

REALPAGE INC  
Form 10-Q  
August 07, 2012  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2012

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: 001-34846

**RealPage, Inc.**

(Exact name of registrant as specified in its charter)

Edgar Filing: REALPAGE INC - Form 10-Q

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

**75-2788861**  
(I.R.S. Employer  
Identification No.)

**4000 International Parkway**  
**Carrollton, Texas**  
(Address of principal executive offices)

**75007-1951**  
(Zip Code)

**(972) 820-3000**  
(Registrant's telephone number, including area code)

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

<u>Class</u>	<b>Outstanding at July 31, 2012</b>
Common Stock, \$0.001 par value	73,661,710

**Table of Contents**

**INDEX**

**PART I FINANCIAL INFORMATION**

<u>Item 1. Financial Statements</u>	1
<u>Condensed Consolidated Balance Sheets</u>	1
<u>Condensed Consolidated Statements of Operations</u>	2
<u>Condensed Consolidated Statements of Comprehensive Income (Loss)</u>	3
<u>Condensed Consolidated Statements of Stockholders' Equity</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	5
<u>Notes to the Condensed Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	25
<u>Item 4. Controls and Procedures</u>	25
<b><u>PART II OTHER INFORMATION</u></b>	
<u>Item 1. Legal Proceedings</u>	26
<u>Item 1A. Risk Factors</u>	28
<u>Item 6. Exhibits</u>	52
<b><u>SIGNATURES AND EXHIBIT INDEX</u></b>	52
<u>Signatures</u>	52
<u>Exhibit Index</u>	52

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements.****REALPAGE, INC.****Condensed Consolidated Balance Sheets****(in thousands, except share data)**

	<b>June 30, 2012 (Unaudited)</b>	<b>December 31, 2011</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 45,837	\$ 51,273
Restricted cash	24,170	19,098
Accounts receivable, less allowance for doubtful accounts of \$990 and \$979 at June 30, 2012 and December 31, 2011, respectively	43,750	43,883
Deferred tax asset, net of valuation allowance	387	272
Other current assets	10,919	10,232
Total current assets	125,063	124,758
Property, equipment, and software, net	31,453	27,974
Goodwill	130,540	129,292
Identified intangible assets, net	106,123	112,308
Deferred tax asset, net of valuation allowance	4,641	2,539
Other assets	3,973	3,194
Total assets	\$ 401,793	\$ 400,065
<b>Liabilities and stockholders equity</b>		
Current liabilities:		
Accounts payable	\$ 11,655	\$ 12,218
Accrued expenses and other current liabilities	28,903	25,816
Current portion of deferred revenue	56,989	57,325
Customer deposits held in restricted accounts	24,133	19,017
Total current liabilities	121,680	114,376
Deferred revenue	9,534	8,693
Long-term debt, less current portion	35,000	50,312
Other long-term liabilities	3,672	3,803
Total liabilities	169,886	177,184
Commitments and contingencies (Note 8)		
Stockholders equity:		
Preferred stock, \$0.001 par value, 10,000,000 shares authorized and zero shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively		
Common stock, \$0.001 par value: 125,000,000 shares authorized, 74,436,163 and 73,115,779 shares issued and 73,658,956 and 72,701,571 shares outstanding at June 30, 2012 and December 31, 2011, respectively	74	73
Additional paid-in capital	328,270	316,964
Treasury stock, at cost: 777,207 and 414,208 shares at June 30, 2012 and December 31, 2011, respectively	(4,762)	(3,138)
Accumulated deficit	(91,613)	(90,961)

Edgar Filing: REALPAGE INC - Form 10-Q

Accumulated other comprehensive loss	(62)	(57)
Total stockholders' equity	231,907	222,881
Total liabilities and stockholders' equity	\$ 401,793	\$ 400,065

See accompanying notes.

**Table of Contents****REALPAGE, INC.****Condensed Consolidated Statements of Operations****(in thousands, except per share data)****(Unaudited)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
<b>Revenue:</b>				
On demand	\$ 74,938	\$ 57,039	\$ 145,656	\$ 109,976
On premise	1,261	1,628	2,677	3,273
Professional and other	2,593	2,968	4,876	5,934
<b>Total revenue</b>	<b>78,792</b>	<b>61,635</b>	<b>153,209</b>	<b>119,183</b>
Cost of revenue(1)	31,848	25,810	62,461	50,493
<b>Gross profit</b>	<b>46,944</b>	<b>35,825</b>	<b>90,748</b>	<b>68,690</b>
<b>Operating expense:</b>				
Product development(1)	11,738	10,537	23,051	20,853
Sales and marketing(1)	18,588	14,510	35,394	27,304
General and administrative(1)	19,946	9,574	32,249	19,350
<b>Total operating expense</b>	<b>50,272</b>	<b>34,621</b>	<b>90,694</b>	<b>67,507</b>
<b>Operating income (loss)</b>	<b>(3,328)</b>	<b>1,204</b>	<b>54</b>	<b>1,183</b>
Interest expense and other, net	(577)	(732)	(1,213)	(1,898)
<b>Income (loss) before income taxes</b>	<b>(3,905)</b>	<b>472</b>	<b>(1,159)</b>	<b>(715)</b>
Income tax expense (benefit)	(1,533)	190	(507)	(349)
<b>Net income (loss)</b>	<b>\$ (2,372)</b>	<b>\$ 282</b>	<b>\$ (652)</b>	<b>\$ (366)</b>
<b>Net income (loss) per share</b>				
Basic	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)
Diluted	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)
Weighted average shares used in computing net income (loss) per share				
Basic	71,102	68,673	70,846	67,741
Diluted	71,102	72,012	70,846	67,741

(1) Includes stock-based compensation expense as follows:

Cost of revenue	\$ 750	\$ 312	\$ 1,439	\$ 610
Product development	1,002	1,105	2,064	2,085
Sales and marketing	1,032	2,627	1,769	5,360
General and administrative	1,532	925	3,032	1,767

*See accompanying notes.*



**Table of Contents**

**REALPAGE, INC.**

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

**(in thousands)**

**(Unaudited)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
	<b>(in thousands, unaudited)</b>			
Net income (loss)	\$ (2,372)	\$ 282	\$ (652)	\$ (366)
Foreign currency translation loss	(1)	(8)	(5)	(20)
<b>Comprehensive income (loss)</b>	<b>\$ (2,373)</b>	<b>\$ 274</b>	<b>\$ (657)</b>	<b>\$ (386)</b>

*See accompanying notes.*



**Table of Contents****REALPAGE, INC.****Condensed Consolidated Statements of Stockholders Equity****(in thousands)****(Unaudited)**

	Common Stock		Additional	Other	Accumulated	Treasury Shares		Total
	Shares	Amount	Paid-in	Comprehensive	Deficit	Shares	Amount	Stockholders
			Capital	Loss				Equity
Balance as of December 31, 2011	73,116	\$ 73	\$ 316,964	\$ (57)	\$ (90,961)	(414)	\$ (3,138)	\$ 222,881
Foreign currency translation				(5)				(5)
Net loss					(652)			(652)
Exercise of stock options	636	1	3,002					3,003
Treasury stock purchase, at cost						(363)	(1,624)	(1,624)
Issuance of restricted stock	684							
Stock-based compensation			8,304					8,304
Balance as of June 30, 2012	74,436	\$ 74	\$ 328,270	\$ (62)	\$ (91,613)	(777)	\$ (4,762)	\$ 231,907

*See accompanying notes.*

**Table of Contents****REALPAGE, INC.****Condensed Consolidated Statements of Cash Flows****(in thousands)****(Unaudited)**

	<b>Six Months Ended June 30,</b>	
	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (652)	\$ (366)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	15,737	14,016
Deferred tax benefit	(856)	(767)
Stock-based compensation	8,304	9,822
Loss on disposal of assets	379	395
Acquisition-related contingent consideration	182	105
Changes in assets and liabilities, net of assets acquired and liabilities assumed in business combinations:		
Accounts receivable	161	(4,034)
Customer deposits	44	17
Other current assets	30	(1,208)
Other assets	(775)	(493)
Accounts payable	(387)	1,941
Accrued compensation, taxes and benefits	1,461	(1,336)
Deferred revenue	471	2,275
Other current and long-term liabilities	8,107	(1,146)
Net cash provided by operating activities	32,206	19,221
<b>Cash flows from investing activities:</b>		
Purchases of property, equipment and software	(9,905)	(5,642)
Acquisition of businesses, net of cash acquired	(13,509)	(20,031)
Acquisition of intangible assets	(225)	
Net cash used by investing activities	(23,639)	(25,673)
<b>Cash flows from financing activities:</b>		
Stock issuance costs from public offerings		(775)
Payments on revolving credit facility	(15,312)	
Payments on notes payable		(5,391)
Payments on capital lease obligations	(65)	(351)
Issuance of common stock	3,003	7,437
Purchase of treasury stock	(1,624)	(473)
Net cash (used) provided by financing activities	(13,998)	447
Net decrease in cash and cash equivalents	(5,431)	(6,005)
Effect of exchange rate on cash	(5)	(20)
<b>Cash and cash equivalents:</b>		
Beginning of period	51,273	118,010
End of period	\$ 45,837	\$ 111,985

Edgar Filing: REALPAGE INC - Form 10-Q

**Supplemental cash flow information:**

Cash paid for interest	\$ 953	\$ 1,390
Cash paid for income taxes, net of refunds	\$ 257	\$ 665

*See accompanying notes.*

---

**Table of Contents**

**Notes to the Condensed Consolidated Financial Statements**

**(Unaudited)**

**1. The Company**

RealPage, Inc., a Delaware corporation, and its subsidiaries, (the Company or we or us ) is a provider of property management solutions that enable owners and managers of single-family and a wide variety of multi-family rental property types to manage their marketing, pricing, screening, leasing, accounting, purchasing and other property operations. Our on demand software solutions are delivered through an integrated software platform that provides a single point of access and a shared repository of prospect, resident and property data. By integrating and streamlining a wide range of complex processes and interactions among the rental housing ecosystem of owners, managers, prospects, residents and service providers, our platform optimizes the property management process and improves the experience for all of these constituents. Our solutions enable property owners and managers to optimize revenues and reduce operating costs through higher occupancy, improved pricing methodologies, new sources of revenue from ancillary services, improved collections and more integrated and centralized processes.

**2. Summary of Significant Accounting Policies**

***Basis of Presentation***

The accompanying unaudited condensed consolidated financial statements and footnotes have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) have been condensed or omitted pursuant to those rules and regulations. We believe that the disclosures made are adequate to make the information not misleading.

The condensed consolidated financial statements included herein reflect all adjustments (consisting of normal, recurring adjustments) which are, in the opinion of management, necessary to state fairly the results for the interim periods presented. All intercompany balances and transactions have been eliminated in consolidation. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the fiscal year.

It is suggested that these financial statements be read in conjunction with the financial statements and the notes thereto included in our Annual Report on Form 10-K filed with the SEC on February 24, 2012 ( Form 10-K ).

***Segment and Geographic Information***

Our chief operating decision maker is our Chief Executive Officer, who reviews financial information presented on a company-wide basis. As a result, we determined that the Company has a single reporting segment and operating unit structure.

Principally, all of our revenue for the three and six months ended June 30, 2012 and 2011 was in North America.

Net long-lived assets held were \$28.7 million and \$26.4 million in North America and \$2.8 million and \$1.6 million in our international subsidiaries at June 30, 2012 and December 31, 2011, respectively.

***Accounting Policies and Use of Estimates***

The preparation of financial statements in conformity with GAAP requires our management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates include: the allowance for doubtful accounts; the useful lives of intangible assets and the recoverability or impairment of tangible and intangible asset values; fair value measurements; purchase accounting allocations and related reserves; revenue and deferred revenue; stock-based compensation; and our effective income tax rate and the recoverability of deferred tax assets, which are based upon our expectations of future taxable income and allowable deductions. Actual results could differ from these estimates. For greater detail regarding these accounting policies and estimates, refer to our Form 10-K.

***Revenue Recognition***

## Edgar Filing: REALPAGE INC - Form 10-Q

We derive our revenue from three primary sources: our on demand software solutions; our on premise software solutions; and professional and other services. We commence revenue recognition when all of the following conditions are met:

there is persuasive evidence of an arrangement;

6

## Table of Contents

the solution and/or service has been provided to the customer;

the collection of the fees is probable; and

the amount of fees to be paid by the customer is fixed or determinable.

For multi-element arrangements that include multiple software solutions and/or services, we allocate arrangement consideration to all deliverables that have stand-alone value based on their relative selling prices. In such circumstances, we utilize the following hierarchy to determine the selling price to be used for allocating revenue to deliverables as follows:

*Vendor specific objective evidence (VSOE), if available.* The price at which we sell the element in a separate stand-alone transaction;

*Third-party evidence of selling price (TPE), if VSOE of selling price is not available.* Evidence from us or other companies of the value of a largely interchangeable element in a transaction; and

*Estimated selling price (ESP), if neither VSOE nor TPE of selling price is available.* Our best estimate of the stand-alone selling price of an element in a transaction.

Our process for determining ESP for deliverables without VSOE or TPE considers multiple factors that may vary depending upon the unique facts and circumstances related to each deliverable. Key factors primarily considered in developing ESP include prices charged by us for similar offerings when sold separately, pricing policies and approvals from standard pricing and other business objectives.

From time to time, we sell on demand software solutions with professional services. In such cases, as each element has stand alone value, we allocate arrangement consideration based on our estimated selling price of the on demand software solution and VSOE of the selling price of the professional services.

Taxes collected from customers and remitted to governmental authorities are presented on a net basis.

### *On Demand Revenue*

Our on demand revenue consists of license and subscription fees, transaction fees related to certain of our software-enabled value-added services and commissions derived from us selling certain risk mitigation services.

License and subscription fees are comprised of a charge billed at the initial order date and monthly or annual subscription fees for accessing our on demand software solutions. The license fee billed at the initial order date is recognized as revenue on a straight-line basis over the longer of the contractual term or the period in which the customer is expected to benefit, which we consider to be four years. Recognition starts once the product has been activated. Revenue from monthly and annual subscription fees is recognized on a straight-line basis over the access period.

We recognize revenue from transaction fees derived from certain of our software-enabled value-added services as the related services are performed.

As part of our risk mitigation services to the rental housing industry, we act as an insurance agent and derive commission revenue from the sale of insurance products to individuals. The commissions are based upon a percentage of the premium that the insurance company charges to the policyholder and are subject to forfeiture in instances where a policyholder cancels prior to the end of the policy. If the policy is cancelled, our commissions are forfeited as a percent of the unearned premium. As a result, we recognize the commissions related to these services ratably over the policy term as the associated premiums are earned. Our contract with our underwriting partner provides for contingent commissions to be paid to us in accordance with the agreement. This agreement provides for a calculation that considers, on the policies sold by us, earned premiums less i) earned agent commissions; ii) a percent of premium retained by our underwriting partner; iii) incurred losses; iv) profit retained by our underwriting partner during the time period. Our estimate of contingent commission revenue considers historical loss experience on the

policies sold by us.

*On Premise Revenue*

Revenue from our on premise software solutions is comprised of an annual term license, which includes maintenance and support. Customers can renew their annual term license for additional one-year terms at renewal price levels. We recognize the annual term license on a straight-line basis over the contract term.

In addition, we have arrangements that include perpetual licenses with maintenance and other services to be provided over

---

## **Table of Contents**

a fixed term. We allocate and defer revenue equivalent to the VSOE of fair value for the undelivered elements and recognize the difference between the total arrangement fee and the amount deferred for the undelivered elements as revenue. We have determined that we do not have VSOE of fair value for our customer support and professional services in these specific arrangements. As a result, the elements within our multiple-element sales agreements do not qualify for treatment as separate units of accounting. Accordingly, we account for fees received under multiple-element arrangements with customer support or other professional services as a single unit of accounting and recognize the entire arrangement ratably over the longer of the customer support period or the period during which professional services are rendered.

### *Professional and Other Revenue*

Professional & other revenue is recognized as the services are rendered for time and material contracts. Training revenues are recognized after the services are performed.

### *Fair Value Measurements*

The Company measures certain financial assets and liabilities at fair value pursuant to a fair value hierarchy based on inputs to valuation techniques that are used to measure fair value that are either observable or unobservable. Observable inputs reflect assumptions market participants would use in pricing an asset or liability based on market data obtained from independent sources while unobservable inputs reflect a reporting entity's pricing based upon its own market assumptions. The fair value hierarchy consists of the following three levels:

- Level 1     Inputs are quoted prices in active markets for identical assets or liabilities.
- Level 2     Inputs are quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable and market-corroborated inputs which are derived principally from or corroborated by observable market data.
- Level 3     Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable.

### *Concentrations of Credit Risk*

Our cash accounts are maintained at various financial institutions and may, from time to time, exceed federally insured limits. The Company has not experienced any losses in such accounts.

Concentrations of credit risk with respect to accounts receivable result from substantially all of our customers being in the multi-family rental housing market. Our customers, however, are dispersed across different geographic areas. We do not require collateral from customers. We maintain an allowance for losses based upon the expected collectability of accounts receivable. Accounts receivable are written off upon determination of non-collectability following established Company policies based on the aging from the accounts receivable invoice date.

No single customer accounted for 5% or more of our revenue or accounts receivable for the three and six months ended June 30, 2012 or 2011.

### *Recently Issued Accounting Standards*

Based on our evaluation of recently issued accounting standards, there were no standards issued in 2012 that would materially impact our financial position, results of operations or related disclosures.

## **3. Acquisitions**

### *2012 Acquisition*

In January 2012, we acquired substantially all of the operating assets of Vigilant, Incorporated ( Vigilant ). A provider of assisted living software-as-a-service, Vigilant products allow assisted living communities to monitor and schedule detailed care, manage labor costs, provide accurate billing as well as compliance tools through its comprehensive compliance module. This asset acquisition allows us to integrate Vigilant with existing senior living software solutions to further expand the RealPage Senior Living product offerings. We acquired Vigilant for a purchase price of \$5.0 million consisting of a cash payment of \$4.0 million and two additional cash payments of up to \$0.5 million each due 12 months and 24 months after the acquisition date. The \$1.0 million withheld from the purchase consideration was subject to a downward



## Edgar Filing: REALPAGE INC - Form 10-Q

adjustment if certain revenue targets (a level 3 input) were not met for the six months ended June 30, 2012. The fair value of the future cash payment was \$1.0 million as of June 30, 2012. This acquisition was financed from proceeds from cash flows from operations. Acquired intangibles were recorded at fair value based on assumptions made by us. The acquired developed product technologies have a useful life of three years amortized on a straight-line basis. Acquired customer relationships have a useful life of ten years which will be amortized proportionately to the expected

**Table of Contents**

discounted cash flows derived from the asset. All direct acquisition costs were less than \$0.1 million and expensed as incurred. We included the results of operations of this acquisition in our consolidated financial statements from the effective date of the acquisition. Goodwill and identified intangibles associated with this acquisition are deductible for tax purposes.

We have allocated the purchase price for Vigilant as follows:

	<b>Vigilant</b> <b>(in thousands)</b>
Intangible assets:	
Developed product technologies	\$ 1,430
Customer relationships	1,150
Goodwill	2,454
Net other assets	(34)
 Total purchase price	 \$ 5,000

**2011 Acquisitions**

In May 2011, we acquired substantially all of the assets of Compliance Depot, LLC ( Compliance Depot ) for approximately \$22.5 million which included a cash payment of \$19.2 million at closing and three deferred payments of \$1.1 million each payable six, twelve and eighteen months after the acquisition date. As of June 30, 2012, only one payment of \$1.1 million remains outstanding. The acquisition of Compliance Depot expands our ability to provide vendor risk management and compliance software solutions for the rental housing industry. This acquisition was financed from proceeds from our initial public offering and cash flows from operations. Acquired intangibles were recorded at fair value based on assumptions made by us. The acquired developed product technologies have a useful life of three years amortized on a straight-line basis. Acquired customer relationships have a useful life of nine years which will be amortized proportionately to the expected discounted cash flows derived from the asset. The tradenames acquired have an indefinite useful life as we do not plan to cease using the tradenames in the marketplace. All direct acquisition costs were less than \$0.1 million and expensed as incurred. We included the results of operations of this acquisition in our consolidated financial statements from the effective date of the acquisition. Goodwill and identified intangibles associated with this acquisition are deductible for tax purposes.

In July 2011, we acquired Senior-Living.com, Inc., operating under the name SeniorLiving.net ( SLN ), pursuant to an Agreement and Plan of Merger. The acquisition of SLN expands our lead generation capabilities into the senior living rental housing market. The preliminary purchase price consisted of a cash payment of \$4.0 million at closing, additional cash payments of \$0.5 million, half of which is due on each of the first and second anniversaries of the acquisition date, and an estimated cash payment payable (acquisition-related contingent consideration) and up to 400,000 shares of our common stock, in each case payable based on the achievement of certain revenue targets as defined in the purchase agreement. This acquisition was financed from proceeds from cash flows from operations. At the acquisition date, we recorded a liability for the estimated fair value of the acquisition-related contingent consideration of \$0.3 million. In addition, we recorded the fair value of the common shares of \$8.4 million. These fair values were based on management's estimate of the fair value of the cash and the restricted common shares using a probability weighted discounted cash flow model on the achievement of certain revenue targets. The cash payment has a maximum value of \$0.5 million. The acquired developed product technologies have a useful life of three years amortized on a straight-line basis. Acquired customer relationships have a useful life of ten years which will be amortized proportionately to the expected discounted cash flows derived from the asset. The tradenames acquired have an indefinite useful life as we do not plan to cease using the tradenames in the marketplace. All direct acquisition costs were approximately \$0.1 million and expensed as incurred. We included the results of operations of this acquisition in our consolidated financial statements from the effective date of the acquisition. Goodwill and identified intangibles associated with this acquisition are not deductible for tax purposes. The liability established for the acquisition-related contingent consideration will continue to be re-evaluated and recorded at an estimated fair value based on the probabilities, as determined by management, of achieving the related targets (a level 3 input). This evaluation will be performed until all of the targets have been met or terms of the agreement expire. As of June 30, 2012, our liability for the estimated cash payment was \$0.5 million. During the three and six months ended June 30, 2012, we recognized losses of less than \$0.1 million and \$0.1 million, respectively, due to changes in the estimated fair value of the cash acquisition-related contingent consideration.

In August 2011, we acquired Multifamily Technology Solutions, Inc. ( MTS ), which owns the Internet listing service for rental properties called MyNewPlace, pursuant to an Agreement and Plan of Merger. MTS continued as the surviving corporation of the Merger and a wholly owned subsidiary of RealPage. The acquisition of MTS adds an Internet listing service for rental properties and expands our syndication and organic lead generation capabilities. This acquisition was financed from proceeds from our initial public offering, cash flows from operations and

## Edgar Filing: REALPAGE INC - Form 10-Q

issuance of restricted common stock. The preliminary purchase price consisted of a cash payment of \$64.0 million, including amount placed in escrow, net of cash acquired, 294,770 shares of RealPage restricted common stock and the assumption of MTS stock options exercisable for 349,693 shares of RealPage common stock. In addition, the purchase agreement included a put option on the restricted common shares, in which, if the average market price of our common shares falls below an established threshold, we will pay the difference between the average market price and the established threshold in cash. We established a liability of \$1.2 million for the put option which is based on its estimated fair value at the acquisition date.

**Table of Contents**

We also recorded the fair value of the restricted common shares and the assumed stock options of \$6.3 million and \$3.6 million, respectively. The fair value of the restricted common shares was based on management's estimate of the fair value of restricted common shares using a probability weighted discounted cash flow model. The fair values of the assumed stock options and the put option was based on the Black-Scholes option pricing model using inputs consistent with those used in the valuation of our stock options. The acquired developed product technologies have a useful life of three years amortized on a straight-line basis. Acquired customer relationships have a useful life of ten years which will be amortized proportionately to the expected discounted cash flows derived from the asset. The tradenames acquired have an indefinite useful life as we do not plan to cease using the tradenames in the marketplace. All direct acquisition costs were approximately \$0.8 million and expensed as incurred. We included the results of operations of this acquisition in our consolidated financial statements from the effective date of the acquisition. Goodwill and identified intangibles associated with this acquisition are not deductible for tax purposes. The liability established for the put option on the restricted common shares will continue to be re-evaluated and recorded at an estimated fair value based on the changes in market prices of our common stock (a level 2 input). During the three and six months ended June 30, 2012, we recognized a gain of \$0.3 million and a loss of less than \$0.1 million, respectively, due to changes in the estimated fair value of the put option for restricted common shares. One of the minority shareholders of MTS is our customer. In connection with the distribution of the purchase price, we paid this customer for their proportionate share of the purchase price. This transaction was at arm's length and is not related to the ongoing relationship with us.

The purchase agreement also included a portion of the cash and restricted common shares consideration to be placed into escrow. As such, we placed \$14.0 million in cash and 65,873 restricted common shares into an escrow account on the date of acquisition. One half of these amounts will be released from escrow twelve months after the acquisition date. The remaining amounts will be released eighteen months after the acquisition date.

We allocated the purchase price for MTS, SLN and Compliance Depot as follows:

	MTS	SLN (in thousands)	Compliance Depot
<b>Intangible assets:</b>			
Developed product technologies	\$ 2,280	\$ 1,200	\$ 382
Customer relationships	27,600	2,630	9,030
Tradenames	24,800	2,560	2,230
Goodwill	33,795	8,356	13,349
Deferred revenue	(164)		(2,380)
Net deferred taxes	(15,574)	(1,347)	
Net other assets	2,210	(224)	(110)
<b>Total purchase price, net of cash acquired</b>	<b>\$ 74,947</b>	<b>\$ 13,175</b>	<b>\$ 22,501</b>

**Other Acquisition-Related Fair Value Adjustments**

We have acquired companies in previous years for which acquisition-related contingent consideration was included in the purchase price and recorded at fair value. The liability established for the acquisition-related contingent consideration will continue to be re-evaluated and recorded at an estimated fair value based on the probabilities, as determined by management, of achieving the related targets. This evaluation will be performed until all of the targets have been met or terms of the agreement expire.

In July 2010, we purchased 100% of the outstanding stock of eReal Estate Integration, Inc. (eREI), which included an estimated cash payment payable upon the achievement of certain revenue targets (acquisition-related contingent consideration). The fair value of this acquisition-related contingent consideration was based on management's estimate of the fair value of the cash using a probability weighted discounted cash flow model on the achievement of certain revenue targets (a level 3 input). The cash payment has a maximum value of \$1.8 million. As of June 30, 2012, our liability for the estimated cash payment was \$0.7 million. During the three and six months ended June 30, 2012, we recognized losses of less than \$0.1 million and during the three and six months ended June 30, 2011, we recognized losses of less than \$0.1 million and \$0.1 million, respectively, due to changes in the estimated fair value of the cash acquisition-related contingent consideration.

**Pro Forma Results of Acquisitions**

## Edgar Filing: REALPAGE INC - Form 10-Q

The following table presents unaudited actual results of operations for the three and six months ended June 30, 2012 and pro forma results of operations for the three and six months ended June 30, 2011 as if the Vigilant, MTS, SLN and Compliance Depot acquisitions had occurred at the beginning of the prior year presented. The pro forma financial information for the three and six months ended June 30, 2011, respectively, includes the business combination accounting effects resulting from these acquisitions including: interest expense of \$0.1 million and \$0.2 million; tax benefit of \$1.1 million and \$2.3 million; and approximately \$1.1 million and \$2.1 million of amortization charges from acquired intangible assets as though the aforementioned companies were combined as of the beginning of fiscal year 2011. We prepared the pro forma financial information for the combined entities for comparative purposes only, and it is not indicative of what actual results would have been if the acquisitions had taken place at the beginning of the periods presented, or of future results:

**Table of Contents**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012 Actual	2011 Pro Forma	2012 Actual	2011 Pro Forma
(in thousands, except per share amounts)				
<b>Revenue:</b>				
On demand	\$ 74,938	\$ 63,511	\$ 145,656	\$ 122,921
On premise	\$ 1,261	\$ 1,628	\$ 2,677	\$ 3,273
Professional and other	\$ 2,593	\$ 2,968	\$ 4,876	\$ 5,934
<b>Total revenue</b>	<b>\$ 78,792</b>	<b>\$ 68,107</b>	<b>\$ 153,209</b>	<b>\$ 132,128</b>
Net loss	\$ (2,372)	\$ (1,411)	\$ (652)	\$ (3,752)
<b>Net loss per share:</b>				
Basic	\$ (0.03)	\$ (0.02)	\$ (0.01)	\$ (0.06)
Diluted	\$ (0.03)	\$ (0.02)	\$ (0.01)	\$ (0.06)

**4. Property, Equipment and Software**

Property, equipment and software consist of the following:

	June 30, 2012	December 31, 2011
(in thousands)		
Leasehold improvements	\$ 11,059	\$ 9,924
Data processing and communications equipment	41,383	38,926
Furniture, fixtures, and other equipment	11,190	9,680
Software	36,171	31,266
	99,803	89,796
Less: Accumulated depreciation and amortization	(68,350)	(61,822)
<b>Property, equipment and software, net</b>	<b>\$ 31,453</b>	<b>\$ 27,974</b>

Depreciation and amortization expense for property, equipment and software was \$3.5 million, \$3.2 million, \$6.9 million and \$6.4 million for the three months ended June 30, 2012 and 2011 and the six months ended June 2012 and 2011, respectively. This includes depreciation for assets purchased through capital leases.

**5. Goodwill and Other Intangible Assets**

The change in the carrying amount of goodwill for the six months ended June 30, 2012 is as follows:

	(in thousands)
Balance at December 31, 2011	\$ 129,292
Goodwill acquired	2,454
Other	(1,206)
<b>Balance at June 30, 2012</b>	<b>\$ 130,540</b>

Other intangible assets consisted of the following at June 30, 2012 and December 31, 2011:

Edgar Filing: REALPAGE INC - Form 10-Q

	Amortization Period	Carrying Amount	June 30, 2012		December 31, 2011		
			Accumulated Amortization	Net (in thousands)	Carrying Amount	Accumulated Amortization	Net
<b>Finite-lived intangible assets</b>							
Developed technologies	3 years	\$ 27,467	\$ (18,952)	\$ 8,515	\$ 25,963	\$ (14,847)	\$ 11,116
Customer relationships	1-10 years	75,383	(19,306)	56,077	74,233	(14,949)	59,284
Vendor relationships	7 years	5,650	(3,693)	1,957	5,650	(3,316)	2,334
<b>Total finite-lived intangible assets</b>		<b>108,500</b>	<b>(41,951)</b>	<b>66,549</b>	<b>105,846</b>	<b>(33,112)</b>	<b>72,734</b>
<b>Indefinite-lived intangible assets</b>							
Tradenames		39,574		39,574	39,574		39,574
<b>Total intangible assets</b>		<b>\$ 148,074</b>	<b>\$ (41,951)</b>	<b>\$ 106,123</b>	<b>\$ 145,420</b>	<b>\$ (33,112)</b>	<b>\$ 112,308</b>

Amortization of finite-lived intangible assets was \$4.4 million, \$4.0 million, \$8.8 million and \$7.6 million for the three months ended June 30, 2012 and 2011 and six months ended June 2012 and 2011, respectively.

---

## **Table of Contents**

### **6. Debt**

In December 2011, we entered into an Amended and Restated Credit Agreement ( Restated Agreement ) to amend our original credit facility. The Restated Agreement provides for a secured revolving credit facility in an aggregate principal amount of up to \$150.0 million, subject to a borrowing formula, with a sublimit of \$10.0 million for the issuance of letters of credit on our behalf. The Restated Agreement converted our outstanding term loan under the original credit facility into revolving loans. Revolving loans accrue interest at a per annum rate equal to, at the Company's option, either LIBOR or Wells Fargo's prime rate (or, if greater, the federal funds rate plus 0.50% or three month LIBOR plus 1.00%), in each case plus a margin ranging from 2.50% to 3.00%, in the case of LIBOR loans, and 0.00% to 0.25% in the case of prime rate loans, based upon the Company's senior leverage ratio. The interest is due and payable monthly, in arrears, for loans bearing interest at the prime rate and at the end of the applicable 1-, 2-, or 3-month interest period in the case of loans bearing interest as the adjusted LIBOR rate. Principal, together with all accrued and unpaid interest, is due and payable on December 30, 2015. Advances under the credit facility may be voluntarily prepaid, and must be prepaid with the proceeds of certain dispositions, extraordinary receipts and indebtedness and in full upon a change in control.

As of June 30, 2012 and December 31, 2011, we had \$35.0 million and \$50.3 million outstanding under our revolving line of credit, which approximates its fair value. As of June 30, 2012, \$115.0 million was available under our revolving line of credit and \$10.0 million was available for the issuance of letters of credit. We had unamortized debt issuance costs of \$1.1 million and \$1.3 million at June 30, 2012 and December 31, 2011, respectively. As of June 30, 2012, we were in compliance with our debt covenants.

### **7. Share-based Compensation**

In February 2012, we granted 696,150 options with an exercise price of \$20.01 which vest over four years with 75% vesting over 15 quarters and the remaining 25% vesting on the 16<sup>th</sup> quarter. We also granted 382,050 shares of restricted stock at \$20.01 which vest ratably over four years, 74,760 shares at \$20.01 that vest quarterly over one year and 4,365 shares at \$21.22 which vest over one year. All stock options and restricted stock were granted under the 2010 Equity Plan.

In April 2012, we granted 31,302 shares of restricted stock at \$19.17 which vest ratably over four years to our Board of Directors.

On May 8, 2012, we granted 240,124 options with an exercise price of \$18.10 which vest over four years with 75% vesting over 15 quarters and the remaining 25% vesting on the 16<sup>th</sup> quarter. We also granted 121,564 shares of restricted stock at \$18.10 which vest ratably over four years. Both stock options and restricted stock were granted under the 2010 Equity Plan. We also granted 70,000 shares of performance restricted stock at \$18.10 to certain employees which vest as product specific revenue targets are achieved.

### **8. Commitments and Contingencies**

We have agreements whereby we indemnify our officers and directors for certain events or occurrences while the officer or director is or was serving at our request in such capacity. The term of the indemnification period is for the officer or director's lifetime. The maximum potential amount of future payments we could be required to make under these indemnification agreements is unlimited; however, we have a director and officer insurance policy that limits our exposure and enables us to recover a portion of any future amounts paid. As a result of our insurance policy coverage, we believe the estimated fair value of these indemnification agreements is minimal. Accordingly, we had no liabilities recorded for these agreements as of June 30, 2012 or December 31, 2011.

In the ordinary course of our business, we enter into standard indemnification provisions in our agreements with our customers. Pursuant to these provisions, we indemnify our customers for losses suffered or incurred in connection with third-party claims that our products infringed upon any U.S. patent, copyright, trademark or other intellectual property right. Where applicable, we generally limit such infringement indemnities to those claims directed solely to our products and not in combination with other software or products. With respect to our products, we also generally reserve the right to resolve such claims by designing a non-infringing alternative, by obtaining a license on reasonable terms, or by terminating our relationship with the customer and refunding the customer's fees.

The potential amount of future payments to defend lawsuits or settle indemnified claims under these indemnification provisions is unlimited in certain agreements; however, we believe the estimated fair value of these indemnity provisions is minimal, and, accordingly, we had no liabilities recorded for these agreements as of June 30, 2012 or December 31, 2011.

### ***Litigation***

From time to time, in the normal course of our business, we are a party to litigation matters and claims. Litigation can be expensive and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict and our view of these



## Edgar Filing: REALPAGE INC - Form 10-Q

matters may change in the future as the litigation and events related thereto unfold. We expense legal fees as incurred. Insurance recoveries associated with legal costs incurred are recorded when they are deemed probable of recovery.

## Table of Contents

We review the status of each matter and record a provision for a liability when we consider both that it is probable that a liability has been incurred and that the amount of the loss can be reasonably estimated. These provisions are reviewed quarterly and adjusted as additional information becomes available. If either or both of the criteria are not met, we assess whether there is at least a reasonable possibility that a loss, or additional losses beyond those already accrued, may be incurred. If there is a reasonable possibility that a material (or additional material loss in excess of any accrual) loss may be incurred, we disclose an estimate of the amount of loss or range of losses, either individually or in the aggregate, as appropriate, if such an estimate can be made, or disclose that an estimate of loss cannot be made. An unfavorable outcome in any legal matter, if material, could have an adverse effect on our operations, financial position, liquidity and results of operations.

On January 24, 2011, Yardi Systems, Inc. ( "Yardi" ) filed a lawsuit in the U.S. District Court for the Central District of California against RealPage, Inc. and DC Consulting, Inc. (this lawsuit and the related litigation, the "Yardi Lawsuit" ) and filed a First Amended Complaint on August 12, 2011. On March 28, 2011, we filed an answer and counterclaims, on May 18, 2011, we filed amended counterclaims, on September 2, 2011, we filed Second Amended Counterclaims and on September 12, 2011, we filed an answer to Yardi's First Amended Complaint. Yardi filed a pending motion to dismiss several of our counterclaims which we opposed. On February 13, 2012, the Court denied Yardi's motion with respect to all claims except for a portion of one of our claims for intentional interference with contract, as to which dismissal was granted. On July 1, 2012, the Company and Yardi entered into a settlement agreement (the "Settlement Agreement" ) resolving all outstanding litigation between the parties. The Settlement Agreement also includes a license of certain Yardi intellectual property to the Company and a license of certain of our intellectual property to Yardi.

The Settlement Agreement is a multiple element arrangement for accounting purposes. For the multiple element arrangement, the Company identified each element of the arrangement and determined when those elements should be recognized. The Company allocated the consideration to each element using the estimated fair value of the elements. The Company considered several factors in determining the accounting fair value of the elements of the Settlement Agreement. The inputs and assumptions used in this valuation were from a market participant perspective and included projected revenue, estimated discount rates, useful lives and income tax rates, among others. The development of a number of these inputs and assumptions in the model requires a significant amount of management judgment and is based upon a number of factors. Changes in any number of these assumptions may have had a substantial impact on the fair value as assigned to each element. These inputs and assumptions represent management's best estimates at the time of the transaction. Based on the estimated fair value, we have recognized the following: \$3.0 million for the license from Yardi, which will be capitalized upon execution of the Settlement Agreement and amortized as a cost of revenue over its estimated useful life, beginning in July 2012; \$1.0 million for the license sold to Yardi, which will be recognized as revenue over the estimated useful life of the technology, beginning in July 2012; and \$8.5 million inclusive of the settlement and other related legal costs, which were expensed in the second quarter of 2012.

In connection with the Yardi Lawsuit, the Company made claims for reimbursement against each of its primary and excess layer general liability and professional liability insurance carriers. Each of our primary and excess layer professional liability insurance carriers other than Homeland Insurance of New York ( "Homeland" ) reimbursed the Company up to each of its policy limits. On July 19, 2012, we became aware of assertions by one of our primary layer insurance carriers that such carrier no longer considered the previously reimbursed \$5.0 million payment covered under such policy, and that the carrier demanded reimbursement of the \$5.0 million payment that the carrier had previously reimbursed to us. The Company disputes this assertion by the carrier. We intend to defend these allegations and to pursue coverage and other appropriate relief in connection with this insurance policy. It is not possible to predict the outcome of this insurance matter, and as such, we have not recorded a contingent liability as we believe an unfavorable outcome is not probable as of the date of this filing.

In addition, in connection with the Yardi Lawsuit, the Company has an excess professional liability insurance policy with Homeland that provides an additional \$5.0 million of coverage above the amounts previously reimbursed to us. The Company made claims for reimbursement under the Homeland policy with respect to the Yardi Lawsuit, but Homeland denied such claims and never made payment to us. On May 30, 2012, Homeland filed a motion for declaratory judgment against the Company in the United States District Court for the Northern District of Texas seeking a determination by the court that Homeland's policy does not provide coverage for amounts incurred in connection with the Yardi Lawsuit. We have not recorded any amounts as recoverable in relation to the Homeland insurance policy as of June 30, 2012.

We are involved in other litigation matters not listed above but we do not consider the matters to be material either individually or in the aggregate at this time. Our view of the matters not listed may change in the future as the litigation and events related thereto unfold.

## **9. Net Income (Loss) Per Share**

Basic net income (loss) per share is computed by dividing the net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed by using the weighted average number of common shares outstanding, including potential dilutive shares of common stock assuming the dilutive effect of outstanding stock options and restricted stock using the treasury stock method. Weighted average shares from common share equivalents in the amount of 2,236,933, 2,456,022, and 3,541,946 shares were excluded from the dilutive shares outstanding because their effect was anti-dilutive for the three and six months ended June 30, 2012 and

Edgar Filing: REALPAGE INC - Form 10-Q

the six months ended June 30, 2011, respectively.

The following table presents the calculation of basic and diluted net income (loss) per share:

**Table of Contents**

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2012	2011	2012	2011
(in thousands, except per share amounts)				
<b>Numerator:</b>				
Net income (loss)	\$ (2,372)	\$ 282	\$ (652)	\$ (366)
<b>Denominator:</b>				
<b>Basic:</b>				
Weighted average common shares used in computing basic net income (loss) per share	71,102	68,673	70,846	67,741
<b>Diluted:</b>				
<b>Add weighted average effect of dilutive securities:</b>				
Stock options and restricted stock		3,339		
<b>Weighted average common shares used in computing diluted net income (loss) per share</b>				
	71,102	72,012	70,846	67,741
<b>Net income (loss) per common share:</b>				
<b>Basic</b>				
	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)
<b>Diluted</b>				
	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)

**10. Income Taxes**

We make estimates and judgments in determining income tax expense for financial statement purposes. These estimates and judgments occur in the calculation of certain tax assets and liabilities, which arise from differences in the timing of recognition of revenue and expense for tax and financial statement purposes.

Our provision for income taxes in interim periods is based on our estimated annual effective tax rate. We record cumulative adjustments in the quarter in which a change in the estimated annual effective rate is determined. The estimated annual effective tax rate calculation does not include the effect of discrete events that may occur during the year. The effect of these events, if any, is recorded in the quarter in which the event occurs.

**11. Related Party**

Beginning in 2012, Scott S. Ingraham began serving on our board of directors. He is an investor in Zuma Capital Greenville LLC ( ZCG ), which is a minority member of the parent entity of the entities from which we acquired certain assets relating to the LevelOne business in November 2010. Pursuant to the LevelOne acquisition agreement, we held back a portion of the purchase price for a period of time in order to ensure payment for any claims that arose post-acquisition, which amount, net of claims and adjustments, was paid in May 2012. ZCG s interest in this pay-out, based on its ownership percentage of such parent entity, was \$0.5 million and Mr. Ingraham s interest in this pay-out, was approximately \$0.2 million. Mr. Ingraham also serves on the Board of Trust Managers of Camden Property Trust, one of our larger customers.

**12. Subsequent Event**

In July 2012, we acquired all of the issued and outstanding shares of Rent Mine Online, Inc. for a purchase price which consists of a cash payment of \$5.5 million at closing, a deferred payment of up to \$3.5 million and a contingent deferred earn out payment of up to 300,000 shares of our common stock, payable based on the achievement of specified milestones on or before December 31, 2014. The acquisition of Rent Mine Online, Inc. expands our resident referral capabilities into the multifamily residential rental housing market. Due to the timing of this acquisition, the purchase price allocation was not complete as of the date of this filing due to the pending completion of the valuation of intangible assets.

## **Table of Contents**

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

*This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (which Sections were adopted as part of the Private Securities Litigation Reform Act of 1995). Statements preceded by, followed by or that otherwise include the words anticipates, believes, could, seeks, estimates, expects, intends, may, plans, potential, predicts, projects, should, will, would or similar expressions and the negatives of those terms are generally forward-looking in nature and not historical facts. These forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any anticipated results, performance or achievements. Factors that might cause or contribute to such differences include, but are not limited to those discussed in the section entitled Risk Factors in Part II, Item 1A of this report. You should carefully review the risks described herein and in the other documents we file from time to time with the Securities and Exchange Commission (SEC), including our Annual Report on Form 10-K for fiscal year 2011. You should not place undue reliance on forward-looking statements herein, which speak only as of the date of this report. Except as required by law, we disclaim any intention, and undertake no obligation, to revise any forward-looking statements, whether as a result of new information, a future event or otherwise.*

### **Overview**

RealPage, Inc., a Delaware corporation, and its subsidiaries, (the Company or we or us) is a leading provider of on demand software solutions for the rental housing industry. Our broad range of property management solutions enables owners and managers of single-family and a wide variety of multi-family rental property types to manage their marketing, pricing, screening, leasing, accounting, purchasing and other property operations. Our on demand software solutions are delivered through an integrated software platform that provides a single point of access and a shared repository of prospect, resident and property data. By integrating and streamlining a wide range of complex processes and interactions among the rental housing ecosystem of owners, managers, prospects, residents and service providers, our platform helps optimize the property management process and improves the experience for all of these constituents.

Our solutions enable property owners and managers to increase revenues and reduce operating costs through higher occupancy, improved pricing methodologies, new sources of revenue from ancillary services, improved collections and more integrated and centralized processes. As of June 30, 2012, over 8,200 customers used one or more of our on demand software solutions to help manage the operations of approximately 7.5 million rental housing units. Our customers include each of the ten largest multi-family property management companies in the United States, ranked as of January 1, 2011 by the National Multi Housing Council, based on number of units managed.

We sell our solutions through our direct sales organization. Our total revenues were approximately \$78.8 million, \$61.6 million, \$153.2 million and \$119.2 million for the three months ended June 30, 2012 and 2011 and the six months ended June 2012 and 2011, respectively. In the same periods, we had operating income (loss) of approximately \$(3.3) million, \$1.2 million, \$0.1 million and \$1.2 million, respectively, and net income (loss) of approximately \$(2.4) million, \$0.3 million, \$(0.7) million and \$(0.4) million, respectively.

Our company was formed in 1998 to acquire Rent Roll, Inc., which marketed and sold on premise property management systems for the conventional and affordable multi-family rental housing markets. In June 2001, we released OneSite, our first on demand property management system. Since 2002, we have expanded our on demand software solutions to include a number of software-enabled value-added services that provide complementary sales and marketing, asset optimization, risk mitigation, billing and utility management and spend management capabilities. In connection with this expansion, we have allocated greater resources to the development and infrastructure needs of developing and increasing sales of our suite of on demand software solutions. In addition, since July 2002, we have completed 19 acquisitions of complementary technologies to supplement our internal product development and sales and marketing efforts and expand the scope of our solutions, the types of rental housing properties served by our solutions and our customer base.

### **New Product Families**

In August 2011, we announced our new product family, LeaseStar, which will consolidate and integrate products and services related to our acquisitions of eREI, LevelOne, SeniorLiving.net, MTS and our suite of products and services historically branded as Crossfire. We believe the LeaseStar product family will unify major organic and paid lead channels into a single marketplace where consumers can find a rental unit and transact business by viewing real time availability, pricing, pre-qualify and lease online.

In February 2012, we announced our new product family, RealPage Senior Living. We believe RealPage Senior Living will help owners and managers attract more residents and improve the living and care experience enjoyed by those residents.

### **Recent Acquisitions**



---

## **Table of Contents**

In May 2011, we acquired substantially all of the assets of Compliance Depot LLC ( Compliance Depot ) for approximately \$22.5 million which included a cash payment of \$19.2 million and three deferred payments of \$1.1 million each payable six, twelve and eighteen months after the acquisition date. The acquisition of Compliance Depot expands our ability to provide vendor risk management and compliance software for the rental housing industry. Interfacing with vendors through a branded platform, Compliance Depot allows property managers and owners to: track compliance with vendor obligations to carry workers compensation and general liability insurance, identify vendor bankruptcy filings, liens, criminal records, collections and professional license verification, confirm federal regulation compliance, such as The Patriot Act; as well as manage contractual agreements and federal and state tax documents.

In July 2011, we acquired Senior-Living.com, Inc., operating under the name SeniorLiving.net ( SLN ), for a purchase price consisting of a cash payment of \$4.0 million at closing, additional cash payments of \$0.5 million, half of which is due on each of the first and second anniversaries of the acquisition date, and a deferred earn out payment of up to \$0.5 million in cash and up to 400,000 shares of our common stock, in each case payable based on the achievement of specified milestones on or before June 30, 2014. The acquisition of SLN expands our lead generation capabilities into the senior living rental housing market.

In August 2011, we acquired Multifamily Technology Solutions, Inc. ( MTS ), which owns the Internet listing service for rental properties called MyNewPlace, pursuant to an Agreement and Plan of Merger. MTS continued as the surviving corporation of the Merger and a wholly owned subsidiary of RealPage. We acquired MTS for a purchase price of \$74.9 million, net of cash acquired, comprised of approximately \$64.0 million in cash, 294,770 shares of RealPage restricted common stock and the assumption of MTS stock options exercisable for 349,693 shares of RealPage common stock. The acquisition of MTS adds a pay-for-performance Internet listing service, expands our suite of SAAS lead generation and management tools and service delivery capabilities.

In January 2012, we acquired substantially all of the operating assets of Vigilant, Incorporated ( Vigilant ). A provider of assisted living software-as-a-service, Vigilant products allow assisted living communities to monitor and schedule detailed care, manage labor costs, provide accurate billing as well as compliance tools through its comprehensive compliance module. We acquired Vigilant for a purchase price of \$5.0 million consisting of a cash payment of \$4.0 million and two additional cash payments of up to \$0.5 million each due 12 months and 24 months after the acquisition date.

In July 2012, we acquired all of the issued and outstanding shares of Rent Mine Online, Inc. for a purchase price which consists of a cash payment of \$5.5 million at closing, a deferred payment of up to \$3.5 million and a contingent deferred earn out payment of up to 300,000 shares of our common stock, payable based on the achievement of specified milestones on or before December 31, 2014. The acquisition of Rent Mine Online, Inc. expands our resident referral capabilities into the multifamily residential rental housing market. Due to the timing of this acquisition, the purchase price allocation was not complete as of the date of this filing due to the pending completion of the valuation of intangible assets.

### **Critical Accounting Policies and Estimates**

The preparation of our condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses and related disclosures. We base these estimates and assumptions on historical experience or on various other factors that we believe to be reasonable and appropriate under the circumstances. We reconsider and evaluate our estimates and assumptions on an on-going basis. Accordingly, actual results may differ significantly from these estimates

We believe that the following critical accounting policies involve our more significant judgments, assumptions and estimates, and therefore, could have the greatest potential impact on our condensed consolidated financial statements:

Revenue recognition;

Accounts receivable;

Business combinations;

Goodwill and other intangible assets with indefinite lives;

Impairment of long-lived assets;

Fair value measurements;

Intangible assets;

Stock-based compensation;

Income taxes; and

Capitalized product development costs.

A full discussion of our critical accounting policies, which involve significant management judgment, appears in our Form 10-K under Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates. For further information regarding our business, industry trends, accounting policies and estimates, and risks and uncertainties, refer to our Form 10-K.



---

## **Table of Contents**

### **Key Components of Our Results of Operations**

#### ***Revenue***

We derive our revenue from three primary sources: our on demand software solutions; our on premise software solutions; and our professional and other services.

*On demand revenue.* Revenue from our on demand software solutions is comprised of license and subscription fees relating to our on demand software solutions, typically licensed for one year terms, commission income from sales of renters insurance policies, and transaction fees for certain on demand software solutions, such as payment processing, spend management and billing services. Typically, we price our on demand software solutions based primarily on the number of units or beds the customer manages with our solutions. For our insurance based solutions, our agreement provides for a fixed commission on earned premiums related to the policies sold by us. The agreement also provides for a contingent commission to be paid to us in accordance with the agreement. This agreement provides for a calculation that considers, on the policies sold by us, earned premiums less i) earned agent commissions; ii) a percent of premium retained by our underwriting partner; iii) incurred losses; iv) profit retained by our underwriting partner during the time period. Our estimate of our contingent commission revenue considers historical loss experience on the policies sold by us. For our transaction-based solutions, we price based on a fixed rate per transaction.

*On premise revenue.* Our on premise software solutions are distributed to our customers and maintained locally on the customers' hardware. Revenue from our on premise software solutions is comprised of license fees under term and perpetual license agreements. Typically, we have licensed our on premise software solutions pursuant to term license agreements with an initial term of one year that include maintenance and support. Customers can renew their term license agreement for additional one-year terms at renewal price levels. In February 2010, we completed a strategic acquisition of assets that included on premise software solutions that were historically marketed and sold pursuant to perpetual license agreements and related maintenance agreements.

We no longer actively market our legacy on premise software solutions to new customers, and only license our on premise software solutions to a small portion of our existing on premise customers as they expand their portfolio of rental housing properties. While we intend to support our recently acquired on premise software solutions, we expect that many of the customers who license these solutions will transition to our on demand software solutions over time.

*Professional and other revenue.* Revenue from professional and other services consists of consulting and implementation services, training, and other ancillary services. Professional and other services engagements are typically time and material based.

#### ***Cost of Revenue***

Cost of revenue consists primarily of personnel costs related to our operations, support services, training and implementation services, expenses related to the operation of our data center and fees paid to third-party service providers. Personnel costs include salaries, bonuses, stock-based compensation and employee benefits. Cost of revenue also includes an allocation of facilities costs, overhead costs and depreciation, as well as amortization of acquired technology related to strategic acquisitions and amortization of capitalized development costs. We allocate facilities, overhead costs and depreciation based on headcount.

#### ***Operating Expenses***

We classify our operating expenses into three categories: product development, sales and marketing, and general and administrative. Our operating expenses primarily consist of personnel costs, costs for third-party contracted development, marketing, legal, accounting and consulting services and other professional service fees. Personnel costs for each category of operating expenses include salaries, bonuses, stock-based compensation and employee benefits for employees in that category. In addition, our operating expenses include an allocation of our facilities costs, overhead costs and depreciation based on headcount for that category, as well as amortization of purchased intangible assets resulting from our acquisitions.

*Product development.* Product development expense consists primarily of personnel costs for our product development employees and executives and fees to contract development vendors. Our product development efforts are focused primarily on increasing the functionality and enhancing the ease of use of our on demand software solutions and expanding our suite of on demand software solutions. In 2008 and 2011, we established a product development and service center in Hyderabad, India and Manila, Philippines, respectively, to take advantage of strong technical talent at lower personnel costs compared to the United States.

## Edgar Filing: REALPAGE INC - Form 10-Q

*Sales and marketing.* Sales and marketing expense consists primarily of personnel costs for our sales, marketing and business development employees and executives, travel and entertainment and marketing programs. Marketing programs consist of amounts paid for online advertising, including search engine optimization ( SEO ) and search engine marketing ( SEM ), renter s insurance and other advertising, tradeshow, user conferences, public relations, industry sponsorships and affiliations and product marketing. In addition, sales and marketing expense includes amortization of certain purchased intangible assets, including customer relationships and key vendor and supplier relationships obtained in connection with our acquisitions.

**Table of Contents**

*General and administrative.* General and administrative expense consists of personnel costs for our executive, finance and accounting, human resources, management information systems and legal personnel, as well as legal, accounting and other professional service fees and other corporate expenses.

**Key Business Metrics**

In addition to traditional financial measures, we monitor our operating performance using a number of financially and non-financially derived metrics that are not included in our condensed consolidated financial statements. We monitor the key performance indicators as follows:

*On demand revenue.* This metric represents the license and subscription fees relating to our on demand software solutions, typically licensed for one year terms, commission income from sales of renters insurance policies and transaction fees for certain of our on demand software solutions. We consider on demand revenue to be a key business metric because we believe the market for our on demand software solutions represents the largest growth opportunity for our business.

*On demand revenue as a percentage of total revenue.* This metric represents on demand revenue for the period presented divided by total revenue for the same period. We use on demand revenue as a percentage of total revenue to measure our success in executing our strategy to increase the penetration of our on demand software solutions and expand our recurring revenue streams attributable to these solutions. We expect our on demand revenue to remain a significant percentage of our total revenue although the actual percentage may vary from period to period due to a number of factors, including the timing of acquisitions, professional and other revenue and on premise perpetual license sales and maintenance fees resulting from our February 2010 acquisition.

*Ending on demand units.* This metric represents the number of rental housing units managed by our customers with one or more of our on demand software solutions at the end of the period. We use ending on demand units to measure the success of our strategy of increasing the number of rental housing units managed with our on demand software solutions. Property unit counts are provided to us by our customers as new sales orders are processed. Property unit counts may be adjusted periodically as information related to our customers' properties is updated or supplemented, which could result in adjusting the number of units previously reported.

*Non-GAAP on demand revenue.* This metric represents on demand revenue adjusted to reverse the effect of the write down of deferred revenue associated with purchase accounting for strategic acquisitions. We use this metric to evaluate our on demand revenue as we believe its inclusion provides a more accurate depiction of on demand revenue arising from our strategic acquisitions.

The following provides a reconciliation of non-GAAP on demand revenue:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
On demand revenue	\$ 74,938	\$ 57,039	\$ 145,656	\$ 109,976
Acquisition-related deferred revenue adjustment	2	244	83	244
Non-GAAP on demand revenue	\$ 74,940	\$ 57,283	\$ 145,739	\$ 110,220

*Non-GAAP on demand revenue per average on demand unit.* This metric represents non-GAAP on demand revenue for the period presented divided by average on demand units for the same period. For interim periods, the calculation is performed on an annualized basis. We calculate average on demand units as the average of the beginning and ending on demand units for each quarter in the period presented. We monitor this metric to measure our success in increasing the number of on demand software solutions utilized by our customers to manage their rental housing units, our overall revenue and profitability.

*Adjusted EBITDA.* We define this metric as net (loss) income plus depreciation and asset impairment; amortization of intangible assets; interest expense, net; income tax expense (benefit); stock-based compensation expense and acquisition-related expense. Beginning in 2011, Adjusted EBITDA excludes litigation-related expenses pertaining to the Yardi litigation as discussed in Part II, Item 1, Legal Proceedings. Beginning in the second quarter of 2011, Adjusted EBITDA includes acquisition-related deferred revenue adjustments. We believe that the use of Adjusted EBITDA is useful in evaluating our operating performance because it excludes certain non-cash expenses, including depreciation, amortization and stock-based compensation. Adjusted EBITDA is not determined in accordance with accounting principles generally accepted in the United States, or GAAP, and should not be considered as a substitute for or superior to financial measures determined in accordance with GAAP. For

## Edgar Filing: REALPAGE INC - Form 10-Q

further discussion regarding Adjusted EBITDA and a reconciliation of Adjusted EBITDA to net income, refer to Reconciliation of Non-GAAP Financial Measures herein. Our Adjusted EBITDA grew from approximately \$13.7 million and \$25.9 million for the three and six months ended June 30, 2011 to approximately \$17.4 million and \$33.8 million for the three and six months ended June 30, 2012 as a result of our efforts to expand market share and increase revenue.

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

The following tables set forth our results of operations for the specified periods. The period-to-period comparison of financial results is not necessarily indicative of future results.

**Condensed Consolidated Statements of Operations Data**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenue:</b>				
On demand	\$ 74,938	\$ 57,039	\$ 145,656	\$ 109,976
On premise	1,261	1,628	2,677	3,273
Professional and other	2,593	2,968	4,876	5,934
<b>Total revenue</b>	<b>78,792</b>	<b>61,635</b>	<b>153,209</b>	<b>119,183</b>
Cost of revenue(1)	31,848	25,810	62,461	50,493
<b>Gross profit</b>	<b>46,944</b>	<b>35,825</b>	<b>90,748</b>	<b>68,690</b>
<b>Operating expense:</b>				
Product development(1)	11,738	10,537	23,051	20,853
Sales and marketing(1)	18,588	14,510	35,394	27,304
General and administrative(1)	19,946	9,574	32,249	19,350
<b>Total operating expense</b>	<b>50,272</b>	<b>34,621</b>	<b>90,694</b>	<b>67,507</b>
<b>Operating income (loss)</b>	<b>(3,328)</b>	<b>1,204</b>	<b>54</b>	<b>1,183</b>
Interest expense and other, net	(577)	(732)	(1,213)	(1,898)
<b>Income (loss) before income taxes</b>	<b>(3,905)</b>	<b>472</b>	<b>(1,159)</b>	<b>(715)</b>
Income tax expense (benefit)	(1,533)	190	(507)	(349)
<b>Net income (loss)</b>	<b>\$ (2,372)</b>	<b>\$ 282</b>	<b>\$ (652)</b>	<b>\$ (366)</b>
<b>Net income (loss) per share</b>				
Basic	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)
Diluted	\$ (0.03)	\$ 0.00	\$ (0.01)	\$ (0.01)
<b>Weighted average shares used in computing net income (loss) per share</b>				
Basic	71,102	68,673	70,846	67,741
Diluted	71,102	72,012	70,846	67,741

(1) Includes stock-based compensation expense as follows:

Cost of revenue	\$ 750	\$ 312	\$ 1,439	\$ 610
Product development	1,002	1,105	2,064	2,085
Sales and marketing	1,032	2,627	1,769	5,360
General and administrative	1,532	925	3,032	1,767

The following table sets forth our results of operations for the specified periods as a percentage of our revenue for those periods. The period-to-period comparison of financial results is not necessarily indicative of future results.

Edgar Filing: REALPAGE INC - Form 10-Q

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
(as a percentage of total revenue)				
<b>Revenue:</b>				
On demand	95.1%	92.5%	95.1%	92.3%
On premise	1.6	2.6	1.7	2.7
Professional and other	3.3	4.9	3.2	5.0
<b>Total revenue</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
Cost of revenue	40.4	41.9	40.8	42.4
<b>Gross profit</b>	<b>59.6</b>	<b>58.1</b>	<b>59.2</b>	<b>57.6</b>
<b>Operating expense:</b>				
Product development	14.9	17.1	15.0	17.5
Sales and marketing	23.6	23.5	23.1	22.9
General and administrative	25.3	15.5	21.0	16.2
<b>Total operating expenses</b>	<b>63.8</b>	<b>56.1</b>	<b>59.1</b>	<b>56.6</b>
<b>Operating income (loss)</b>	<b>(4.2)</b>	<b>2.0</b>	<b>0.1</b>	<b>1.0</b>
Interest expense and other, net	(0.7)	(1.2)	(0.8)	(1.6)
<b>Net income (loss) before taxes</b>	<b>(4.9)</b>	<b>0.8</b>	<b>(0.7)</b>	<b>(0.6)</b>
Income tax expense (benefit)	(1.9)	0.3	(0.3)	(0.3)
<b>Net income (loss)</b>	<b>(3.0)</b>	<b>0.5</b>	<b>(0.4)</b>	<b>(0.3)</b>

**Table of Contents****Three and Six Months Ended June 30, 2012 compared to Three and Six Months Ended June 30, 2011****Revenue**

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012	2011	Change	% Change	2012	2011	Change	% Change
(in thousands, except dollar per unit data)								
<b>Revenue:</b>								
On demand	\$ 74,938	\$ 57,039	\$ 17,899	31.4%	\$ 145,656	\$ 109,976	\$ 35,680	32.4%
On premise	1,261	1,628	(367)	(22.5)	2,677	3,273	(596)	(18.2)
Professional and other	2,593	2,968	(375)	(12.6)	4,876	5,934	(1,058)	(17.8)
<b>Total revenue</b>	<b>\$ 78,792</b>	<b>\$ 61,635</b>	<b>\$ 17,157</b>	<b>27.8</b>	<b>\$ 153,209</b>	<b>\$ 119,183</b>	<b>\$ 34,026</b>	<b>28.5</b>
<b>On demand unit metrics:</b>								
Ending on demand units	7,537	6,381	1,156	18.1	7,537	6,381	1,156	18.1
Average on demand units	7,484	6,270	1,214	19.4	7,425	6,191	1,234	19.9
Non-GAAP on demand revenue	\$ 74,940	\$ 57,283	\$ 17,657	30.8	\$ 145,739	\$ 110,220	\$ 35,519	32.2
Non-GAAP on demand revenue per average on demand unit	\$ 40.05	\$ 36.54	\$ 3.51	9.6	\$ 39.26	\$ 35.61	\$ 3.65	10.2

The changes in total revenue for the three and six months ended June 30, 2012 and 2011 are due to the following changes in our three revenue components:

*On demand revenue.* Our on demand revenue increased for the three and six months ended June 30, 2012 as compared to the same periods in 2011, primarily due to an increase in rental property units managed with our on demand solutions and an increase in the number of our on demand solutions utilized by our existing customer base, combined with revenue contributed from our strategic acquisitions of Compliance Depot, SLN, MTS and Vigilant.

*On premise revenue.* On premise revenue decreased for the three and six months ended June 30, 2012 as compared to the same periods in 2011. We no longer actively market our on premise software solutions to new customers, and only license our on premise software solutions to a small portion of our existing on premise customers as they expand their portfolio of rental housing properties. While we continue to support our recently acquired on premise software solutions, we expect that many of the customers who license these solutions will transition to our on demand software solutions over time. As a result, our on premise revenue has declined during the three months ended June 30, 2012 as compared to the same period in 2011. We expect this trend to continue.

*Professional and other revenue.* Professional and other services revenue decreased for the three and six months ended June 30, 2012 as compared to the same periods in 2011, primarily due to a decrease in revenue from training and consulting services.

*On demand unit metrics.* As of June 30, 2012, our on demand solutions were utilized in the management of 7.5 million rental property units, representing an increase compared to June 30, 2011. The increase in the number of rental property units managed by one or more of our on demand solutions was due to new customer sales and marketing efforts and our strategic acquisitions of MTS and Vigilant contributing approximately 7.2% of ending on demand units as of June 30, 2012.

For the three and six months ended June 30, 2012, our annualized non-GAAP on demand revenue per average on demand unit increased compared to the prior year periods, primarily due to improved penetration of our on demand solutions into our customer base and revenue contributed from our strategic acquisitions.

**Cost of Revenue**

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012	2011	Change	% Change	2012	2011	Change	% Change

Edgar Filing: REALPAGE INC - Form 10-Q

	(in thousands)							
Cost of revenue	\$ 27,860	\$ 22,060	\$ 5,800	26.3%	\$ 54,470	\$ 43,077	\$ 11,393	26.4%
Depreciation and amortization	3,988	3,750	238	6.3	7,991	7,416	575	7.8
Total cost of revenue	\$ 31,848	\$ 25,810	\$ 6,038	23.4	\$ 62,461	\$ 50,493	\$ 11,968	23.7



**Table of Contents**

*Cost of revenue.* The increase in cost of revenue for the three months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$1.9 million increase from costs related to investments in infrastructure and other support services to support the increased sales of our solutions; a \$3.5 million increase in personnel expense primarily related to our 2011 and 2012 acquisitions and associated costs to support our growth initiatives; a \$0.1 million increase in non-cash amortization of acquired technology; a \$0.1 million increase in property and equipment depreciation expense resulting from expanding our infrastructure to support revenue delivery activities; and a \$0.4 million increase in stock-based compensation related to our professional services and datacenter operations personnel. The decrease in cost of revenue as a percentage of total revenue was primarily the result of leveraging our fixed cost base, which was partially offset by an increase in costs as a result of our 2011 and 2012 acquisitions.

The increase in cost of revenue for the six months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$4.0 million increase from costs related to investments in infrastructure and other support services to support the increased sales of our solutions; a \$6.6 million increase in personnel expense primarily related to our 2011 and 2012 acquisitions and associated costs to support our growth initiatives; a \$0.4 million increase in non-cash amortization of acquired technology as a result of our 2011 and 2012 acquisitions; a \$0.2 million increase in property and equipment depreciation expense resulting from expanding our infrastructure to support revenue delivery activities; and a \$0.8 million increase in stock-based compensation related to our professional services and datacenter operations personnel. The decrease in cost of revenue as a percentage of total revenue was primarily the result of leveraging our fixed cost base, which was partially offset by an increase in costs as a result of our 2011 and 2012 acquisitions.

**Operating Expenses**

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012	2011	Change	% Change	2012	2011	Change	% Change
	(in thousands)							
Product development	\$ 11,132	\$ 10,076	\$ 1,056	10.5%	\$ 21,865	\$ 19,906	\$ 1,959	9.8%
Depreciation and amortization	606	461	145	31.5	1,186	947	239	25.2
Total product development expense	\$ 11,738	\$ 10,537	\$ 1,201	11.4	\$ 23,051	\$ 20,853	\$ 2,198	10.5

*Product development.* The increase in product development expense for the three months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$0.8 million increase in personnel expense and consulting fees primarily related to our 2011 and 2012 acquisitions and associated costs to support our growth initiatives; a \$0.2 million increase in consulting fees; and a \$0.2 million increase in other general product development expense.

The increase in product development expense for the six months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$0.8 million increase in facilities expenses; a \$0.7 million increase in personnel expense and consulting fees primarily related to our 2011 and 2012 acquisitions and associated costs to support our growth initiatives; a \$0.4 million increase in consulting fees; a \$0.2 million increase in depreciation expense and a \$0.1 million increase in other general product development expense.

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012	2011	Change	% Change	2012	2011	Change	% Change
	(in thousands)							
Sales and marketing	\$ 15,975	\$ 12,005	\$ 3,970	33.1%	\$ 30,097	\$ 22,701	\$ 7,396	32.6%
Depreciation and amortization	2,613	2,505	108	4.3	5,297	4,603	694	15.1
Total sales and marketing expense	\$ 18,588	\$ 14,510	\$ 4,078	28.1	\$ 35,394	\$ 27,304	\$ 8,090	29.6

*Sales and marketing.* The increase in sales and marketing expense for the three months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$2.5 million increase marketing program expense, primarily related to an increase in SEO and SEM activity driven by our acquisitions of MTS and SLN; a \$2.3 million increase in personnel expense related to the increase of sales force head count as a result of our 2011 and 2012 acquisitions and overall company growth; a \$0.4 million increase in information technology expenses; a \$0.1 million increase in non-cash amortization of acquired technology; and a \$0.4 million increase in other general sales and marketing expense, offset by a decrease of \$1.6 million in share-based compensation expense resulting from certain performance-based restricted stock awards that were previously

expected to vest.

The increase in sales and marketing expense for the six months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$5.0 million increase in marketing program expense, primarily related to an increase in SEO and SEM activity driven by our acquisitions of MTS and SLN; a \$4.7 million increase in personnel expense related to sales personnel added as a result of our 2011 and 2012 acquisitions and overall company growth; a \$0.6 million increase in non-cash amortization of acquired technology as a result of our 2011 and 2012 acquisitions; a \$0.6 million increase in information technology expenses; a \$0.2 million increase in travel related expenses; a \$0.1 million increase in depreciation expense; and a \$0.5 million increase in other general sales and marketing expense. These increases were partially offset by a decrease of \$3.6 million in stock-based compensation due to certain performance-based restricted stock awards that were previously expected to vest.

**Table of Contents**

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012	2011	Change	% Change	2012	2011	Change	% Change
	(in thousands)							
General and administrative	\$ 19,294	\$ 9,047	\$ 10,247	113.3%	\$ 30,986	\$ 18,300	\$ 12,686	69.3%
Depreciation and amortization	652	527	125	23.7	1,263	1,050	213	20.3
<b>Total general and administrative expense</b>	<b>\$ 19,946</b>	<b>\$ 9,574</b>	<b>\$ 10,372</b>	<b>108.3</b>	<b>\$ 32,249</b>	<b>\$ 19,350</b>	<b>\$ 12,899</b>	<b>66.7</b>

*General and administrative.* The increase in general and administrative expense for the three months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$1.0 million increase in personnel expense related to our 2011 and 2012 acquisitions and overall company growth; a \$0.1 million increase in depreciation expense; a \$0.3 million increase in facilities expense; a \$0.6 million increase in stock-based compensation; a \$0.4 million increase in other general and administrative expenses; and an \$8.5 million increase in litigation expense related to fees and the accrual of the settlement of the Yardi litigation. Refer to Part II, Item 1, *Legal Proceedings* for further information regarding the litigation settlement. These increases were offset by a \$0.3 million decrease from the fair value adjustment of acquisition-related liabilities and a \$0.2 million decrease in travel related expenses.

The increase in general and administrative expense for the six months ended June 30, 2012 as compared to the same period in 2011 was primarily due to: a \$2.2 million increase in personnel expense related to our 2011 and 2012 acquisitions and overall company growth; a \$0.2 million increase in depreciation expense; a \$1.3 million increase in stock-based compensation; a \$0.4 million increase from the loss on disposal of assets; a \$0.3 million increase in professional fees; a \$0.1 million increase in facilities expense; a \$0.2 million increase in other general and administrative expenses; and a \$8.5 million increase in litigation expense related to fees and the accrual of the settlement of the Yardi litigation. Refer to Part II, Item 1, *Legal Proceedings* for further information regarding the litigation settlement. These increases were offset by a \$0.2 million decrease in consulting fees and a \$0.1 million decrease in travel related expenses.

***Interest Expense and Other, Net***

The decrease in interest expense and other, net for the three and six months ended June 30, 2012 as compared to the same period in 2011 was primarily due to a decrease in interest expense as a result of lower debt balances from the December 2011 amendment to our Credit Agreement. In addition to the decrease in interest expense, for the six months ended June 30, 2012, interest expense and other decreased due to other losses of \$0.4 million related to the sale of a non-operating asset held for sale as of June 30, 2011 compared to no losses recorded as of June 30, 2012. See *Long-Term Debt Obligations* for further information regarding our Credit Agreement.

***Provision for Taxes***

We compute our provision for income taxes on a quarterly basis by applying the estimated annual effective tax rate to income from recurring operations and other taxable income. Our effective income tax rate was 39.3% and 40.3% for the three months ended June 30, 2012 and 2011, respectively, and 43.7% and 48.8% for the six months ended June 30, 2012 and 2011. Our effective tax rate fluctuated from the prior period predominantly due to the impact of permanent differences in relation to our results of operations before income taxes.

**Reconciliation of Non-GAAP Financial Measures**

We define Adjusted EBITDA as net income plus depreciation and asset impairment, amortization of intangible assets, interest expense, net, income tax expense (benefit), stock-based compensation expense, and acquisition-related expense. Beginning in 2011, Adjusted EBITDA excludes litigation-related expenses pertaining to the Yardi litigation as discussed in Part II, Item 1, *Legal Proceedings*. Beginning in the second quarter of 2011, Adjusted EBITDA includes acquisition-related deferred revenue adjustments. We believe that the use of Adjusted EBITDA is useful to investors and other users of our financial statements in evaluating our operating performance because it provides them with an additional tool to compare business performance across companies and across periods. We believe that:

Adjusted EBITDA provides investors and other users of our financial information consistency and comparability with our past financial performance, facilitates period-to-period comparisons of operations and facilitates comparisons with our peer companies, many of which use similar non-GAAP financial measures to supplement their GAAP results; and

## Edgar Filing: REALPAGE INC - Form 10-Q

it is useful to exclude certain non-cash charges, such as depreciation and asset impairment, amortization of intangible assets and stock-based compensation and non-core operational charges, such as acquisition-related expense, from Adjusted EBITDA because the amount of such expenses in any specific period may not directly correlate to the underlying performance of our business operations and these expenses can vary significantly between periods as a result of new acquisitions, full amortization of previously acquired tangible and intangible assets or the timing of new stock-based awards, as the case may be.

We use Adjusted EBITDA in conjunction with traditional GAAP operating performance measures as part of our overall assessment of our performance, for planning purposes, including the preparation of our annual operating budget, to evaluate the effectiveness of our business strategies and to communicate with our board of directors concerning our financial performance.

**Table of Contents**

We do not place undue reliance on Adjusted EBITDA as our only measure of operating performance. Adjusted EBITDA should not be considered as a substitute for other measures of liquidity or financial performance reported in accordance with GAAP. There are limitations to using non-GAAP financial measures, including that other companies may calculate these measures differently than we do, that they do not reflect our capital expenditures or future requirements for capital expenditures and that they do not reflect changes in, or cash requirements for, our working capital. We compensate for the inherent limitations associated with using the Adjusted EBITDA measures through disclosure of these limitations, presentation of our financial statements in accordance with GAAP and reconciliation of Adjusted EBITDA to the most directly comparable GAAP measure, net income (loss).

The following provides a reconciliation of net income (loss) to Adjusted EBITDA:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2012	2011	2012	2011
	(in thousands)			
Net income (loss)	\$ (2,372)	\$ 282	\$ (652)	\$ (366)
Acquisition-related deferred revenue adjustment	2	244	83	244
Depreciation, asset impairment and loss on sale of asset	3,375	2,750	6,602	5,874
Amortization of intangible assets	4,685	4,491	9,514	8,537
Interest expense, net	578	732	1,216	1,515
Income tax expense (benefit)	(1,533)	190	(507)	(349)
Litigation related expense	8,539	36	8,899	356
Stock-based compensation expense	4,316	4,969	8,304	9,822
Acquisition-related expense (income)	(237)	44	316	230
Adjusted EBITDA	\$ 17,353	\$ 13,738	\$ 33,775	\$ 25,863

**Liquidity and Capital Resources**

On August 11, 2010, our registration statement on Form S-1 (File No. 333-166397) relating to our initial public offering was declared effective by the SEC. We sold 6,000,000 shares of common stock in our initial public offering. On December 6, 2010, our registration statement on Form S-1 (File No 333-170667) relating to a public stock offering was declared effective by the SEC. We sold an additional 4,000,000 shares of common stock in the offering. Both offerings resulted in proceeds, net of transaction expenses, of \$155.2 million.

Our primary sources of liquidity as of June 30, 2012 consisted of \$45.8 million of cash and cash equivalents, \$115.0 million available under our revolving line of credit and \$14.5 million of current assets less current liabilities (excluding \$45.8 of cash and cash equivalents and \$57.0 million of deferred revenue).

Our principal uses of liquidity have been to fund our operations, working capital requirements, capital expenditures and acquisitions and to service our debt obligations. We expect that working capital requirements, capital expenditures and acquisitions will continue to be our principal needs for liquidity over the near term. In addition, we have made several acquisitions in which a portion of the cash purchase price is payable at various times through 2014.

We believe that our existing cash and cash equivalents, working capital (excluding deferred revenue and cash and cash equivalents) and our cash flow from operations, will be sufficient to fund our operations and planned capital expenditures and service our debt obligations for at least the next 12 months. Our future capital requirements will depend on many factors, including our rate of revenue growth, the timing and size of acquisitions, the expansion of our sales and marketing activities, the timing and extent of spending to support product development efforts, the timing of introductions of new solutions and enhancements to existing solutions and the continuing market acceptance of our solutions. We may enter into acquisitions of, complementary businesses, applications or technologies, in the future, which could require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us, or at all. As of December 31, 2011, we have Federal and State net operating loss carryforwards of \$163.5 million and \$5.3 million, respectively. These carryforwards may be available to offset potential payments of future federal and state income tax liabilities and which, if unused, expire at various dates through 2031 for both federal and state income tax purposes.

The following table sets forth cash flow data for the periods indicated therein:

Edgar Filing: REALPAGE INC - Form 10-Q

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2012</b>	<b>2011</b>
Net cash provided by operating activities	\$ 32,206	\$ 19,221
Net cash used in investing activities	(23,639)	(25,673)
Net cash (used) provided by financing activities	(13,998)	447

---

## **Table of Contents**

### ***Net Cash Provided by Operating Activities***

In the six months ended June 30, 2012, cash from operating activities consisted of a net loss of \$(0.7) million, fair value purchase accounting adjustment of \$0.2 million, deferred tax benefit of \$0.9 million, increases in working capital of \$9.1 million and net non-cash charges of \$24.0 million. Net non-cash charges to income increased \$0.2 million or 0.9%, compared to the same period in 2011, and primarily consisted of depreciation, amortization and stock-based compensation expense. The cash inflow resulting from the changes in working capital was primarily due to changes in litigation accruals and accrued compensation, offset by decreases in other assets and accounts payable.

### ***Net Cash Used in Investing Activities***

In the six months ended June 30, 2012, investing activities consisted of acquisition-related payments of \$13.5 million primarily related to LevelOne and Compliance Depot contingent consideration payments and the Vigilant acquisition as well as \$9.9 million of capital expenditures. Capital expenditures in the six months ended June 30, 2012 were primarily related to investments in technology infrastructure to support our growth initiatives.

### ***Net Cash Used in Financing Activities***

Cash used in financing activities as of June 30, 2012 was primarily due to payments of \$15.3 million on our revolving line of credit, capital lease payments of \$0.1 million offset by net proceeds of \$1.4 million from stock issuances under our stock based compensation plans.

## **Contractual Obligations, Commitments and Contingencies**

### ***Contractual Obligations***

Our contractual obligations relate primarily to borrowings and interest payments under credit facilities, capital leases, operating leases and purchase obligations. There have been no material changes outside normal operations in our contractual obligations from our disclosures within our Form 10-K.

### ***Long-Term Debt Obligations***

In December 2011, we entered into an Amended and Restated Credit Agreement ( Restated Agreement ) to amend our original credit facility. The Restated Agreement provides for a secured revolving credit facility in an aggregate principal amount of up to \$150.0 million, subject to a borrowing formula, with a sublimit of \$10.0 million for the issuance of letters of credit on our behalf. The Restated Agreement converted our outstanding term loan under the original credit facility into revolving loans. Revolving loans accrue interest at a per annum rate equal to, at the Company's option, either LIBOR or Wells Fargo's prime rate (or, if greater, the federal funds rate plus 0.50% or three month LIBOR plus 1.00%), in each case plus a margin ranging from 2.50% to 3.00%, in the case of LIBOR loans, and 0.00% to 0.25% in the case of prime rate loans, based upon the Company's senior leverage ratio. The interest is due and payable monthly, in arrears, for loans bearing interest at the prime rate and at the end of the applicable 1-, 2-, or 3-month interest period in the case of loans bearing interest as the adjusted LIBOR rate. Principal, together with all accrued and unpaid interest, is due and payable on December 30, 2015. Advances under the credit facility may be voluntarily prepaid, and must be prepaid with the proceeds of certain dispositions, extraordinary receipts and indebtedness and in full upon a change in control.

All of our obligations under the loan facility are secured by substantially all of our property. All of our existing and future domestic subsidiaries are required to guaranty our obligations under the credit facility, other than certain immaterial subsidiaries and our payment processing subsidiary, RealPage Payment Processing Services, Inc. Our foreign subsidiaries may, under certain circumstances, be required to guaranty our obligations under the credit facility. Such guarantees by existing and future subsidiaries are and will be secured by substantially all of the property of such subsidiaries.

Our credit facility contains customary covenants which limit our and certain of our subsidiaries' ability to, among other things, incur additional indebtedness or guarantee indebtedness of others; create liens on our assets; enter into mergers or consolidations; dispose of assets; prepay indebtedness or make changes to our governing documents and certain of our agreements; pay dividends

---

## **Table of Contents**

and make other distributions on our capital stock, and redeem and repurchase our capital stock; make investments, including acquisitions; enter into transactions with affiliates; and make capital expenditures. Our credit facility additionally contains customary affirmative covenants, including requirements to, among other things, take certain actions in the event we form or acquire new subsidiaries; hold annual meetings with our lenders; provide copies of material contracts and amendments to our lenders; locate our collateral only at specified locations; and use commercially reasonable efforts to ensure that certain material contracts permits the assignment of the contract to our lenders; subject in each case to customary exceptions and qualifications. We are also required to comply with a fixed charge coverage ratio, which is a ratio of our EBITDA to our fixed charges as determined in accordance with the credit facility, of 1.25:1.00 for each 12-month period ending at the end of a fiscal quarter, and a senior leverage ratio, which is a ratio of the outstanding revolver usage to our EBITDA as determined in accordance with the credit facility, of 2.75:1.00 on the last day of each fiscal quarter.

In the event of a default on our credit facility, the obligations under the credit facility could be accelerated, the applicable interest rate under the credit facility could be increased, and our subsidiaries that have guaranteed the credit facility could be required to pay the obligations in full, and our lenders would be permitted to exercise remedies with respect to all of the collateral that is securing the credit facility, including substantially all of our and our subsidiary guarantors' assets. Any such default that is not cured or waived could have a material adverse effect on our liquidity and financial condition.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet financing arrangements and we do not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in interest rates. We do not hold or issue financial instruments for trading purposes.

We had cash and cash equivalents of \$45.8 million and \$51.3 million at June 30, 2012 and December 31, 2011, respectively.

We hold cash and cash equivalents for working capital purposes. We do not have material exposure to market risk with respect to investments, as our investments consist primarily of highly liquid investments purchased with original maturities of three months or less. We do not use derivative financial instruments for speculative or trading purposes; however, we may adopt specific hedging strategies in the future. Any declines in interest rates, however, will reduce future interest income.

We had \$35.0 million and \$50.3 million outstanding under our revolving line of credit at June 30, 2012 and December 31, 2011, respectively. The interest rate on this debt is variable and adjusts periodically based on the three-month LIBOR rate. If the LIBOR rate changes by 1%, our annual interest expense would change by approximately \$0.4 million.

### **Item 4. Controls and Procedures.**

#### **Evaluation of Disclosure Controls and Procedures**

Pursuant to Rule 13a-15(b) and Rule 15d-15(b) under the Securities Exchange Act of 1934, as amended (the Exchange Act), we carried out an evaluation, with the participation of our management, and under the supervision of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined under Rule 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of June 30, 2012, in ensuring that information required to be disclosed in the reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Management's assessment of the effectiveness of our disclosure controls and procedures is expressed at the level of reasonable assurance because management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives.



**Changes in Internal Controls**

There were no changes in the Company's internal control over financial reporting during the six months ended June 30, 2012 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

---

**Table of Contents****Inherent Limitations of Internal Controls**

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

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

From time to time, we have been and may be involved in various legal proceedings arising from our ordinary course of business.

On January 24, 2011, Yardi Systems, Inc. filed a lawsuit in the U.S. District Court for the Central District of California against RealPage, Inc. and DC Consulting, Inc. (this lawsuit and the related litigation, the Yardi Lawsuit ). Yardi filed a First Amended Complaint on August 12, 2011. The lawsuit alleged claims for relief for violation of the Computer Fraud and Abuse Act, violation of the California Comprehensive Data Access and Fraud Act, violation of the Digital Millennium Copyright Act, copyright infringement, trade secret misappropriation, unfair competition, and inducement of breach of contract. Yardi sought injunctive relief, punitive damages, recovery of all profits attributable to Defendants' allegedly wrongful acts and infringements, statutory damages, exemplary damages, prejudgment interest, and attorneys' fees and costs. The First Amended Complaint alleged, among other things, that the Company took Yardi employee, client and independent consultant credentials and used them to access Yardi's computer system and steal Yardi's trade secrets and copyrighted software, related support documentation, price lists and other proprietary information. In addition, the First Amended Complaint alleged that the Company improperly obtained administrative-level access to Yardi's software and copied it onto the Company's servers for its own competitive purposes, used these unauthorized software copies to discover the allegedly proprietary programming, functionality and feature set of Yardi's software, to compete unfairly against Yardi, to create unauthorized derivative works from Yardi's software, and to enhance the Company's own products and services. Yardi alleged that in doing so, and in offering to indemnify our customers, the Company induced Cloud customers to violate their confidentiality and other agreements with Yardi. On March 28, 2011, the Company filed an answer to Yardi's Complaint, and on September 12, 2011, the Company answered the First Amended Complaint. The Company also filed counterclaims against Yardi, first in connection with its March 28 answer and then in First Amended Counterclaims filed on May 18, 2011. On September 2, 2011, following the Court's order granting in part and denying in part Yardi's motion to dismiss certain of the Company's causes of action without prejudice, the Company filed Second Amended Counterclaims. The Company's counterclaims alleged that Yardi and its agents wrongfully obtained and used our trade secrets and engaged in anti-competitive behavior with respect to certain of our clients. The Company's counterclaims sought relief for misappropriation of trade secrets, Sherman Act (antitrust) violations and California Cartwright Act violations, intentional interference with contract, intentional interference with prospective economic advantage, and violation of California's unfair competition statute. The Company sought damages, punitive damages, injunctive relief and all profits, gains and advantages that Yardi received as a result of its wrongful conduct along with attorneys' fees and costs. Yardi filed a Motion to Dismiss the Company's Second Amended Counterclaims on September 30, 2011. On February 13, 2012, the Court denied Yardi's motion with respect to all claims except for a portion of one of our claims for intentional interference with contract, as to which dismissal was granted. On July 1, 2012, the Company and Yardi entered into a Settlement Agreement resolving all outstanding litigation between the parties. The Settlement Agreement also includes a license of certain Yardi intellectual property to the Company and a license of certain of our intellectual property to Yardi.

In connection with the Yardi Lawsuit, the Company made claims for reimbursement against each of its primary and excess layer general liability and professional liability insurance carriers. Each of our primary and excess layer professional liability insurance carriers other than Homeland Insurance of New York (Homeland) reimbursed the Company up to each of its policy limits. On July 19, 2012, we became aware of assertions by one of our primary layer insurance carriers that such carrier no longer considered the previously reimbursed \$5.0 million payment covered under such policy, and that the carrier demanded reimbursement of the \$5.0 million payment that the carrier had previously reimbursed to us. The Company disputes this assertion by the carrier. We intend to defend these allegations and to pursue coverage and other appropriate relief in connection with this insurance policy. It is not possible to predict the outcome of this insurance matter, and as such, we have not recorded a contingent liability as we believe an unfavorable outcome is not probable as of the date of this filing.

## Edgar Filing: REALPAGE INC - Form 10-Q

In addition, in connection with the Yardi Lawsuit, the Company has an excess professional liability insurance policy with Homeland that provides an additional \$5.0 million of coverage above the amounts previously reimbursed to us. The Company made claims for reimbursement under the Homeland policy with respect to the Yardi Lawsuit, but Homeland denied such claims and never made payment to us. On May 30, 2012, Homeland filed a motion for declaratory judgment against the Company in the United States District Court for the Northern District of Texas seeking a determination by the court that Homeland's policy does not provide coverage for amounts incurred in connection with the Yardi Lawsuit. We have not recorded any amounts as recoverable in relation to the Homeland insurance policy as of June 30, 2012.

**Table of Contents**

In March 2010, the District Attorney of Ventura County, California issued an administrative subpoena to us seeking certain information related to our provision of utility billing services in the State of California. A representative of the District Attorney has informed us that the subpoena was issued in connection with a general investigation of industry practices with respect to utility billing in California. Utility billing is subject to regulation by state law and various state administrative agencies, including, in California, the California Public Utility Commission, or the CPUC, and the Division of Weights and Measures, or the DWM. We have provided the District Attorney with the information requested in the subpoena. In late August 2010, we received limited, follow-up requests for information to which we have responded. The District Attorney's office has not initiated an administrative or other enforcement action against us, nor have they asserted any violations of the applicable regulations by us. Given the early stage of this investigation, it is difficult to predict its outcome and whether the District Attorney will pursue an administrative or other enforcement action against us in the State of California and what the result of any such action would be. However, penalties or assessments of violations of regulations promulgated by the CPUC or DWM or other regulators may be calculated on a per occurrence basis. Due to the large number of billing transactions we process for our customers in California, our potential liability in an enforcement action could be significant. If the District Attorney ultimately pursues an administrative or other enforcement action against us, we believe that we have meritorious defenses to the potential claims and would defend them vigorously. However, even if we were successful in defending against such claims, the proceedings could result in significant costs and divert management's attention.

On March 26, 2010, Smarter Agent, LLC, a provider of mobile real estate applications, filed a complaint against our subsidiary, Multifamily Technology Solutions, Inc., and multiple other defendants for patent infringement in the U.S. District Court for the District of Delaware. The complaint alleges, among other things, that our mobile technology infringes three patents held by Smarter Agent purporting to cover: a Global positioning-based real estate database access device and method, a Position-based information access device and method and a Position-based information access device and method of searching, and seeks injunctive relief, unspecified damages, enhanced damages, prejudgment interest, and attorneys' fees and costs. We have denied the allegations and asserted counterclaims seeking declarations that we are not infringing the patents and that the patents are invalid. In November 2010, the U.S. Patent and Trademark Office granted our petition for re-examination of the three patents-in-suit and its first office action found all claims invalid. Smarter Agent submitted arguments to overcome the objections, but the U.S Patent and Trademark Office has finally rejected one of the patents, issuing an action closing the prosecution ( ACP ), while final action and ACP for the remaining patent remains pending. In March 2011, the court stayed the litigation pending the completion of the re-examination proceedings and any related appeals. Because this lawsuit is at an early stage, it is not possible to predict its outcome. We intend to defend this case and pursue our counterclaims vigorously. However, even if we were successful in defending against such claims or in prevailing on our counterclaims, the proceedings could result in significant costs and divert management's attention.

**Table of Contents**

**Item 1A. Risk Factors.  
Risks Related to Our Business**

**Risks Related to Our Business**

*Our quarterly operating results have fluctuated in the past and may fluctuate in the future, 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. Fluctuations in our quarterly operating results may be due to a number of factors, including the risks and uncertainties discussed elsewhere in this filing. Some of the important factors that could cause our revenues and operating results to fluctuate from quarter to quarter include:

the extent to which on demand software solutions maintain current and achieve broader market acceptance;

our ability to timely introduce enhancements to our existing solutions and new solutions;

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

changes in our pricing policies or those of our competitors;

the variable nature of our sales and implementation cycles;

general economic, industry and market conditions in the rental housing industry that impact the financial condition of our current and potential customers;

the amount and timing of our investment in research and development activities;

technical difficulties, service interruptions, data or document losses or security breaches;

Internet usage trends among consumers, and the methodologies internet search engines utilized to direct those consumers to websites such as our LeaseStar product family;

our ability to hire and retain qualified key personnel, including the rate of expansion of our sales force and IT department;

changes in the legal, regulatory or compliance environment related to the rental housing industry, including without limitation fair credit reporting, payment processing, privacy, utility billing, insurance, the Internet and e-commerce, licensing, HIPAA and HITECH;

the amount and timing of operating expenses and capital expenditures related to the expansion of our operations and infrastructure;

## Edgar Filing: REALPAGE INC - Form 10-Q

the timing of revenue and expenses related to recent and potential acquisitions or dispositions of businesses or technologies;

our ability to integrate acquisition operations in a cost-effective and timely manner;

litigation and settlement costs, including unforeseen costs;

public company reporting requirements; and

new accounting pronouncements and changes in accounting standards or practices, particularly any affecting the recognition of subscription revenue or accounting for mergers and acquisitions.

## **Table of Contents**

Fluctuations in our quarterly operating results or guidance that we provide may lead analysts to change their long-term model for valuing our common stock, cause us to face short-term liquidity issues, impact our ability to retain or attract key personnel or cause other unanticipated issues, all of which could cause our stock price to decline. As a result of the potential variations in our quarterly revenue and operating results, we believe that quarter-to-quarter comparisons of our revenues and operating results may not be meaningful and the results of any one quarter should not be relied upon as an indication of future performance.

### ***We have a history of operating losses and may not maintain profitability in the future.***

We have not been consistently profitable on a quarterly or annual basis. While we have experienced significant growth over recent quarters, we may not be able to sustain or increase our growth or profitability in the future. We expect to make significant future expenditures related to the development and expansion of our business. As a result of increased general and administrative expenses due to the additional operational and reporting costs associated with being a public company, we will need to generate and sustain increased revenue to achieve future profitability expectations. We may incur significant losses in the future for a number of reasons, including the other risks and uncertainties described in this filing. Additionally, we may encounter unforeseen operating expenses, difficulties, complications, delays and other unknown factors that may result in losses in future periods. If these losses exceed our expectations or our growth expectations are not met in future periods, our financial performance will be affected adversely.

### ***If we are unable to manage the growth of our diverse and complex operations, our financial performance may suffer.***

The growth in the size, dispersed geographic locations, complexity and diversity of our business and the expansion of our product lines and customer base has placed, and our anticipated growth may continue to place, a significant strain on our managerial, administrative, operational, financial and other resources. We increased our number of employees from 654 as of December 31, 2007 to 2,478 as of June 30, 2012. We increased our number of on demand customers from 2,199 as of December 31, 2007 to over 8,200 as of June 30, 2012. We increased the number of on demand product centers that we offer from 25 as of December 31, 2007 to 49 as of June 30, 2012. In addition, in the past, we have grown and expect to continue to grow through acquisitions. Our ability to effectively manage our anticipated future growth will depend on, among other things, the following:

successfully supporting and maintaining a broad range of solutions;

maintaining continuity in our senior management and key personnel;

attracting, retaining, training and motivating our employees, particularly technical, customer service and sales personnel;

enhancing our financial and accounting systems and controls;

enhancing our information technology infrastructure, processes and controls; and

managing expanded operations in geographically dispersed locations.

If we do not manage the size, complexity and diverse nature of our business effectively, we could experience product performance issues, delayed software releases and longer response times for assisting our customers with implementation of our solutions and could lack adequate resources to support our customers on an ongoing basis, any of which could adversely affect our reputation in the market and our ability to generate revenue from new or existing customers.

***The nature of our platform is complex and highly integrated, and if we fail to successfully manage releases or integrate new solutions, it could harm our revenues, operating income and reputation.***

## Edgar Filing: REALPAGE INC - Form 10-Q

We manage a complex platform of solutions that consists of our property management systems, integrated software-enabled value-added services and web-based advertising and lease generation services. Many of our solutions include a large number of product centers that are highly integrated and require interoperability with other RealPage products, as well as products and services of third-party service providers. Additionally, we typically deploy new releases of the software underlying our on demand software solutions on a bi-weekly, monthly or quarterly schedule depending on the solution. Due to this complexity and the condensed development cycles under which we operate, we may experience errors in our software, corruption or loss of our data or unexpected performance issues from time to time. For example, our solutions may face interoperability difficulties with software operating systems or programs being used by our customers, or new releases, upgrades, fixes or the integration of acquired technologies may have unanticipated consequences on the operation and performance of our other solutions. If we encounter integration challenges or discover errors in our solutions late in our development cycle, it may cause us to delay our launch dates. Any major integration or interoperability issues or launch delays could have a material adverse effect on our revenues, operating income and reputation.



---

## **Table of Contents**

***Our business depends substantially on customers renewing and expanding their subscriptions for our solutions and any increase in customer cancellations or decline in customer renewals or expansions would harm our future operating results.***

With the exception of some of our LeaseStar and Propertyware solutions, which are typically month-to-month, we generally license our solutions pursuant to customer agreements with a term of one year. Our customers have no obligation to renew these agreements after their term expires, or to renew these agreements at the same or higher annual contract value. In addition, under specific circumstances, our customers have the right to cancel their customer agreements before they expire, for example, in the event of an uncured breach by us, or in some circumstances, by giving 30 days' notice or paying a cancellation fee. In addition, customers often purchase a higher level of professional services in the initial term than they do in renewal terms to ensure successful activation. As a result, our ability to grow is dependent in part on customers purchasing additional solutions or professional services after the initial term of their customer agreement. Though we maintain and analyze historical data with respect to rates of customer renewals, upgrades and expansions, those rates may not accurately predict future trends in customer renewals. Our customers' renewal rates may decline or fluctuate for a number of reasons, including, but not limited to, their level of satisfaction with our solutions, our pricing, our competitors' pricing, reductions in our customers' spending levels or reductions in the number of units managed by our customers. If our customers cancel or amend their agreements with us during their term, do not renew their agreements, renew on less favorable terms or do not purchase additional solutions or professional services in renewal periods, our revenue may grow more slowly than expected or decline and our profitability may be harmed.

Additionally, we have experienced, and expect to continue to experience, some level of customer turnover as properties are sold and the new owners and managers of properties previously owned or managed by our customers do not continue to use our solutions. We cannot predict the amount of customer turnover we will experience in the future. However, we have experienced slightly higher rates of customer turnover with our recently acquired Propertyware property management system, primarily because it serves smaller properties than our OneSite property management system, and we may experience higher levels of customer turnover to the extent Propertyware grows as a percentage of our revenues. If we experience increased customer turnover, our financial performance and operating results could be adversely affected.

We have also experienced, and expect to continue to experience, some number of consolidations of our customers with other parties. If one of our customers consolidates with a party who is not a customer, our customer may decide not to continue to use our solutions. In addition, if one of our customers is consolidated with another customer, the acquiring customer may have negotiated lower prices for our solutions or may use fewer of our solutions than the acquired customer. In each case, the consolidated entity may attempt to negotiate lower prices for using our solutions as a result of their increased size. These consolidations may cause us to lose customers or require us to reduce prices as a result of enhanced customer leverage, which could cause our financial performance and operating results to be adversely affected.

***Because we recognize subscription revenue over the term of the applicable customer agreement, a decline in subscription renewals or new service agreements may not be reflected immediately in our operating results.***

We generally recognize revenue from customers ratably over the terms of their customer agreements which, with the exception of our month-to-month advertising, lease generation and Propertyware agreements, are typically one year. As a result, much of the revenue we report in each quarter is deferred revenue from customer agreements entered into during previous quarters. Consequently, a decline in new or renewed customer agreements in any one quarter will not be fully reflected in our revenue or our results of operations until future periods. Accordingly, this revenue recognition model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription term.

***We may not be able to continue to add new customers and retain and increase sales to our existing customers, which could adversely affect our operating results.***

Our revenue growth is dependent on our ability to continually attract new customers while retaining and expanding our service offerings to existing customers. Growth in the demand for our solutions may be inhibited and we may be unable to sustain growth in our customer base for a number of reasons, including, but not limited to:

our failure to develop new or additional solutions;

our inability to market our solutions in a cost-effective manner to new customers or in new vertical or geographic markets;



**Table of Contents**

our inability to expand our sales to existing customers;

the inability of our LeaseStar product family to grow traffic to its websites, resulting in lower levels of lead and lease/move-in traffic to customers;

our inability to build and promote our brand; and

perceived security, integrity, reliability, quality or compatibility problems with our solutions.

A substantial amount of our past revenue growth was derived from purchases of upgrades and additional solutions by existing customers. Our costs associated with increasing revenue from existing customers are generally lower than costs associated with generating revenue from new customers. Therefore, a reduction in the rate of revenue increase from our existing customers, even if offset by an increase in revenue from new customers, could reduce our profitability and have a material adverse effect on our operating results.

***If we are not able to integrate past or future acquisitions successfully, our operating results and prospects could be harmed.***

We have acquired new technology and domain expertise through multiple acquisitions, including our most recent acquisition of Compliance Depot in May 2011, SeniorLiving.net in July 2011, Multifamily Technology Solutions, Inc. in August 2011, Vigilant, Inc. in January 2012 and RentMineOnline, Inc. in July 2012. We expect to continue making acquisitions. The success of our future acquisition strategy will depend on our ability to identify, negotiate, complete and integrate acquisitions. Acquisitions are inherently risky, and any acquisitions we complete may not be successful. Any acquisitions we pursue would involve numerous risks, including the following:

difficulties in integrating and managing the operations and technologies of the companies we acquire;

diversion of our management's attention from normal daily operations of our business;

our inability to maintain the key employees, the key business relationships and the reputations of the businesses we acquire;

the acquisitions may generate insufficient revenue to offset our increased expenses associated with acquisitions;

our responsibility for the liabilities of the businesses we acquire, including, without limitation, liabilities arising out of their failure to maintain effective data security, data integrity, disaster recovery and privacy controls prior to the acquisition;

difficulties in complying with new regulatory standards to which we were not previously subject;

delays in our ability to implement internal standards, controls, procedures and policies in the businesses we acquire; and

adverse effects of acquisition activity on the key performance indicators we use to monitor our performance as a business.

Our current acquisition strategy includes the acquisition of companies that offer property management systems that may not interoperate with our software-enabled value-added services. In order to integrate and fully realize the benefits of such acquisitions, we expect to build application interfaces that enable such customers to use a wide range of our solutions while they continue to use their legacy management systems. In addition, over time we expect to migrate the acquired company's customers to our on demand property management systems to retain them as

## Edgar Filing: REALPAGE INC - Form 10-Q

customers and to be in a position to offer them our solutions on a cost-effective basis. These efforts may be unsuccessful or entail costs that result in losses or reduced profitability.

We may be unable to secure the equity or debt funding necessary to finance future acquisitions on terms that are acceptable to us, or at all. If we finance acquisitions by issuing equity or convertible debt securities, our existing stockholders will likely experience ownership dilution, and if we finance future acquisitions with debt funding, we will incur interest expense and may have to comply with additional financing covenants or secure that debt obligation with our assets.

---

## **Table of Contents**

***If we are unable to successfully develop or acquire and sell enhancements and new solutions, our revenue growth will be harmed and we may not be able to meet profitability expectations.***

The industry in which we operate is characterized by rapidly changing customer requirements, technological developments 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 successfully develop, bring to market and sell enhancements to our existing solutions and new solutions that effectively respond to the rapid changes in our industry. Any enhancements or new solutions that we develop or acquire may not be introduced to the market in a timely or cost-effective manner and may not achieve the broad market acceptance necessary to generate the revenue required to offset the operating expenses and capital expenditures related to development or acquisition. If we are unable to timely develop or acquire and sell enhancements and new solutions that keep pace with the rapid changes in our industry, our revenue will not grow as expected and we may not be able to maintain or meet profitability expectations.

***We derive a substantial portion of our revenue from a limited number of our solutions and failure to maintain demand for these solutions or diversify our revenue base through increasing demand for our other solutions could negatively affect our operating results.***

Historically, a majority of our revenue was derived from sales of our OneSite property management system and our LeasingDesk software-enabled value-added service. If we are unable to develop enhancements to these solutions to maintain demand for these solutions or to diversify our revenue base by increasing demand for our other solutions, our operating results could be negatively impacted.

***We use a small number of data centers to deliver our solutions. Any disruption of service at our data centers or other facilities could interrupt or delay our customers' access to our solutions, which could harm our operating results.***

The ability of our customers to access our service is critical to our business. We currently serve a majority of our customers from a primary data center located in Carrollton, Texas. We also maintain a secondary data center in downtown Dallas, Texas, approximately 20 miles from our primary data center. Services of our most recent acquisitions are provided from data centers located across the United States, many of which are operated by third party data vendors. We plan to maintain a data center in San Francisco for LeaseStar and certain other solutions and intend to migrate all other data services to our primary and secondary data centers in Carrollton and Dallas. Until this migration is complete, we have no assurances that the policies and procedures in place at our Carrollton and Dallas data centers will be followed at data centers operated by third party vendors or even at our other locations. Any event resulting in extended interruption or delay in our customers' access to our services or their data could harm our operating results. There can be no certainty that the measures we have taken to eliminate single points of failure in the primary and secondary data centers will be effective to prevent or minimize interruptions to our operations. Our data centers or other facilities are vulnerable to interruption or damage from a number of sources, many of which are beyond our control, including, without limitation:

extended power loss;

telecommunications failures from multiple telecommunication providers or other internet service providers;

natural disaster or an act of terrorism;

software and hardware errors, or failures in our own systems or in other systems;

network environment disruptions such as computer viruses, hacking and similar problems in our own systems and in other systems;

theft and vandalism of equipment;

actions or events arising from human error; and

actions or events caused by or related to third parties.

The occurrence of an extended interruption of services at one or more of our data centers or other facilities could result in lengthy interruptions in our services. Since January 1, 2007, we have experienced two extended service interruptions lasting more than eight hours caused by equipment and hardware failures. Our service level agreements require us to refund a prorated portion of the access fee if we fail to satisfy our service level commitments related to availability. Refunds for breach of this service level commitment have resulted in

## **Table of Contents**

immaterial payments to customers in the past. An extended service outage could result in refunds to our customers and harm our customer relationships. In addition, under some of our advertising and lease generation agreements, we are generally paid for performance and would be unable to perform services under those agreements in the event of a service interruption.

We attempt to mitigate these risks at our data centers or other facilities through various business continuity efforts, including redundant infrastructure, 24 x 7 x 365 system activity monitoring, backup and recovery procedures, use of a secure off-site storage facility for backup media, separate test systems and change management and system security measures, but our precautions may not protect against all potential problems. Our secondary data center is equipped with physical space, power, storage and networking infrastructure and Internet connectivity to support the solutions we provide in the event of the interruption of services at our primary data center. Even with this secondary data center, however, our operations would be interrupted during the transition process should our primary data center experience a failure. Moreover, both our primary and secondary data centers are located in the greater metropolitan Dallas area. As a result, any regional disaster could affect both data centers and result in a material disruption of our services.

For customers who specifically pay for accelerated disaster recovery services, we replicate their data from our primary data center to our secondary data center with the necessary stand-by servers and disk storage available to provide services within two hours of a disaster. This process is currently audited by some of our customers who pay for this service on an annual basis. For customers who do not pay for such services, our current service level agreements with our customers require that we provide disaster recovery within 72 hours.

Disruptions at our data centers or other facilities could cause disruptions in our services and data or document loss or corruption. This could damage our reputation, cause us to issue credits to customers, subject us to potential liability or costs related to defending against claims or cause customers to terminate or elect not to renew their agreements, any of which could negatively impact our revenues.

***We provide service level commitments to our customers, and our failure to meet the stated service levels could significantly harm our revenue and our reputation.***

Our customer agreements provide that we maintain certain service level commitments to our customers relating primarily to product functionality, network uptime, critical infrastructure availability and hardware replacement. For example, our service level agreements generally require that our solutions are available 98% of the time during coverage hours (normally 6:00 a.m. through 10:00 p.m. Central time daily) 365 days per year. If we are unable to meet the stated service level commitments, we may be contractually obligated to provide customers with refunds or credits. Additionally, if we fail to meet our service level commitments a specified number of times within a given time frame or for a specified duration, our customers may terminate their agreement with us or extend the term of their agreement at no additional fee. As a result, a failure to deliver services for a relatively short duration could cause us to issue credits or refunds to a large number of affected customers or result in the loss of customers. In addition, we cannot assure you that our customers will accept these credits, refunds, termination or extension rights in lieu of other legal remedies that may be available to them. Our failure to meet our commitments could also result in substantial customer dissatisfaction or loss. Because of the loss of future revenues through the issuance of credits or the loss of customers or other potential liabilities, our revenue could be significantly impacted if we cannot meet our service level commitments to our customers.

***We face intense competitive pressures and our failure to compete successfully could harm our operating results.***

The market for many of our solutions is intensely competitive, fragmented and rapidly changing. Some of these markets have relatively low barriers to entry. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. Increased competition generally could result in pricing pressures, reduced sales and reduced margins. Often we compete to sell our solutions against existing systems that our potential customers have already made significant expenditures to install.

Our competitors vary depending on our product and service. In the market for accounting software we compete with Yardi, MRI, AMSI, Intacct, NetSuite, Intuit, Oracle, PeopleSoft, J.D. Edwards, SAP, Microsoft, AppFolio and other small providers of accounting software. Accounting software typically requires high switching costs. In the market for property management software, we face competitive pressure from Yardi and its Voyager products, AMSI Property Management (owned by Infor Global Solutions, Inc.), Property Boulevard, Inc., Boston Post (acquired by MRI Software LLC), Jenark (owned by CoreLogic), Entrada (a division of Property Solutions International (Property Solutions)) and MRI Software LLC. In the single-family market, our accounting and property management Systems primarily compete with Yardi, AppFolio, Intuit, DIY Real Estate Solutions (acquired by Yardi), Buildium, LLC, Rent Manager (owned by London Computer Systems, Inc.) and Property Boss Solutions, LLC.

In the market for vertically-integrated cloud computing for multifamily real estate owners and property managers, our only substantial competition is from Yardi and Property Solutions. We also compete with cloud computing service providers such as Amazon.com, Rackspace, IBM and many others.

## Edgar Filing: REALPAGE INC - Form 10-Q

We offer a number of software-enabled value-added services that compete with a disparate and large group of competitors. In the applicant screening market, our principal competitors are LexisNexis, CoreLogic, Inc. (formerly First Advantage Corporation, an affiliate of The First American Corporation), TransUnion Rental Screening



---

## **Table of Contents**

Solutions, Inc. (a subsidiary of TransUnion LLC), Yardi, On-Site.com and many other smaller regional and local screening companies. In the insurance market, our principal competitors are Assurant, Inc., Bader Company, Property Solutions and a number of national insurance underwriters (including GEICO Corporation, The Allstate Corporation, State Farm Fire and Casualty Company, Farmers Insurance Exchange, Nationwide Mutual Insurance Company and United Services Automobile Association) that market renters insurance. There are many smaller screening and insurance providers in the risk mitigation area that we encounter less frequently, but they nevertheless present a competitive presence in the market.

In the customer relationship management, or CRM, market, we compete with providers of contact center and call tracking services, including Call Source Inc. (currently owned by Lease Hawk), Yardi, Property Solutions and numerous regional and local contact centers. In addition, we compete with lead tracking solution providers, including Call Source Inc., Lead Tracking Solutions (recently acquired by Yardi) and Who's Calling, Inc. In addition, we compete with content syndication providers Realty DataTrust Corporation (acquired by MRI Software, LLC), RentSentinel.com (owned by Yield Technologies, Inc.) and rentbits.com, Inc. Finally, we compete with companies providing web portal services, including Apartments24-7.com, Inc., Ellipse Communications, Inc., Property Solutions, GS Search Marketing, Inc., Spherexx.com, Active Building and Yardi. Certain Internet listing services also offer websites for their customers, usually as a free value add to their listing service.

In the marketing and web portal services market, we compete with G5 Search Marketing, Inc., Spherexx LLC, ReachLocal, Inc., Property Solutions, Yodle, Inc. and many local or regional advertising agencies.

In the Internet listing service market, we compete with ForRent (a division of Dominion Enterprises), Apartment Guide (a division of Primedia Inc.), Rent.com (owned by Primedia, Inc.), Apartments.com (a division of Classified Ventures, LLC, Apartment Finder (a division of Network Communications, Inc.), Move, Inc., Property Solutions, Rent Café, (a division of Yardi) and many other companies in regional areas.

In the Senior Living market, we compete against A Place for Mom, Inc., SeniorsForLiving, Inc., Care.com, Inc., Caring, Inc., Care Patrol Franchise Systems, LLC, Yardi, Aging with Grace, LLC, and SeniorHomes.com (owned by Moseo, Corp.) and many other companies in regional areas.

In the utility billing and energy management market, we compete at a national level with American Utility Management, Inc., Conservice, LLC, Ista North America (recently acquired by Yardi), NWP Services Corporation, Minol USA, L.P. and Yardi. Many other smaller utility billing companies compete for smaller rental properties or in regional areas.

In the revenue management market, we compete with The Rainmaker Group, Inc. and Yardi. MPF Research competes with Reis, Axiometrix and CoStar / PPR.

In the spend management market, we compete with Yardi, AvidXchange, Inc., Nexus Systems, Inc., Ariba, Inc. and Oracle Corporation.

In the payment processing market, we compete with Chase Paymentech Solutions, LLC (a subsidiary of JPMorgan Chase & Co.), First Data Corporation, Fiserv, Inc., MoneyGram International, Inc., NWP Services Corporation, Property Solutions, RentPayment.com (a subsidiary of Yapstone, Inc.), Yardi and a number of national banking institutions.

In addition, many of our existing or potential customers have developed or may develop their own solutions that may be competitive with our solutions. We also may face competition for potential acquisition targets from our competitors who are seeking to expand their offerings.

With respect to all of our competitors, we compete based on a number of factors, including total cost of ownership, level of integration with property management systems, ease of implementation, product functionality and scope, performance, security, scalability and reliability of service, brand and reputation, sales and marketing capabilities and financial resources. Some of our existing competitors and new market entrants may enjoy substantial competitive advantages, such as greater name recognition, longer operating histories, larger installed customer bases and larger sales and marketing budgets, as well as greater financial, technical and other resources. In addition, any number of our existing competitors or new market entrants could combine or consolidate to become a more formidable competitor with greater resources. As a result of such competitive advantages, our existing and future competitors may be able to:

develop superior products or services, gain greater market acceptance and expand their offerings more efficiently or more rapidly;

adapt to new or emerging technologies and changes in customer requirements more quickly;

---

**Table of Contents**

take advantage of acquisition and other opportunities more readily;

adopt more aggressive pricing policies and devote greater resources to the promotion of their brand and marketing and sales of their products and services; and

devote greater resources to the research and development of their products and services.

If we are not able to compete effectively, our operating results will be harmed.

We integrate our software-enabled value-added services with competitive property management software for some of our customers. Our application infrastructure, marketed to our customers as The RealPage Cloud, is based on an open architecture that enables third-party applications to access and interface with applications hosted in The RealPage Cloud through our RealPage Exchange platform. Likewise, through this platform our RealPage Cloud services are able to access and interface with other third-party applications, including third-party property management systems. We also provide services to assist in the implementation, training, support and hosting with respect to the integration of some of our competitors' applications with our solutions. We sometimes rely on the cooperation of our competitors to implement solutions for our customers. However, frequently our reliance on the cooperation of our competitors can result in delays in integration. There is no assurance that our competitors, even if contractually obligated to do so, will continue to cooperate with us or will not prospectively alter their obligations to do so. We also occasionally develop interfaces between our software-enabled value-added services and competitor property management software without their cooperation or consent. There is no assurance that our competitors will not alter their applications in ways that inhibit integration or assert that their intellectual property rights restrict our ability to integrate our solutions with their applications.

On January 24, 2011, one of our competitors, Yardi, filed a lawsuit in the U.S. District Court for the Central District of California against RealPage, Inc. and DC Consulting, Inc. The lawsuit alleged claims for relief for violation of the Computer Fraud and Abuse Act, violation of the California Comprehensive Data Access and Fraud Act, violation of the Digital Millennium Copyright Act, copyright infringement, trade secret misappropriation, unfair competition, and inducement of breach of contract. Yardi sought injunctive relief, punitive damages, recovery of all profits attributable to the defendants' allegedly wrongful acts and infringements, statutory damages, exemplary damages, prejudgment interest, and attorneys' fees and costs. Yardi alleged, among other things, that RealPage took Yardi employee, client and independent consultant credentials and used them to access Yardi's computer system and steal Yardi's trade secrets and copyrighted software, related support documentation, price lists and other proprietary information. In addition, Yardi alleged that RealPage improperly obtained administrative-level access to Yardi's software and copied it onto RealPage's servers for its own competitive purposes, used these unauthorized software copies to discover the allegedly proprietary programming, functionality and feature set of Yardi's software, to compete unfairly against Yardi, to create unauthorized derivative works from Yardi's software, and to enhance RealPage's own products and services. Yardi alleged that in doing so, and in offering to indemnify our customers, RealPage induced Cloud customers to violate their confidentiality and other agreements with Yardi. RealPage answered Yardi's complaint and also filed counterclaims against Yardi. RealPage's counterclaims alleged that Yardi and its agents wrongfully obtained and used our trade secrets and engaged in anti-competitive behavior with respect to certain of our clients. RealPage's counterclaims sought relief for Yardi's misappropriation of RealPage's trade secrets, Sherman Act (antitrust) violations and California Cartwright Act violations, intentional interference with contract, intentional interference with prospective economic advantage, and violation of California's unfair competition statute. RealPage sought damages, punitive damages, injunctive relief and all profits, gains and advantages that Yardi received as a result of its wrongful conduct along with attorneys' fees and costs.

On July 1, 2012, RealPage and Yardi entered into a comprehensive settlement of all outstanding litigation between them, and the lawsuit was dismissed. As part of the settlement, Yardi and RealPage granted each other perpetual licenses and rights to substantially expanded interfaces so that clients can experience a more full-featured integration between RealPage and Yardi applications. The parties also established ongoing testing environments to ensure that the interfaces operate smoothly as designed. In addition, Yardi granted RealPage a license to certain patents. Under the settlement, RealPage will continue providing hosting services for Yardi software for current clients for five more years. RealPage also agreed to stop offering hosting services for Yardi software to new customers and to stop providing support or implementation services for Yardi software. While we expect this settlement comprehensively addressed the matters with respect to Yardi, if competitors do not cooperate with us, alter their applications in ways that inhibit or restrict the integration of our solutions or assert that their intellectual property rights restrict our ability to integrate our solutions with their applications and we are not able to find alternative ways to integrate our solutions with our competitors' applications, our business would be harmed.

*We face competition to attract consumers to our LeaseStar product websites and mobile applications, which could impair our ability to continue to grow the number of users who use our websites and mobile applications, which would harm our business, results of operations and financial condition.*



---

**Table of Contents**

The success of our LeaseStar product family depends in part on our ability to continue to attract additional consumers to our websites and mobile applications. Our existing and potential competitors include companies that could devote greater technical and other resources than we have available, have a more accelerated time frame for deployment and leverage their existing user bases and proprietary technologies to provide products and services that consumers might view as superior to our offerings. Any of our future or existing competitors may introduce different solutions that attract consumers or provide solutions similar to our own but with better branding or marketing resources. If we are unable to continue to grow the number of consumers who use our website and mobile applications, our business, results of operations and financial condition would be harmed.

***We are entering a business environment in which social media integration is playing a significantly increasing role. Social media is a new and rapidly changing industry wherein the rules and regulations related to use and disclosure of personal information is unclear and evolving.***

The operation and marketing of multitenant real estate developments is likely to become more dependent upon the use of and integration with social media platforms as communities attempt to reach their current and target customers through applications like Facebook, Twitter, LinkedIn and other current and emerging social applications. The use of these applications necessarily involves the disclosure of personal information by individuals participating in social media, and the corresponding utilization of such personal information by our products and services via integration programs and data exchanges. The regulatory framework for social media privacy and security issues is currently in flux and is likely to remain so for the foreseeable future. Practices regarding the collection, use, storage, transmission and security of personal information by companies on social media platforms have recently come under increased public scrutiny as various government agencies and consumer groups have called for new regulation and changes in industry practices. We are also subject to each social media platform's terms and conditions for application development and integration, which may be modified, restricted, or otherwise changed to the detriment of our operations.

These factors, many of which are beyond our control, present a high degree of uncertainty for the future of social media integration. As such, there is no assurance that our participation will be risk free, as contractual, statutory or other legal restrictions may be created that limit or otherwise impede our participation in or leverage of social media integration.

***We may be unable to compete successfully against our existing or future competitors in attracting advertisers, which could harm our business, results of operations and financial condition.***

In our LeaseStar product family, we compete to attract advertisers with media sites, including websites dedicated to providing real estate listings and other rental housing related services to real estate professionals and consumers, and major Internet portals, general search engines and social media sites, as well as other online companies. We also compete for a share of advertisers' overall marketing budgets with traditional media such as television, magazines, newspapers and home/apartment guide publications, particularly with respect to advertising dollars spent at the local level by real estate professionals to advertise their qualifications and listings. Large companies with significant brand recognition have large numbers of direct sales personnel and substantial proprietary advertising inventory and web traffic, which may provide a competitive advantage. To compete successfully for advertisers against future and existing competitors, we must continue to invest resources in developing our advertising platform and proving the effectiveness and relevance of our advertising products and services. Pressure from competitors seeking to acquire a greater share of our advertisers' overall marketing budget could adversely affect our pricing and margins, lower our revenue, and increase our research and development and marketing expenses. If we are unable to compete successfully against our existing or future competitors, our business, financial condition or results of operations would be harmed.

***Variability in our sales and activation cycles could result in fluctuations in our quarterly results of operations and cause our stock price to decline.***

The sales and activation cycles for our solutions, from initial contact with a prospective customer to contract execution and activation, vary widely by customer and solution. We do not recognize revenue until the solution is activated. While most of our activations follow a set of standard procedures, a customer's priorities may delay activation and our ability to recognize revenue, which could result in fluctuations in our quarterly operating results.

***Many of our customers are price sensitive, and if market dynamics require us to change our pricing model or reduce prices, our operating results will be harmed.***

Many of our existing and potential customers are price sensitive, and recent adverse global economic conditions have contributed to increased price sensitivity in the multi-family housing market and the other markets that we serve. As market dynamics change, or as new and existing competitors introduce more competitive pricing or pricing models, we may be unable to renew our



---

## **Table of Contents**

agreements with existing customers or customers of the businesses we acquire or attract new customers at the same price or based on the same pricing model as previously used. As a result, it is possible that we may be required to change our pricing model, offer price incentives or reduce our prices, which could harm our revenue, profitability and operating results.

***If we do not effectively expand and train our sales force, we may be unable to add new customers or increase sales to our existing customers and our business will be harmed.***

We continue to be substantially dependent on our sales force to obtain new customers and to sell additional solutions to our existing customers. We believe that there is significant competition for sales 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 sales 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 in the markets where we do business or plan to do business. If we are unable to hire and train sufficient numbers of effective sales personnel, or the sales personnel are not successful in obtaining new customers or increasing sales to our existing customer base, our business will be harmed.

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

The software applications underlying our solutions 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 the software applications underlying our solutions and new errors in our existing solutions may be detected in the future. Any errors or defects that cause performance problems or service interruptions could result in:

a reduction in new sales or subscription renewal rates;

unexpected sales credits or refunds to our customers, loss of customers and other potential liabilities;

delays in customer payments, increasing our collection reserve and collection cycle;

diversion of development resources and associated costs;

harm to our reputation and brand; and

unanticipated litigation costs.

Additionally, the costs incurred in correcting defects or errors could be substantial and could adversely affect our operating results.

***Failure to effectively manage the development of our solutions and data processing efforts outside the United States could harm our business.***

Our success depends, in part, on our ability to process high volumes of customer data and enhance existing solutions and develop new solutions rapidly and cost effectively. We currently maintain an office in Hyderabad, India where we employ development and data processing personnel. We recently opened an office in Manila, Philippines. We believe that performing these activities in Hyderabad and Manila increases the efficiency and decreases the costs of our development and data processing efforts. However, managing and staffing international operations requires management's attention and financial resources. The level of cost-savings achieved by our international operations may not exceed the amount of investment and additional resources required to manage and operate these international operations. Additionally, if we experience difficulties as a result of political, social or economic instability, limitations of local infrastructure, or problems with our workforce or facilities

## Edgar Filing: REALPAGE INC - Form 10-Q

at our or third parties' international operations, our business could be harmed due to delays in product release schedules or data processing services.

***We rely on third-party technologies and services that may be difficult to replace or that could cause errors, failures or disruptions of our service, any of which could harm our business.***

We rely on a number of third-party providers, including, but not limited to, computer hardware and software vendors and database providers, to deliver our solutions. We currently utilize equipment, software and services from Akami Inc., Avaya Inc., Cisco Systems, Inc., Compellent Technologies, Inc., Dell Inc., EMC Corporation, Microsoft Corporation, Oracle Corporation and salesforce.com, inc., as well as many other smaller providers. Our OneSite Accounting service relies on a SaaS-based accounting



**Table of Contents**

system developed and maintained by a third-party service provider. We host this application in our data centers and provide supplemental development resources to extend this accounting system to meet the unique requirements of the rental housing industry. Our shared cloud portfolio reporting service utilizes software licensed from IBM. We expect to utilize additional service providers as we expand our platform. Although the third-party technologies and services that we currently require are commercially available, such technologies and services may not continue to be available on commercially reasonable terms, or at all. Any loss of the right to use any of these technologies or services could result in delays in the provisioning of our solutions until alternative technology is either developed by us, or, if available, is identified, obtained and integrated, and such delays could harm our business. It also may be time consuming and costly to enter into new relationships. Additionally, any errors or defects in the third-party technologies we utilize or delays or interruptions in the third-party services we rely on could result in errors, failures or disruptions of our services, which also could harm our business.

***We depend upon third-party service providers for important payment processing functions. If these third-party service providers do not fulfill their contractual obligations or choose to discontinue their services, our business and operations could be disrupted and our operating results would be harmed.***

We rely on several large payment processing organizations to enable us to provide payment processing services to our customers, including electronic funds transfers, or EFT, check services, bank card authorization, data capture, settlement and merchant accounting services and access to various reporting tools. These organizations include Bank of America Merchant Services, Paymentech, LLC, Jack Henry & Associates, Inc., JPMorgan Chase Bank, N.A. and Wells Fargo, N.A. We also rely on third-party hardware manufacturers to manufacture the check scanning hardware our customers utilize to process transactions. Some of these organizations and service providers are competitors who also directly or indirectly sell payment processing services to customers in competition with us. With respect to these organizations and service providers, we have significantly less control over the systems and processes than if we were to maintain and operate them ourselves. In some cases, functions necessary to our business are performed on proprietary third-party systems and software to which we have no access. We also generally do not have long-term contracts with these organizations and service providers. Accordingly, the failure of these organizations and service providers to renew their contracts with us or fulfill their contractual obligations and perform satisfactorily could result in significant disruptions to our operations and adversely affect operating results. In addition, businesses that we have acquired, or may acquire in the future, typically rely on other payment processing service providers. We may encounter difficulty converting payment processing services from these service providers to our payment processing platform. If we are required to find an alternative source for performing these functions, we may have to expend significant money, time and other resources to develop or obtain an alternative, and if developing or obtaining an alternative is not accomplished in a timely manner and without significant disruption to our business, we may be unable to fulfill our responsibilities to customers or meet their expectations, with the attendant potential for liability claims, damage to our reputation, loss of ability to attract or maintain customers and reduction of our revenue or profits.

***We face a number of risks in our payment processing business that could result in a reduction in our revenues and profits.***

In connection with our electronic payment processing services, we process resident payments and subsequently submit these resident payments to our customers after varying clearing times established by RealPage. These payments are settled through our sponsoring clearing bank, and in the case of EFT, our Originating Depository Financial Institutions, or ODFI. Currently, we rely on Wells Fargo, N.A. and JPMorgan Chase Bank, N.A. as our sponsoring clearing banks. In the future, we expect to enter into similar sponsoring clearing bank relationships with one or more other national banking institutions. The resident payments that we process for our customers at our sponsoring clearing bank are identified in our consolidated balance sheets as restricted cash and the corresponding liability for these resident payments is identified as customer deposits. Our electronic payment processing business and related maintenance of custodial accounts subjects us to a number of risks, including, but not limited to:

liability for customer costs related to disputed or fraudulent transactions if those costs exceed the amount of the customer reserves we have during the clearing period or after resident payments have been settled to our customers;

electronic processing limits on the amount of custodial balances that any single ODFI will underwrite;

reliance on clearing bank sponsors, card payment processors and other service payment provider partners to process electronic transactions;

## Edgar Filing: REALPAGE INC - Form 10-Q

failure by us or our bank sponsors to adhere to applicable laws and regulatory requirements or the standards of the electronic payments rules and regulations;

incidences of fraud, a security breach or our failure to comply with required external audit standards; and

---

## **Table of Contents**

our inability to increase our fees at times when electronic payment partners or associations increase their transaction processing fees. If any of these risks related to our electronic payment processing business were to occur, our business or financial results could be negatively affected. Additionally, with respect to the processing of EFTs, we are exposed to financial risk. EFTs between a resident and our customer may be returned for various reasons such as insufficient funds, stop payment, etc. These returns are charged back to the customer by us. However, if we or our sponsoring clearing banks are unable to collect such amounts from the customer's account or if the customer refuses or is unable to reimburse us for the chargeback, we bear the risk of loss for the amount of the transfer. While we have not experienced material losses resulting from chargebacks in the past, there can be no assurance that we will not experience significant losses from chargebacks in the future. Any increase in chargebacks not paid by our customers may adversely affect our financial condition and results of operations.

***If our security measures are breached and unauthorized access is obtained to our customers' or their residents' data, we may incur significant liabilities, our solutions may be perceived as not being secure and customers may curtail or stop using our solutions.***

The solutions we provide involve the collection, storage and transmission of confidential personal and proprietary information regarding our customers and our customers' current and prospective residents and business partners. Specifically, we collect, store and transmit a variety of customer data such as demographic information and payment histories of our customers' prospective and current residents and business partners. Additionally, we collect and transmit sensitive financial data such as credit card and bank account information. Treatment of certain types of data, such as personally identifiable information, protected health information and sensitive financial data may be subject to federal or state regulations of heightened privacy and security requirements. If our data security or data integrity measures are breached or otherwise fail or prove to be inadequate for any reason, as a result of third-party actions or our employees' or contractors' errors or malfeasance or otherwise, and unauthorized persons obtain access to this information, or the data is otherwise compromised, we could incur significant liability to our customers and to their prospective or current residents or business partners, significant costs associated with internal regulatory investigations and litigation, or significant fines and sanctions by payment processing networks or governmental authorities. Any of these events or circumstances could result in damage to our reputation and material harm to our business.

We also rely upon our customers as users of our system to promote security of the system and the data within it, such as administration of customer-side access credentialing and control of customer-side display of data. On occasion, our customers have failed to perform these activities in such a manner as to prevent unauthorized access to data. To date, these breaches have not resulted in claims against us or in material harm to our business, but we cannot be certain that the failure of our customers in future periods to perform these activities will not result in claims against us, which could expose us to potential litigation, damage to our reputation and material harm to our business.

There can be no certainty that the measures we have taken to protect the privacy and integrity of our customers' and their current or prospective residents' and business partners' data are adequate to prevent or remedy unauthorized access to our system. Because techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventive measures. Experienced computer programmers seeking to intrude or cause harm, or hackers, may attempt to penetrate our service infrastructure from time to time. A hacker who is able to penetrate our service infrastructure could misappropriate proprietary or confidential information or cause interruptions in our services. We might be required to expend significant capital and resources to protect against, or to remedy, problems caused by hackers, and we may not have a timely remedy against a hacker who is able to penetrate our service infrastructure. In addition to purposeful breaches, inadvertent actions or the transmission of computer viruses could expose us to security risks. If an actual or perceived breach of our security occurs or if our customers and potential customers perceive vulnerabilities, the market perception of the effectiveness of our security measures could be harmed, we could lose sales and customers and our business could be materially harmed.

***If we are unable to cost-effectively scale or adapt our existing architecture to accommodate increased traffic, technological advances or changing customer requirements, our operating results could be harmed.***

As we continue to increase our customer base, the number of users accessing our on demand software solutions over the Internet will continue to increase. Increased traffic could result in slow access speeds and response times. Since our customer agreements typically include service availability commitments, slow speeds or our failure to accommodate increased traffic could result in breaches of our customer agreements. In addition, the market for our solutions is characterized by rapid technological advances and changes in customer requirements. In order to accommodate increased traffic and respond to technological advances and evolving customer requirements, we expect that we will be required to make future investments in our network architecture. If we do not implement future upgrades to our network architecture cost-effectively, or if we experience prolonged delays or unforeseen difficulties in connection with upgrading our network architecture, our service quality may suffer and our operating results could be harmed.

---

**Table of Contents**

***Because certain solutions we provide depend on access to customer data, decreased access to this data or the failure to comply with applicable privacy laws and regulations or address privacy concerns applicable to such data could harm our business.***

Certain of our solutions depend on our continued access to our customers' data regarding their prospective and current residents, including data compiled by other third-party service providers who collect and store data on behalf of our customers. Federal and state governments and agencies have adopted, or are considering adopting, laws and regulations regarding the collection, use and disclosure of such data. Any decrease in the availability of such data from our customers, or other third parties that collect and store such data on behalf of our customers, and the costs of compliance with, and other burdens imposed by, applicable legislative and regulatory initiatives may limit our ability to collect, aggregate or use this data. Any limitations on our ability to collect, aggregate or use such data could reduce demand for certain of our solutions. Additionally, any inability to adequately address privacy concerns, even if unfounded, or comply with applicable privacy laws, regulations and policies, could result in liability to us or damage to our reputation and could inhibit sales and market acceptance of our solutions and harm our business.

***The market for on demand software solutions in the rental housing industry is new and continues to develop, and if it does not develop further or develops more slowly than we expect, our business will be harmed.***

The market for on demand SaaS software solutions in the rental housing industry delivered via the Internet through a web browser is rapidly growing but still relatively immature compared to the market for traditional on premise software installed on a customer's local personal computer or server. It is uncertain whether the on demand delivery model will achieve and sustain high levels of demand and market acceptance, making our business and future prospects difficult to evaluate and predict. While our existing customer base has widely accepted this new model, our future success will depend, to a large extent, on the willingness of our potential customers to choose on demand software solutions for business processes that they view as critical. Many of our potential customers have invested substantial effort and financial resources to integrate traditional enterprise software into their businesses and may be reluctant or unwilling to switch to on demand software solutions. Some businesses may be reluctant or unwilling to use on demand software solutions because they have concerns regarding the risks associated with security capabilities, reliability and availability, among other things, of the on demand delivery model. If potential customers do not consider on demand software solutions to be beneficial, then the market for these solutions may not further develop, or it may develop more slowly than we expect, either of which would adversely affect our operating results.

***If use of the Internet and mobile technology, particularly with respect to online rental housing products and services, does not continue to increase as rapidly as we anticipate, our business could be harmed.***

Our future success is substantially dependent on the continued use of the Internet and mobile technology as effective media of business and communication by our customers and consumers. Internet and mobile technology use may not continue to develop at historical rates, and consumers may not continue to use the Internet or mobile technology as media for information exchange. Further, these media may not be accepted as viable long-term outlets for rental housing information for a number of reasons, including actual or perceived lack of security of information and possible disruptions of service or connectivity. If consumers begin to access rental housing information through other media and we fail to innovate, our business may be negatively impacted.

***Economic trends that affect the rental housing market may have a negative effect on our business.***

Our customers include a range of organizations whose success is intrinsically linked to the rental housing market. Economic trends that negatively affect the rental housing market may adversely affect our business. The recent downturn in the global economy has caused volatility in the real estate markets, generally, including the rental housing market, and increases in the rates of mortgage defaults and bankruptcy. Continued instability or downturns affecting the rental housing market may have a material adverse effect on our business, prospects, financial condition and results of operations by:

reducing the number of occupied sites and units on which we earn revenue;

preventing our customers from expanding their businesses and managing new properties;

causing our customers to reduce spending on our solutions;

## Edgar Filing: REALPAGE INC - Form 10-Q

subjecting us to increased pricing pressure in order to add new customers and retain existing customers;

causing our customers to switch to lower-priced solutions provided by our competitors or internally developed solutions;

delaying or preventing our collection of outstanding accounts receivable; and

---

**Table of Contents**

causing payment processing losses related to an increase in customer insolvency.

In addition, economic trends that reduce the frequency of renter turnover or the quantity of new renters may reduce the number of rental transactions completed by our customers and may, as a result, reduce demand for our rental transaction specific services.

***If customers and other advertisers reduce or end their advertising spending on our LeaseStar products and we are unable to attract new advertisers, our business would be harmed.***

Some components of our LeaseStar product family depend on advertising generated through sales to real estate agents and brokerages, property owners and other advertisers relevant to rental housing. Our ability to attract and retain advertisers, and ultimately to generate advertising revenue, depends on a number of factors, including:

increasing the number of consumers of our LeaseStar products and services;

competing effectively for advertising dollars with other online media companies;

continuing to develop our advertising products and services;

keeping pace with changes in technology and with our competitors; and

offering an attractive return on investment to our advertiser customers for their advertising spending with us.

***Reductions in lead generation could have a negative effect on our operating results.***

We could face reductions in leads generated for our clients if third party originators of such leads were to elect to suspend sending leads to us. Reductions in leads generated could reduce the value of our lead generation services, make it difficult for us to add new lead generation services customers, retain existing lead generation services customers and maintain or increase sales levels to our existing lead generation services customers and could adversely affect our operating results.

***We may require additional capital to support business growth, and this capital might not be available.***

We intend to continue to make investments to support our business growth and may require additional funds to respond to business challenges or opportunities, including the need to develop new solutions or enhance our existing solutions, enhance our operating infrastructure or acquire businesses and technologies. Accordingly, we may need to engage in equity or debt financings to secure additional funds. If we raise additional funds through further issuances 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. Debt financing secured by us in the future could involve additional restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. In addition, we may not be able to obtain additional financing on terms favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support our business growth and to respond to business challenges or opportunities could be significantly limited.

***Our debt obligations contain restrictions that impact our business and expose us to risks that could adversely affect our liquidity and financial condition.***

In December 2011, we entered into an Amended and Restated Credit Agreement with Wells Fargo Capital Finance, Comerica Bank and the other lenders party thereto ( Restated Agreement ) to amend and restate our original credit facility. The Restated Agreement provides for a secured revolving credit facility in an aggregate principal amount of up to \$150.0 million, subject to a borrowing formula, with a sublimit of \$10.0 million for the issuance of letters of credit on our behalf. The Restated Agreement converted our outstanding term loan under the original agreement into revolving loans. As of June 30, 2012, \$35.0 million was outstanding under our revolving line of credit and \$10.0 million was

## Edgar Filing: REALPAGE INC - Form 10-Q

available for the issuance of letters of credit. Our interest expense for the credit facility was approximately was \$0.4 million and \$0.6 million for the three months ended June 30, 2012 and 2011 and \$0.9 million and \$1.2 million for the six months ended June 30, 2012 and 2011, respectively. Advances under credit facility may be voluntarily prepaid, and must be prepaid with the proceeds of certain dispositions, extraordinary receipts and indebtedness and in full upon a change in control.

All of our obligations under the loan facility are secured by substantially all of our property. All of our existing and future domestic subsidiaries are required to guaranty our obligations under the credit facility, other than certain immaterial subsidiaries and

## Table of Contents

our payment processing subsidiary, RealPage Payment Processing Services, Inc. Our foreign subsidiaries may, under certain circumstances, be required to guaranty our obligations under the credit facility. Such guarantees by existing and future subsidiaries are and will be secured by substantially all of the property of such subsidiaries.

Our credit facility contains customary covenants, which limit our and certain of our subsidiaries' ability to, among other things:

incur additional indebtedness or guarantee indebtedness of others;

create liens on our assets;

enter into mergers or consolidations;

dispose of assets;

make changes to our governing documents and certain of our agreements;

pay dividends and make other distributions on our capital stock, and redeem and repurchase our capital stock;

make investments, including acquisitions;

enter into transactions with affiliates; and

make capital expenditures.

Our credit facility also contains customary affirmative covenants, including, among other things, requirements to: take certain actions in the event we form or acquire new subsidiaries; hold annual meetings with our lenders; provide copies of material contracts and amendments to our lenders; locate our collateral only at specified locations; and use commercially reasonable efforts to ensure that certain material contracts permit the assignment of the contract to our lenders; subject in each case to customary exceptions and qualifications. We are also required to comply with a fixed charge coverage ratio, which is a ratio of our EBITDA to our fixed charges as determined in accordance with the credit facility, of 1.25:1.00 for each 12-month period ending at the end of a fiscal quarter, and a senior leverage ratio, which is a ratio of the outstanding revolver usage to our EBITDA as determined in accordance with the credit facility, of 2.75:1.00 for each fiscal quarter.

The credit facility contains customary events of default, subject to customary cure periods for certain defaults, that include, among others, non-payment defaults, covenant defaults, material judgment defaults, bankruptcy and insolvency defaults, cross-defaults to certain other material indebtedness, inaccuracy of representations and warranties and a failure to meet certain liquidity thresholds both before and after we make cash payments for earnouts and holdbacks in connection with acquisition transactions.

If we experience a decline in cash flow due to any of the factors described in this "Risk Factors" section or otherwise, we could have difficulty paying interest and principal amounts due on our indebtedness and meeting the financial covenants set forth in our credit facility. If we are unable to generate sufficient cash flow or otherwise obtain the funds necessary to make required payments under our credit facility, or if we fail to comply with the requirements of our indebtedness, we could default under our credit facility. Any default that is not cured or waived could result in the acceleration of the obligations under the credit facility, an increase in the applicable interest rate under the credit facility and a requirement that our subsidiaries that have guaranteed the credit facility pay the obligations in full, and would permit our lender to exercise remedies with respect to all of the collateral that is securing the credit facility, including substantially all of our and our subsidiary guarantors' assets. Any such default could have a material adverse effect on our liquidity and financial condition.



## Edgar Filing: REALPAGE INC - Form 10-Q

Even if we comply with all of the applicable covenants, the restrictions on the conduct of our business could adversely affect our business by, among other things, limiting our ability to take advantage of financings, mergers, acquisitions and other corporate opportunities that may be beneficial to the business. Even if the credit facility was terminated, additional debt we could incur in the future may subject us to similar or additional covenants.

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

The software and technology industries are characterized by the existence of a large number of patents, copyrights, trademarks and trade secrets and by frequent litigation based on allegations of infringement, misappropriation, misuse and other violations of

---

**Table of Contents**

intellectual property rights. We have received in the past, and may receive in the future, communications from third parties claiming that we have infringed or otherwise misappropriated the intellectual property rights of others. Our technologies may not be able to withstand any third-party claims against their use. Since we currently have no patents, we may not use patent infringement as a defensive strategy in such litigation. Additionally, although we have licensed from other parties proprietary technology covered by patents, we cannot be certain that any such patents will not be challenged, invalidated or circumvented. If such patents are invalidated or circumvented, this may allow existing and potential competitors to develop products and services that are competitive with, or superior to, our solutions.

Many of our customer agreements require us to indemnify our customers for certain third-party claims, such as 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 or settlement related to any such claims. These types of claims could harm our relationships with our customers, may deter future customers from purchasing our solutions or could expose us to litigation for these claims. Even if we are not a party to any litigation between a customer and a third party, an adverse outcome in any such litigation could make it more difficult for us to defend our intellectual property in any subsequent litigation in which we are a named party.

On January 24, 2011, one of our competitors, Yardi Systems, Inc. filed a lawsuit in the U.S. District Court for the Central District of California against RealPage, Inc. and DC Consulting, Inc. Yardi filed. The lawsuit alleged claims for relief for violation of the Computer Fraud and Abuse Act, violation of the California Comprehensive Data Access and Fraud Act, violation of the Digital Millennium Copyright Act, copyright infringement, trade secret misappropriation, unfair competition, and inducement of breach of contract. Yardi sought injunctive relief, punitive damages, recovery of all profits attributable to the defendants' allegedly wrongful acts and infringements, statutory damages, exemplary damages, prejudgment interest, and attorneys' fees and costs. Yardi alleged, among other things, that the Company took Yardi employee, client and independent consultant credentials and used them to access Yardi's computer system and steal Yardi's trade secrets and copyrighted software, related support documentation, price lists and other proprietary information. In addition, Yardi alleged that the Company improperly obtained administrative-level access to Yardi's software and copied it onto the Company's servers for its own competitive purposes, used these unauthorized software copies to discover the allegedly proprietary programming, functionality and feature set of Yardi's software, to compete unfairly against Yardi, to create unauthorized derivative works from Yardi's software, and to enhance the Company's own products and services. Yardi alleged that in doing so, and in offering to indemnify our customers, the Company induced Cloud customers to violate their confidentiality and other agreements with Yardi. The Company answered Yardi's complaint and also filed counterclaims against Yardi. The Company's counterclaims alleged that Yardi and its agents wrongfully obtained and used our trade secrets and engaged in anti-competitive behavior with respect to certain of our clients. The Company's counterclaims sought relief for Yardi's misappropriation of the Company's trade secrets, Sherman Act (antitrust) violations and California Cartwright Act violations, intentional interference with contract, intentional interference with prospective economic advantage, and violation of California's unfair competition statute. The Company sought damages, punitive damages, injunctive relief and all profits, gains and advantages that Yardi received as a result of its wrongful conduct along with attorneys' fees and costs. On July 1, 2012, the Company and Yardi entered into a comprehensive settlement of all outstanding litigation between them, and the lawsuit was dismissed. As part of the settlement, Yardi and the Company granted each other perpetual licenses and rights to substantially expanded interfaces so that clients can experience a more full-featured integration between the Company and Yardi applications. The parties also established ongoing testing environments to ensure that the interfaces operate smoothly as designed. In addition, Yardi granted the Company a license to certain patents.

On March 26, 2010, Smarter Agent, LLC, a provider of mobile real estate applications, filed a complaint against one of our subsidiaries, Multifamily Technology Solutions, Inc., and multiple other defendants for patent infringement in the U.S. District Court for the District of Delaware. The complaint alleges, among other things, that our mobile technology infringes three patents held by Smarter Agent purporting to cover: a Global positioning-based real estate database access device and method, a Position-based information access device and method and a Position-based information access device and method of searching, and seeks injunctive relief, unspecified damages, enhanced damages, prejudgment interest, and attorneys' fees and costs. We have denied the allegations and asserted counterclaims seeking declarations that we are not infringing the patents and that the patents are invalid. In November 2010, the U.S. Patent and Trademark Office granted our petition for re-examination of the three patents-in-suit and its first office action found all claims invalid. Smarter Agent submitted arguments to overcome the objections, but the U.S. Patent and Trademark Office has finally rejected two of the patents, with final action on one still pending. In March 2011, the court stayed the litigation pending the completion of the re-examination proceedings and any related appeals. Because this lawsuit is at an early stage, it is not possible to predict its outcome. We intend to defend this case and pursue our counterclaims vigorously. However, even if we were successful in defending against such claims or in prevailing on our counterclaims, the proceedings could result in significant costs and divert management's attention.

The Smarter Agent, LLC litigation or other similar litigation could force us to stop selling, incorporating or using our solutions

---

## **Table of Contents**

that include the challenged intellectual property or redesign those solutions that use the technology. In addition, we may have to pay damages if we are found to be in violation of a third party's rights. We may have to procure a license for the technology, which may not be available on reasonable terms, if at all, may significantly increase our operating expenses or may require us to restrict our business activities in one or more respects. As a result, we may also be required to develop alternative non-infringing technology, which could require significant effort and expense. There is no assurance that we would be able to develop alternative solutions or, if alternative solutions were developed, that they would perform as required or be accepted in the relevant markets. In some instances, if we are unable to offer non-infringing technology, or obtain a license for such technology, we may be required to refund some or the entire license fee paid for the infringing technology by our customers.

Our exposure to risks associated with the use of intellectual property may be increased as a result of acquisitions, as we have a lower level of visibility into the development process with respect to acquired technology or the care taken to safeguard against infringement risks. Third parties may make infringement and similar or related claims after we have acquired technology that had not been asserted prior to our acquisition.

***Any failure to protect and successfully enforce our intellectual property rights could compromise our proprietary technology and impair our brands.***

Our success depends significantly on our ability to protect our proprietary rights to the technologies we use in our solutions. If we are unable to protect our proprietary rights adequately, our competitors could use the intellectual property we have developed to enhance their own products and services, which could harm our business. 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. We currently have no issued patents or pending patent applications and may be unable to obtain patent protection in the future. In addition, if any patents are issued in the future, they may not provide us with any competitive advantages, may not be issued in a manner that gives us the protection that we seek and may be successfully challenged by third parties. Unauthorized parties may attempt to copy or otherwise obtain and use the technologies underlying our solutions. Monitoring unauthorized use of our technologies is difficult, and we do not know whether the steps we have taken will prevent unauthorized use of our technology. If we are unable to protect our proprietary rights, we may find ourselves at a competitive disadvantage to others who have not incurred the substantial expense, time and effort required to create similar innovative products.

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. If we are unable to secure new marks, maintain already existing marks and enforce the rights to use such marks against unauthorized third-party use, our ability to brand, identify and promote our solutions in the marketplace could be impaired, which could harm our business.

We customarily enter into agreements with our employees, contractors and certain 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, we may be required to release the source code of our software to third parties under certain circumstances. For example, some of our customer agreements provide that if we cease to maintain or support a certain solution without replacing it with a successor solution, then we may be required to release the source code of the software underlying such solution. In addition, 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 legal actions being successful against these infringers, but these actions may not be successful, even when our rights have been infringed. Furthermore, 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.

Additionally, if we sell our solutions internationally in the future, effective patent, trademark, service mark, copyright and trade secret protection may not be available or as robust in every country in which our solutions are available. As a result, we may not be able to effectively prevent competitors outside the United States from infringing or otherwise misappropriating our intellectual property rights, which could reduce our competitive advantage and ability to compete or otherwise harm our business.

***We may be unable to halt the operations of websites that aggregate or misappropriate data from our LeaseStar websites.***

From time to time, third parties have misappropriated data from our LeaseStar websites through website scraping, robots or other means and aggregated this data on their websites with data from other companies. In addition, copycat websites have misappropriated data on our network and attempted to imitate our brand or the functionality of our website. When we have become aware of such websites, we have employed technological or legal measures in an attempt to halt their operations. However, we may be unable to detect all such websites in a timely manner and, even if we could, technological and legal measures may be insufficient to halt their operations. In some cases, particularly in the case of websites operating outside of the United States, our available remedies may not be adequate to protect us against the impact of the operation of such websites. Regardless of whether we can successfully enforce our rights against the operators of these websites, any measures that we may

take could require us to expend

---

**Table of Contents**

significant financial or other resources, which could harm our business, results of operations or financial condition. In addition, to the extent that such activity creates confusion among consumers or advertisers, our brand and business could be harmed.

***Current and future legal proceedings against us could be costly and time consuming to defend.***

We are from time to time subject to legal proceedings and claims that arise in the ordinary course of business, including claims brought by our customers in connection with commercial disputes, claims brought by our customers' current or prospective residents, including potential class action lawsuits based on asserted statutory or regulatory violations, employment-based claims made by our current or former employees, administrative agencies, or government regulators. Litigation, enforcement actions, and other legal proceedings, regardless of their outcome, may result in substantial costs and may divert management's attention and our resources, which may harm our business, overall financial condition and operating results. In addition, legal claims that have not yet been asserted against us may be asserted in the future. Although we maintain insurance, there is no guarantee that such insurance will be available or sufficient to cover any such legal proceedings or claims. For example, insurance may not cover or may dispute coverage of such legal proceedings or claims, even after proceeds under such insurance policies have been received by us. In addition, insurance may not be sufficient for one or more such legal proceedings or claims and may not continue to be available on terms acceptable to us, or at all. A legal proceeding or claim brought against us that is uninsured or underinsured could result in unanticipated costs, thereby harming our operating results.

On January 24, 2011, Yardi Systems, Inc. filed a lawsuit in the U.S. District Court for the Central District of California against RealPage, Inc. and DC Consulting, Inc. (this lawsuit and the related litigation, the "Yardi Lawsuit"). Yardi filed a First Amended Complaint on August 12, 2011. The lawsuit alleged claims for relief for violation of the Computer Fraud and Abuse Act, violation of the California Comprehensive Data Access and Fraud Act, violation of the Digital Millennium Copyright Act, copyright infringement, trade secret misappropriation, unfair competition, and inducement of breach of contract. Yardi sought injunctive relief, punitive damages, recovery of all profits attributable to Defendants' alleged wrongful acts and infringements, statutory damages, exemplary damages, prejudgment interest, and attorneys' fees and costs. The First Amended Complaint alleged, among other things, that the Company took Yardi employee, client and independent consultant credentials, and used them to access Yardi's computer system and steal Yardi's trade secrets and copyrighted software, related support documentation, price lists and other proprietary information. In addition, the First Amended Complaint alleged that the Company improperly obtained administrative-level access to Yardi's software and copied it onto the Company's servers for its own competitive purposes, used these unauthorized software copies to discover the allegedly proprietary programming, functionality and feature set of Yardi's software, to compete unfairly against Yardi, to create unauthorized derivative works from Yardi's software, and to enhance the Company's own products and services. Yardi alleged that in doing so, and in offering to indemnify our customers, the Company induced Cloud customers to violate their confidentiality and other agreements with Yardi. On March 28, 2011, the Company filed an answer to Yardi's Complaint, and on September 12, 2011 the Company answered the First Amended Complaint. The Company also filed counterclaims against Yardi, first in connection with its March 28 answer and then in First Amended Counterclaims filed on May 18, 2011. On September 2, 2011, following the Court's order granting in part and denying in part Yardi's motion to dismiss certain of the Company's causes of action without prejudice, the Company filed Second Amended Counterclaims. The Company's counterclaims alleged that Yardi and its agents wrongfully obtained and used our trade secrets and engaged in anti-competitive behavior with respect to certain of our clients. The Company's counterclaims sought relief for misappropriation of trade secrets, Sherman Act (antitrust) violations and California Cartwright Act violations, intentional interference with contract, intentional interference with prospective economic advantage, and violation of California's unfair competition statute. The Company sought damages, punitive damages, injunctive relief and all profits, gains and advantages that Yardi received as a result of its wrongful conduct along with attorneys' fees and costs. Yardi filed a Motion to Dismiss the Company's Second Amended Counterclaims on September 30, 2011. On February 13, 2012, the Court denied Yardi's motion with respect to all claims except for a portion of one of our claims for intentional interference with contract, as to which dismissal was granted. On July 1, 2012, the Company and Yardi Systems entered into a Settlement Agreement resolving all outstanding litigation between the parties. The Settlement Agreement also includes a license of certain Yardi intellectual property to the Company and a license of certain of our intellectual property to Yardi.

In connection with the Yardi Lawsuit, the Company made claims for reimbursement against each of its primary and excess layer general liability and professional liability insurance carriers. Each of our primary and excess layer professional liability insurance carriers other than Homeland Insurance of New York ("Homeland") reimbursed the Company up to each of its policy limits. On July 19, 2012, we became aware of assertions by one of our primary layer insurance carriers that such carrier no longer considered the previously reimbursed \$5.0 million payment covered under such policy, and that the carrier demanded reimbursement of the \$5.0 million payment that the carrier had previously reimbursed to us. The Company disputes this assertion by the carrier. We intend to defend these allegations and to pursue coverage and other appropriate relief in connection with this insurance policy. It is not possible to predict the outcome of this insurance matter, and as such, we have not recorded a contingent liability as we believe an unfavorable outcome is not probable as of the date of this filing.

In addition, in connection with the Yardi Lawsuit, the Company has an excess professional liability insurance policy with Homeland that provides an additional \$5.0 million of coverage above the amounts previously reimbursed to us. The Company made claims for reimbursement under the Homeland policy with respect to the Yardi Lawsuit, but Homeland denied such claims and never made payment to us. On May 30,

## Edgar Filing: REALPAGE INC - Form 10-Q

2012, Homeland filed a motion for declaratory judgment against the Company in the United States District Court for the Northern District of Texas seeking a determination by the court that Homeland's policy does not provide coverage for amounts incurred in connection with the Yardi Lawsuit. We have not recorded any amounts as recoverable in relation to the Homeland insurance policy as of June 30, 2012.

In March 2010, the District Attorney of Ventura County, California issued an administrative subpoena to us seeking certain information related to our provision of utility billing services in the State of California. A representative of the District Attorney has informed us that the subpoena was issued in connection with a general investigation of industry practices with respect to utility billing

---

**Table of Contents**

in California. Utility billing is subject to regulation by state law and various state administrative agencies, including, in California, the California Public Utility Commission, or the CPUC, and the Division of Weights and Measures, or the DWM. We have provided the District Attorney with the information requested in the subpoena. In late August 2010, we received limited, follow-up requests for information to which we have responded. The District Attorney's office has not initiated an administrative or other enforcement action against us, nor have they asserted any violations of the applicable regulations by us. Given the early stage of this investigation, it is difficult to predict its outcome and whether the District Attorney will pursue an administrative or other enforcement action against us in the State of California and what the result of any such action would be. However, penalties or assessments of violations of regulations promulgated by the CPUC or DWM or other regulators may be calculated on a per occurrence basis. Due to the large number of billing transactions we process for our customers in California, our potential liability in an enforcement action could be significant. If the District Attorney ultimately pursues an administrative or other enforcement action against us, we believe that we have meritorious defenses to the potential claims and would defend them vigorously. However, even if we were successful in defending against such claims, the proceedings could result in significant costs and divert management's attention.

On March 26, 2010, Smarter Agent, LLC, a provider of mobile real estate applications, filed a complaint against our subsidiary, Multifamily Technology Solutions, Inc., and multiple other defendants for patent infringement in the U.S. District Court for the District of Delaware. The complaint alleges, among other things, that our mobile technology infringes three patents held by Smarter Agent purporting to cover: a Global positioning-based real estate database access device and method, a Position-based information access device and method and a Position-based information access device and method of searching, and seeks injunctive relief, unspecified damages, enhanced damages, prejudgment interest, and attorneys' fees and costs. We have denied the allegations and asserted counterclaims seeking declarations that we are not infringing the patents and that the patents are invalid. In November 2010, the U.S. Patent and Trademark Office granted our petition for re-examination of the three patents-in-suit and its first office action found all claims invalid. Smarter Agent has submitted arguments to overcome the objections, but the U.S. Patent and Trademark Office has finally rejected two of the patents, with final action on the remaining one still pending. In March 2011, the court stayed the litigation pending the completion of the re-examination proceedings and any related appeals. Because this lawsuit is at an early stage, it is not possible to predict its outcome. We intend to defend this case and pursue our counterclaims vigorously. However, even if we were successful in defending against such claims or in prevailing on our counterclaims, the proceedings could result in significant costs and divert management's attention.

***We could be sued for contract, warranty or product liability claims, and such lawsuits may disrupt our business, divert management's attention and our financial resources or have an adverse effect on our financial results.***

We provide warranties to customers of certain of our solutions and services relating primarily to product functionality, network uptime, critical infrastructure availability and hardware replacement. General errors, defects, inaccuracies or other performance problems in the software applications underlying our solutions or inaccuracies in or loss of the data we provide to our customers could result in financial or other damages to our customers. Additionally, errors associated with any delivery of our services, including utility billing, could result in financial or other damages to our customers. There can be no assurance that any limitations of liability set forth in our contracts would be enforceable or would otherwise protect us from liability for damages. We maintain general liability insurance coverage, including coverage for errors and omissions, in amounts and under terms that we believe are appropriate. There can be no assurance that this coverage will continue to be available on terms acceptable to us, or at all, or in sufficient amounts to cover one or more large product liability claims, or that the insurer will not deny coverage for any future claim or dispute coverage of such legal proceedings or claims even after proceeds under such insurance policies have been received by us. The successful assertion of one or more large product liability claims against us that exceeds available insurance coverage, could have a material adverse effect on our business, prospects, financial condition and results of operations.

***If we fail to develop our brands cost-effectively, our financial condition and operating results could be harmed.***

We market our solutions under discrete brand names. We believe that developing and maintaining awareness of our brands is critical to achieving widespread acceptance of our existing and future solutions and is an important element in attracting new customers and retaining our existing customers. Additionally, we believe that developing these brands in a cost-effective manner is critical in meeting our expected margins. In the past, our efforts to build our brands have involved significant expenses and we intend to continue to make expenditures on brand promotion. Brand promotion activities may not yield increased revenue, and even if they do, any increased revenue may not offset the expenses we incurred in building our brands. If we fail to cost-effectively build and maintain our brands, we may fail to attract new customers or retain our existing customers, and our financial condition and results of operations could be harmed.

***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 that needs to be re-evaluated frequently. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial

Edgar Filing: REALPAGE INC - Form 10-Q

statements in accordance with GAAP. Beginning with the year ended December 31, 2011,



---

## **Table of Contents**

we are required to be in compliance with Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, which requires annual management assessment of the effectiveness of our internal control over financial reporting and a report by our independent auditors. 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, harm our ability to operate our business and reduce the trading price of our stock.

***Changes in, or errors in our interpretations and applications of, financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported results of operations.***

A change in accounting standards or practices can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and may occur in the future. Changes to existing rules or the questioning of current practices or errors in our interpretations and applications of financial accounting standards or practices may adversely affect our reported financial results or the way in which we conduct our business.

***We have incurred, and will incur, increased costs and demands upon management as a result of complying with the laws and regulations affecting public companies, which could harm our operating results.***

As a public company, we have incurred, and will incur, significant legal, accounting, investor relations and other expenses that we did not incur as a private company, including costs associated with public company reporting requirements. We also have incurred and will 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 Exchange Commission and The NASDAQ Stock Market LLC. We expect these rules and regulations to increase our legal and financial compliance costs substantially and to make some activities more time-consuming and costly. As a public company, it is more expensive for us to obtain director and officer liability insurance and that 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.

***Government regulation of the rental housing industry, including background screening services and utility billing, the Internet and e-commerce is evolving, and changes in regulations or our failure to comply with regulations could harm our operating results.***

The rental housing industry is subject to extensive and complex federal, state and local regulations. Our services and solutions must work within the extensive and evolving regulatory requirements applicable to our customers and third-party service providers, including, but not limited to, those under the Fair Credit Reporting Act, the Fair Housing Act, the Deceptive Trade Practices Act, the DPPA, the Gramm-Leach-Bliley Act, the Fair and Accurate Credit Transactions Act, the Privacy Rules, Safeguards Rule and Consumer Report Information Disposal Rule promulgated by the Federal Trade Commission, or FTC, the regulations of the United States Department of Housing and Urban Development, or HUD, HIPAA/HITECH and complex and divergent state and local laws and regulations related to data privacy and security, credit and consumer reporting, deceptive trade practices, discrimination in housing, utility billing and energy and gas consumption. These regulations are complex, change frequently and may become more stringent over time. Although we attempt to structure and adapt our solutions and service offerings to comply with these complex and evolving laws and regulations, we may be found to be in violation. If we are found to be in violation of any applicable laws or regulations, we could be subject to administrative and other enforcement actions as well as class action lawsuits or demands for client reimbursement. Additionally, many applicable laws and regulations provide for penalties or assessments on a per occurrence basis. Due to the nature of our business, the type of services we provide and the large number of transactions processed by our solutions, our potential liability in an enforcement action or class action lawsuit could be significant. In addition, entities such as HUD and the FTC have the authority to promulgate rules and regulations that may impact our customers and our business. 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 personally identifiable information or consumer information could affect our customers' ability to use and share data, potentially reducing demand for our on demand software solutions.

Some of our LeaseStar products operate under the real estate brokerage laws of numerous states and require maintaining licenses in many of these states. Brokerage laws in these states could change, affecting our ability to do provide some LeaseStar products in these states.

We deliver our on demand software solutions over the Internet and sell and market certain of our solutions over the Internet. As Internet commerce continues to evolve, increasing regulation by federal, state or foreign agencies becomes more likely. Taxation of products or 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 information exchange over the Internet could result in a decline in the use of the Internet and the viability of on demand software solutions, which could harm our business and operating results.

***Our business is subject to the risks of international operations.***



## **Table of Contents**

Compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business. These numerous and sometimes conflicting laws and regulations include internal control and disclosure rules, data privacy and filtering requirements, anti-corruption laws, such as the Foreign Corrupt Practices Act, and other local laws prohibiting corrupt payments to governmental officials, and antitrust and competition regulations, among others.

Violations of these laws and regulations could result in fines and penalties, criminal sanctions against us, our officers, or our employees, prohibitions on the conduct of our business and on our ability to carry on operations in one or more countries, and could also materially affect our brand, our international expansion efforts, our ability to attract and retain employees, our business, and our operating results. Although we have implemented policies and procedures designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, or agents will not violate our policies.

In addition, we are subject to a variety of risks inherent in doing business internationally, including:

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

limitations of local infrastructure;

fluctuations in currency exchange rates;

higher levels of credit risk and payment fraud;

reduced protection for intellectual property rights in some countries;

difficulties in staffing and managing global operations and the increased travel, infrastructure, and legal compliance costs associated with multiple international locations; and

compliance with statutory equity requirements and management of tax consequences.

If we are unable to manage the complexity of our international operations successfully, our financial results could be adversely affected.

***Our LeasingDesk insurance business is subject to governmental regulation which could reduce our profitability or limit our growth.***

Through our wholly owned subsidiary, Multifamily Internet Ventures LLC, we hold insurance agent licenses from a number of individual state departments of insurance and are subject to state governmental regulation and supervision in connection with the operation of our LeasingDesk insurance business. This state governmental supervision could reduce our profitability or limit the growth of our LeasingDesk insurance business by increasing the costs of regulatory compliance, limiting or restricting the solutions we provide or the methods by which we provide them or subjecting us to the possibility of regulatory actions or proceedings. Our continued ability to maintain these insurance agent licenses in the jurisdictions in which we are licensed depends on our compliance with the rules and regulations promulgated from time to time by the regulatory authorities in each of these jurisdictions. Furthermore, state insurance departments conduct periodic examinations, audits and investigations of the affairs of insurance agents.

In all jurisdictions, the applicable laws and regulations are subject to amendment or interpretation by regulatory authorities. Generally, such authorities are vested with relatively broad discretion to grant, renew and revoke licenses and approvals and to implement regulations. Accordingly, we may be precluded or temporarily suspended from carrying on some or all of the activities of our LeasingDesk insurance business or otherwise be fined or penalized in a given jurisdiction. No assurances can be given that our LeasingDesk insurance business can continue to be conducted in any given jurisdiction as it has been conducted in the past.

***We generate commission revenue from the insurance policies we sell as a registered insurance agent and if insurance premiums decline or if the insureds experience greater than expected losses, our revenues could decline and our operating results could be harmed.***

Through our wholly owned subsidiary, Multifamily Internet Ventures LLC, a managing general insurance agency, we generate commission revenue from offering liability and renter's insurance. Additionally, Multifamily Internet Ventures LLC has recently commenced the sale of additional insurance products, including auto and other personal lines insurance, to residents that buy renter's insurance from us. These policies are ultimately underwritten by various insurance carriers. Some of the property owners and managers that participate in our programs opt to require residents to purchase rental insurance policies and agree to grant to Multifamily Internet Ventures LLC exclusive marketing rights at their properties. If demand for residential rental housing declines, property owners and managers may be forced to reduce their rental rates and to stop requiring the purchase of rental insurance in order to reduce the overall cost of renting. If property owners or managers cease to require renter's insurance, elect to offer policies from competing providers or insurance premiums decline, our revenues from selling insurance policies will be adversely affected.

Additionally, one type of commission paid by insurance carriers to Multifamily Internet Ventures LLC is contingent commission, which is based on claims experienced at the properties for which the residents purchase insurance. In the event that claims by the insureds increase unexpectedly, the contingent commission we typically earn will be adversely affected. As a result, our quarterly operating results could fall below the expectations of analysts or investors, in which event our stock price may decline.

Multifamily Internet Ventures LLC is required to maintain a 50-state general agency insurance license as well as individual insurance licenses for each sales agent involved in the solicitation of insurance products. Both the agency and individual licenses require compliance with state insurance regulations, payment of licensure fees, and continuing education programs. In the event that regulatory compliance requirements are not met, Multifamily Internet Ventures LLC could be subject to license suspension or revocation, state Department of Insurance audits, and regulatory fines. As a result, our ability to engage in the business of insurance could be restricted, and our operating revenue will be adversely affected.

***Our ability to use net operating losses to offset future taxable income may be subject to certain limitations.***

In general, under Section 382 of the Internal Revenue Code of 1986, as amended, or the Internal Revenue Code, a corporation that undergoes an ownership change is subject to limitations on its ability to utilize its pre-change net operating losses, or NOLs, to

---

## **Table of Contents**

offset future taxable income. Our ability to utilize NOLs of companies that we may acquire in the future may be subject to limitations. Future changes in our stock ownership, some of which are outside of our control, could result in an ownership change under Section 382 of the Internal Revenue Code. For these reasons, we may not be able to utilize a material portion of the NOLs reflected on our balance sheet, even if we maintain profitability.

*If we are required to collect sales and use taxes on the solutions we sell in additional taxing jurisdictions, we may be subject to liability for past sales and our future sales may decrease.*

States and some local taxing jurisdictions have differing rules and regulations governing sales and use taxes, and these rules and regulations are subject to varying interpretations that may change over time. We review these rules and regulations periodically and currently collect and remit sales taxes in taxing jurisdictions where we believe we are required to do so. However, additional state and/or local taxing jurisdictions may seek to impose sales or other tax collection obligations on us, including for past sales. A successful assertion that we should be collecting additional sales or other taxes on our solutions could result in substantial tax liabilities for past sales, discourage customers from purchasing our solutions or may otherwise harm our business and operating results. This risk is greater with regard to solutions acquired through acquisitions.

We may also become subject to tax audits or similar procedures in jurisdictions where we already collect and remit sales taxes. A successful assertion that we have not collected and remitted taxes at the appropriate levels may also result in substantial tax liabilities for past sales. Liability for past taxes may also include very substantial interest and penalty charges. Our customer contracts provide that our customers must pay all applicable sales and similar taxes. Nevertheless, customers may be reluctant to pay back taxes and may refuse responsibility for interest or penalties associated with those taxes. If we are required to collect and pay back taxes and the associated interest and penalties, and if our customers fail or refuse to reimburse us for all or a portion of these amounts, we will incur unplanned expenses that may be substantial. Moreover, imposition of such taxes on our solutions going forward will effectively increase the cost of such solutions to our customers and may adversely affect our ability to retain existing customers or to gain new customers in the areas in which such taxes are imposed.

*Changes in our effective tax rate could harm our future operating results.*

We are subject to federal and state income taxes in the United States and various foreign jurisdictions, and our domestic and international tax liabilities are subject to the allocation of expenses in differing jurisdictions. Our tax rate is affected by changes in the mix of earnings and losses in jurisdictions with differing statutory tax rates, including jurisdictions in which we have completed or may complete acquisitions, certain non-deductible expenses arising from the requirement to expense stock options and the valuation of deferred tax assets and liabilities, including our ability to utilize our net operating losses. Increases in our effective tax rate could harm our operating results.

*We rely on our management team and need additional personnel to grow our business, and the loss of one or more key employees or our inability to attract and retain qualified personnel could harm our business.*

Our success and future growth depend on the skills, working relationships and continued services of our management team. The loss of our Chief Executive Officer or other senior executives could adversely affect our business. Our future success also will depend on our ability to attract, retain and motivate highly skilled software developers, marketing and sales personnel, technical support and product development personnel in the United States and internationally. All of our employees work for us on an at-will basis. Competition for these types of personnel is intense, particularly in the software industry. As a result, we may be unable to attract or retain qualified personnel. Our inability to attract and retain the necessary personnel could adversely affect our business.

*Our corporate culture has contributed to our success, and if we cannot maintain this culture as we grow, we could lose the innovation, creativity and teamwork fostered by our culture, and our business may be harmed.*

We believe that a strong corporate culture that nurtures core values and philosophies is essential to our long-term success. We call these values and philosophies the RealPage Promise and we seek to practice the RealPage Promise in our actions every day. The RealPage Promise embodies our corporate values with respect to customer service, investor communications, employee respect and professional development and management decision-making and leadership. As our organization grows and we are required to implement more complex organizational structures, we may find it increasingly difficult to maintain the beneficial aspects of our corporate culture which could negatively impact our future success.

### **Risks Related to Ownership of our Common Stock**

*The concentration of our capital stock owned by insiders may limit your ability to influence corporate matters.*

## Edgar Filing: REALPAGE INC - Form 10-Q

Our executive officers, directors, and entities affiliated with them together beneficially owned approximately 51.3% of our common stock as of June 30, 2012. Further, Stephen T. Winn, our Chief Executive Officer and Chairman of the Board, and entities

**Table of Contents**

beneficially owned by Mr. Winn held an aggregate of approximately 36.9% of our common stock as of June 30, 2012. This significant concentration of ownership may adversely affect the trading price for our common stock because investors often perceive disadvantages in owning stock in companies with controlling stockholders. Mr. Winn and entities beneficially owned by Mr. Winn may control our management and affairs and matters requiring stockholder approval, including the election of directors and the approval of significant corporate transactions, such as mergers, consolidations or the sale of substantially all of our assets. Consequently, this concentration of ownership may have the effect of delaying or preventing a change of control, including a merger, consolidation or other business combination involving us, or discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control, even if that change of control would benefit our other stockholders.

***The trading price of our common stock price may be volatile.***

The trading price of our common stock could be subject to wide fluctuations in response to various factors, including, but not limited to, those described in this Risk Factors section, some of which are beyond our control. Factors affecting the trading price of our common stock include:

variations in our operating results or in expectations regarding our operating results;

variations in operating results of similar companies;

announcements of technological innovations, new solutions or enhancements, strategic alliances or agreements by us or by our competitors;

announcements by competitors regarding their entry into new markets, and new product, service and pricing strategies;

marketing, advertising or other initiatives by us or our competitors;

the gain or loss of customers;

threatened or actual litigation;

major changes in our board of directors or management;

recruitment or departure of key personnel;

changes in the estimates of our operating results or changes in recommendations by any research analysts that elect to follow our common stock;

market conditions in our industry and the economy as a whole;

the overall performance of the equity markets;

sales of our shares of common stock by existing stockholders;

volatility in our stock price, which may lead to higher stock-based compensation expense under applicable accounting standards; and

adoption or modification of regulations, policies, procedures or programs applicable to our business.

In addition, the stock market in general, and the market for technology and specifically Internet-related companies, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may harm the market price of our common stock regardless of our actual operating performance. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. This litigation, if instituted against us, could result in substantial costs and a diversion of our management's attention and our resources, whether or not we are successful in such litigation.



## **Table of Contents**

### ***Our stock price could decline due to the large number of outstanding shares of our common stock eligible for future sale.***

Sales of substantial amounts of our common stock in the public market, or the perception that these sales could occur, could cause the market price of our common stock to decline. These sales could also make it more difficult for us to sell equity or equity-related securities in the future at a time and price that we deem appropriate.

As of June 30, 2012, we had 73,658,956 shares of common stock outstanding. Of these shares, 72,626,599 were immediately tradable without restriction or further registration under the Securities Act, unless these shares are held by affiliates, as that term is defined in Rule 144 under the Securities Act.

As of June 30, 2012, holders of 29,493,125 shares, or approximately 40.0%, of our outstanding common stock were entitled to rights with respect to the registration of these shares under the Securities Act. If we register their shares of common stock, these stockholders could sell those shares in the public market without being subject to the volume and other restrictions of Rule 144 and Rule 701.

In addition, we have registered approximately 20,934,259 shares of common stock that have been issued or reserved for future issuance under our stock incentive plans. Of these shares, 3,524,928 shares were eligible for sale upon the exercise of vested options as of June 30, 2012.

### ***Our charter documents and Delaware law could prevent a takeover that stockholders consider favorable and could also reduce the market price of our stock.***

Our amended and restated certificate of incorporation and our amended and restated bylaws contain provisions that could delay or prevent a change in control of our company. These provisions could also make it more difficult for stockholders to elect directors and take other corporate actions. These provisions include:

a classified board of directors whose members serve staggered three-year terms;

not providing for cumulative voting in the election of directors;

authorizing our board of directors to issue, without stockholder approval, preferred stock with rights senior to those of our common stock;

prohibiting stockholder action by written consent; and

requiring advance notification of stockholder nominations and proposals.

These and other provisions of our amended and restated certificate of incorporation and our amended and restated bylaws and under Delaware law could discourage potential takeover attempts, reduce the price that investors might be willing to pay in the future for shares of our common stock and result in the market price of our common stock being lower than it would be without these provisions.

### ***If securities analysts do not continue to publish research or reports about our business or if they publish negative evaluations of our stock, the price of our stock could decline.***

We expect that the trading price for our common stock may be affected by research or reports that industry or financial analysts publish about us or our business. If one or more of the analysts who cover us downgrade their evaluations of our stock, the price of our stock could decline. If one or more of these analysts cease coverage of our company, we could lose visibility in the market for our stock, which in turn could cause our stock price to decline.

### ***We do not anticipate paying any dividends on our common stock.***

## Edgar Filing: REALPAGE INC - Form 10-Q

We do not anticipate paying any cash dividends on our common stock in the foreseeable future. If we do not pay cash dividends, you would receive a return on your investment in our common stock only if the market price of our common stock has increased when you sell your shares. In addition, the terms of our credit facilities currently restrict our ability to pay dividends.

**Table of Contents****Item 6. Exhibits.**

The exhibits required to be furnished pursuant to Item 6 are listed in the Exhibit Index filed herewith, which Exhibit Index is incorporated herein by reference.

**SIGNATURES**

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

Date: August 7, 2012

RealPage, Inc.

By /s/ Timothy J. Barker

Timothy J. Barker  
Chief Financial Officer and Treasurer

**EXHIBIT INDEX**

Exhibit Number	Exhibit Description	Incorporated by Reference			Filed Herewith
		Form	Date	Number	
3.1	Amended and Restated Certificate of Incorporation of the Registrant	S-1	07/26/2010	3.2	
3.2	Amended and Restated Bylaws of the Registrant	S-1	07/26/2010	3.4	
4.1	Form of Common Stock certificate of the Registrant	S-1	07/26/2010	4.1	
4.2	Shareholders Agreement among the Registrant and certain stockholders, dated December 1, 1998, as amended July 16, 1999 and November 3, 2000	S-1	04/29/2010	4.2	
4.3	Second Amended and Restated Registration Rights Agreement among the Registrant and certain stockholders, dated February 22, 2008	S-1	04/29/2010	4.3	
4.4	Registration Rights Agreement among the Registrant and certain stockholders, dated November 3, 2010	10-Q	11/05/2010	4.4	
4.5	Registration Rights Agreement among the Registrant and certain stockholders, dated August 24, 2011	10-Q	11/08/2011	4.5	
10.1	Form of 2012 Management Incentive Plan	8-K	2/27/2012	10.1	
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 153-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				X
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 153-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				X
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*				
32.2	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*				
101.INS	Instance				X

Edgar Filing: REALPAGE INC - Form 10-Q

101.SCH	Taxonomy Extension Schema	X
101.CAL	Taxonomy Extension Calculation	X

**Table of Contents**

<b>Exhibit</b>		<b>Incorporated by Reference</b>			
		<b>Form</b>	<b>Date</b>	<b>Number</b>	<b>Filed Herewith</b>
<b>Number</b>	<b>Exhibit Description</b>				
101.LAB	Taxonomy Extension Labels				X
101.PRE	Taxonomy Extension Presentation				X
101.DEF	Taxonomy Extension Definition				X

\* **Furnished herewith**

In accordance with Rule 406T of Regulation S-T, the information in these exhibits is furnished and not deemed filed or a part of a registration statement or prospectus for purposes of Section 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of Section 18 of the Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as set forth by specific reference in such filing.