in:

a reduction in sales or delay in market acceptance of our services;

sales credits or refunds to our customers;

loss of existing customers and difficulty in attracting new customers;

diversion of development resources;

harm to our reputation; and

increased insurance costs.

After the release of our services, defects or errors may also be identified from time to time by our internal team and by our customers. The costs incurred in correcting any material defects or errors in our services may be substantial and could harm our operating results.

***Government regulation of the Internet and e-commerce and of the international exchange of certain technologies is subject to possible unfavorable changes, and our failure to comply with applicable regulations could harm our business and operating results.***

As Internet commerce continues to evolve, increasing regulation by federal, state or foreign governments becomes more likely. For example, we believe increased regulation is likely in the area of data privacy, and laws and

regulations applying to the solicitation, collection, processing or use of personal or consumer information could affect our customers' ability to use and share data, potentially reducing demand for our products and services. In addition, taxation of products and services provided over the Internet or other charges imposed by government agencies or by private organizations for accessing the Internet may also be imposed. Any regulation imposing greater fees for Internet use or restricting the exchange of information over the Internet could result in reduced growth or a decline in the use of the Internet and could diminish the viability of our Internet-based services, which could harm our business and operating results.

Our software products contain encryption technologies, certain types of which are subject to U.S. and foreign export control regulations and, in some foreign countries, restrictions on importation and/or use. We have submitted our encryption products for technical review under U.S. export regulations and have received the necessary approvals. Any failure on our part to comply with encryption or other applicable export control requirements could result in financial penalties or other sanctions under the U.S. export regulations, which could harm our business and operating results. Foreign regulatory restrictions could impair our access to technologies that we seek for improving our products and services and may also limit or reduce the demand for our products and services outside of the United States.

***Our operating results may be harmed if we are required to collect sales or other related taxes for our subscription services in jurisdictions where we have not historically done so.***

Primarily due to the nature of our services in certain states and countries, we do not believe we are required to collect sales or other related taxes from our customers in certain states or countries. However, one or more other states or countries may seek to impose sales or other tax collection obligations on us, including for past sales by us or our resellers and other partners. A successful assertion that we should be collecting sales or other related taxes on our services could result in substantial tax liabilities for past sales, discourage customers from purchasing our services or otherwise harm our business and operating results.

***The loss of key employees or an inability to attract and retain additional personnel may impair our ability to grow our business.***

We are highly dependent upon the continued service and performance of our executive management team, including our President and Chief Executive Officer, as well as other key technical and sales employees. These key employees are not party to an employment agreement with us, and they may terminate employment with us at any time with no advance notice. The replacement of these key employees likely would involve significant time and costs, and the loss of these key employees may significantly delay or prevent the achievement of our business objectives.

We face intense competition for qualified individuals from numerous technology, software and manufacturing companies. For example, our competitors may be able to attract and retain a more qualified engineering team by offering more competitive compensation packages. If we

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are unable to attract new engineers and retain our current engineers, we may not be able to develop and maintain our services at the same levels as our competitors and we may, therefore, lose potential customers and sales penetration in certain markets. Our failure to attract and retain suitably qualified individuals could have an adverse effect on our ability to implement our business plan and, as a result, our ability to compete would decrease, our operating results would suffer and our revenues would decrease.

***Our business is substantially dependent on market demand for, and acceptance of, the cloud-based model for the use of software.***

We derive, and expect to continue to derive, substantially all of our revenue from the sale of cloud-based services. As a result, widespread acceptance and use of the cloud-based business model is critical to our future growth and success. Under the perpetual or periodic license model for software procurement, users of the software typically run applications on their hardware. Because companies are generally predisposed to maintaining control of their IT systems and infrastructure, there may be resistance to the concept of accessing the functionality that software provides as a service through a third party. If the market for cloud-based, software solutions ceases to grow or grows more slowly than we currently anticipate, demand for our services could be negatively affected.

***Growth of our business may be adversely affected if businesses, IT support providers or consumers do not adopt remote access, support and collaboration solutions more widely.***

Our services employ new and emerging technologies for remote access, support and collaboration. Our target customers may hesitate to accept the risks inherent in applying and relying on new technologies or methodologies to supplant traditional methods of remote connectivity. Our business will not be successful if our target customers do not accept the use of our remote access and remote support technologies.

***Our success depends on our customers' continued high-speed access to the Internet and the continued reliability of the Internet infrastructure.***

Because our services are designed to work over the Internet, our revenue growth depends on our customers' high-speed access to the Internet, as well as the continued maintenance and development of the Internet infrastructure. The future delivery of our services will depend on third-party Internet service providers to expand high-speed Internet access, to maintain a reliable network with the necessary speed, data capacity and security, and to develop complementary products and services, including high-speed modems, for providing reliable and timely Internet access and services. The success of our business depends directly on the continued accessibility, maintenance and improvement of the Internet as a convenient means of customer interaction, as well as an efficient medium for the delivery and distribution of information by businesses to their employees. All of these factors are out of our control.

To the extent that the Internet continues to experience increased numbers of users, frequency of use or bandwidth requirements, the Internet may become congested and be unable to support the demands placed on it, and its performance or reliability may decline. Any future Internet outages or delays could adversely affect our ability to provide services to our customers.

## **RISKS RELATED TO OWNERSHIP OF OUR COMMON STOCK**

***Our failure to raise additional capital or generate the cash flows necessary to expand our operations and invest in our services could reduce our ability to compete successfully.***

We may need to raise additional funds, and we may not be able to obtain additional debt or equity financing on favorable terms, if at all. If we raise additional equity financing, our stockholders may experience significant dilution of their ownership interests, and the per share value of our common stock could decline. If we engage in debt financing, we may be required to accept terms that restrict our ability to incur additional indebtedness and force us to maintain specified liquidity or other ratios. If we need additional capital and cannot raise it on acceptable terms, we may not be able to, among other things:

develop or enhance our services;

continue to expand our development, sales and marketing organizations;

acquire complementary technologies, products or businesses;

expand our operations, in the United States or internationally;

hire, train and retain employees; or

respond to competitive pressures or unanticipated working capital requirements.

***Our stock price may be volatile, and the market price of our common stock may drop in the future.***

Prior to the completion of our initial public offering, or IPO, in July 2009, there was no public market for shares of our common stock. During the period from our IPO until July 24, 2014, our common stock has traded as high as \$49.50 and as low as \$15.15. An active, liquid and orderly market for our common stock may not develop or be sustained, which could depress the trading price of our common stock. Some of the factors that may cause the market price of our common stock to fluctuate include:

fluctuations in our quarterly financial results or the quarterly financial results of companies perceived to be similar to us;

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fluctuations in our recorded revenue, even during periods of significant sales order activity;

changes in estimates of our financial results or recommendations by securities analysts;

failure of any of our services to achieve or maintain market acceptance;

changes in market valuations of similar companies;

announcements regarding changes to our current or planned products or services;

success of competitive products or services;

changes in our capital structure, such as future issuances of securities or the incurrence of debt;

announcements by us or our competitors of significant services, contracts, acquisitions or strategic alliances;

regulatory developments in the United States, foreign countries or both;

litigation, including class action litigation, involving our company, our services, or our general industry, including announcements regarding developments in on-going litigation matters;

additions or departures of key personnel;

general perception of the future of the remote-connectivity market or our services;

investors' general perception of us; and

changes in general economic, industry and market conditions.

In addition, if the market for technology stocks or the stock market in general experiences a loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, financial condition or results of operations. If any of the foregoing occurs, it could cause our stock price to fall and may expose us to class action lawsuits that, even if unsuccessful, could be costly to defend and a distraction to management.

***A significant portion of our total outstanding shares may be sold into the public market at any time, which could cause the market price of our common stock to drop significantly, even if our business is doing well.***

If our existing stockholders sell a large number of shares of our common stock or the public market perceives that such existing stockholders might sell shares of common stock, the trading price of our common stock could decline significantly.

***If securities or industry analysts do not publish or cease publishing research or reports about us, our business or our market, or if they publish a negative report or change their recommendations regarding our stock adversely, our stock price and trading volume could decline.***

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about us, our business, our market or our competitors. If any of the analysts who cover us or may cover us in the future publish a negative report or change their recommendation regarding our stock adversely, or provide more favorable relative recommendations about our competitors, our stock price would likely decline. If any analyst who covers us or may cover us in the future were to cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

***Our management has broad discretion over the use of our existing cash resources and might not use such funds in ways that increase the value of our common stock.***

Our management will continue to have broad discretion to use our cash resources. Our management might not apply these cash resources in ways that increase the value of our common stock.

***We do not expect to declare any dividends in the foreseeable future.***

We do not anticipate declaring any cash dividends to holders of our common stock in the foreseeable future. Consequently, stockholders must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on the value of their shares of our common stock.

***As a public company, we incur significant additional costs which could harm our operating results.***

As a public company, we incur significant legal, accounting and other expenses, including costs associated with public company reporting requirements. We also have incurred and will continue to incur costs associated with current corporate governance requirements, including requirements under Section 404 and other provisions of the Sarbanes-Oxley Act, as well as rules implemented by the Securities and Exchange Commission, or SEC, and The NASDAQ Global Select Market. The expenses incurred by public companies for reporting and corporate governance purposes have increased dramatically. We expect these rules and regulations to substantially increase our legal and financial compliance costs and to make some activities more time-consuming and costly. We also expect these new rules and regulations may make it more difficult and more expensive for us to maintain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage previously available. As a result, it may be more difficult for us to attract and retain qualified individuals to serve on our board of directors or as our executive officers.

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***Certain stockholders could attempt to influence changes within the Company which could adversely affect the Company's operations, financial condition and the value of our common stock.***

Our stockholders may from time-to-time seek to acquire a controlling stake in our company, engage in proxy solicitations, advance shareholder proposals or otherwise attempt to effect changes. Campaigns by stockholders to effect changes at publicly traded companies are sometimes led by investors seeking to increase short-term stockholder value through actions such as financial restructuring, increased debt, special dividends, stock repurchases or sales of assets or the entire company. Responding to proxy contests and other actions by activist stockholders can be costly and time-consuming, disrupting our operations and diverting the attention of our Board of Directors and senior management from the pursuit of business strategies. These actions could adversely affect our operations, financial condition and the value of our common stock.

***Anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.***

Our certificate of incorporation, bylaws and Delaware law contain provisions that could have the effect of rendering more difficult or discouraging an acquisition deemed undesirable by our board of directors. Our corporate governance documents include provisions:

authorizing blank check preferred stock, which could be issued with voting, liquidation, dividend and other rights superior to our common stock;

limiting the liability of, and providing indemnification to, our directors and officers;

limiting the ability of our stockholders to call and bring business before special meetings and to take action by written consent in lieu of a meeting;

requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;

controlling the procedures for the conduct and scheduling of board of directors and stockholder meetings;

providing the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings;

limiting the determination of the number of directors on our board of directors and the filling of vacancies or newly created seats on the board to our board of directors then in office; and



providing that directors may be removed by stockholders only for cause.

These provisions, alone or together, could delay hostile takeovers and changes in control of our company or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

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

### **(a) Sales of Unregistered Securities**

We did not sell any unregistered securities in the three and six months ended June 30, 2014.

### **(b) Use of Proceeds**

We did not receive any proceeds from the sale of unregistered securities in the three and six months ended June 30, 2014.

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## (c) Purchases of Equity Securities

<b>Period</b>		<b>Total Number of Shares Purchased</b>	<b>Average Price per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(1)</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares that may yet be Purchased Under the Plans or Programs(1)</b>
April 1, 2014	April 30, 2014	14,600	\$ 39.25	14,600	30,447,644
May 1, 2014	May 31, 2014	1,911	39.98	1,911	30,371,250
June 1, 2014	June 30, 2014	30,000	46.36	30,000	28,980,591
Total		46,511	\$ 43.86	46,511	

- (1) Effective August 13, 2013, we replaced our previous \$25 million share repurchase program with a new \$50 million share repurchase program (See Note 8 to the Condensed Consolidated Financial Statements). As of June 30, 2014, we have purchased an aggregate of 639,911 shares pursuant to our \$50 million share repurchase program.

**Item 6. Exhibits**

The exhibits listed in the Exhibit Index immediately preceding the exhibits are filed (other than exhibits 32.1 and 32.2) as part of this Quarterly Report on Form 10-Q and such Exhibit Index is incorporated herein by reference.

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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.

**LOGMEIN, INC.**

Date: July 25, 2014

By: /s/ Michael K. Simon

Michael K Simon  
President and Chief Executive Officer

(Principal Executive Officer)

Date: July 25, 2014

By: /s/ James F. Kelliher

James F. Kelliher  
Chief Financial Officer

(Principal Financial Officer)

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**Table of Contents*****EXHIBIT INDEX***

Listed and indexed below are all Exhibits filed as part of this report.

<b>Exhibit No.</b>	<b>Description</b>
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Chief Executive Officer.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Chief Financial Officer.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, by Chief Executive Officer.
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, by Chief Financial Officer.
101	The following materials from LogMeIn, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2014, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Comprehensive Income, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements.