LogMeIn, Inc.
Form 10-Q
October 28, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________

Commission file number: 001-34391

LOGMEIN, INC.

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of** **incorporation or organization)**	**20-1515952** **(I.R.S. Employer** **Identification No.)**
320 Summer Street **Boston, Massachusetts** **(Address of principal executive offices)**	**02210** **(Zip Code)**

781-638-9050

(Registrant s telephone number, including area code)

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

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

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

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

Large accelerated filer   Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)   Smaller reporting company

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

As of October 24, 2016, there were 25,486,892 shares of the registrant s Common Stock, par value $0.01 per share, outstanding.

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Condensed Consolidated Balance Sheets

(In thousands, except per share data)

	December 31, 2015	September 30, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 123,143	$ 146,600
Marketable securities	85,284	70,609
Accounts receivable (net of allowance for doubtful accounts of $274 and $256 as of December 31, 2015 and September 30, 2016, respectively)	16,011	16,210
Prepaid expenses and other current assets	11,997	14,543
Total current assets	236,435	247,962
Property and equipment, net	21,711	25,226
Restricted cash	2,467	2,510
Intangibles, net	71,590	63,712
Goodwill	117,545	117,545
Other assets	5,753	4,736
Deferred tax assets	198	219
Total assets	$ 455,699	$ 461,910
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$ 10,327	$ 13,227
Accrued liabilities	31,674	35,937
Deferred revenue, current portion	134,297	159,365
Total current liabilities	176,298	208,529
Long-term debt	60,000	37,500
Deferred revenue, net of current portion	2,692	4,294
Deferred tax liabilities	5,812	6,967
Other long-term liabilities	3,086	8,138
Total liabilities	247,888	265,428
Commitments and contingencies (Note 10)		
Preferred stock, $0.01 par value 5,000 shares authorized, 0 shares outstanding as of December 31, 2015 and September 30, 2016		
Equity:		
	275	283

Common stock, $0.01 par value - 75,000 shares authorized; 27,540 and 28,322 shares issued as of December 31, 2015 and September 30, 2016, respectively; 25,130 and 25,496 outstanding as of December 31, 2015 and September 30, 2016, respectively				
Additional paid-in capital		276,793		300,162
Retained earnings		21,074		9,150
Accumulated other comprehensive loss		(5,216)		(5,199)
Treasury stock, at cost - 2,410 and 2,826 shares as of December 31, 2015 and September 30, 2016, respectively		(85,115)		(107,914)
Total equity		207,811		196,482
Total liabilities and equity	$	455,699	$	461,910

See notes to condensed consolidated financial statements.

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LogMeIn, Inc.

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2016	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2016
Revenue	$ 69,573	$ 85,103	$ 195,516	$ 248,103
Cost of revenue	8,678	11,485	25,195	34,121
Gross profit	60,895	73,618	170,321	213,982
Operating expenses				
Research and development	10,379	14,161	29,758	43,571
Sales and marketing	33,929	39,628	102,919	123,533
General and administrative	8,457	18,694	23,771	40,350
Legal settlements			3,600	
Amortization of acquired intangibles	286	1,363	844	4,103
Total operating expenses	53,051	73,846	160,892	211,557
Income (loss) from operations	7,844	(228)	9,429	2,425
Interest income	177	177	529	546
Interest expense	(109)	(335)	(261)	(1,094)
Other (expense) income	(540)	(180)	981	(676)
Income (loss) before income taxes	7,372	(566)	10,678	1,201
Provision for income taxes	(1,809)	(91)	(2,355)	(425)
Net income (loss)	$ 5,563	$ (657)	$ 8,323	$ 776
Net income (loss) per share:				
Basic	$ 0.22	$ (0.03)	$ 0.34	$ 0.03
Diluted	$ 0.22	$ (0.03)	$ 0.32	$ 0.03
Weighted average shares outstanding:				
Basic	24,955	25,401	24,733	25,230
Diluted	25,768	25,401	25,678	26,009

See notes to condensed consolidated financial statements.

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LogMeIn, Inc.

Condensed Consolidated Statements of Comprehensive Income (Loss)

(In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	**2016**	**2015**	**2016**
Net income (loss)	$ 5,563	$ (657)	$ 8,323	$ 776
Other comprehensive (loss) gain:				
Net unrealized gains (losses) on marketable securities, (net of tax provision of $5 and tax benefit of $33 for the three months ended September 30, 2015 and 2016; and net of tax provision of $62 and $27 for the nine months ended September 30, 2015 and 2016)	10	(58)	109	47
Net translation (losses) gains	(41)	172	(1,342)	(30)
Total other comprehensive (loss) gain	(31)	114	(1,233)	17
Comprehensive income (loss)	$ 5,532	$ (543)	$ 7,090	$ 793

See notes to condensed consolidated financial statements.

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Condensed Consolidated Statements of Cash Flows

(In thousands)

	Nine Months Ended September 30, 2015	2016
Cash flows from operating activities		
Net income	$ 8,323	$ 776
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation	19,235	27,327
Depreciation and amortization	9,232	16,076
Amortization of premium on investments	239	357
Change in fair value of contingent consideration liability		502
Amortization of debt issuance costs	132	218
Provision for bad debts	52	31
Income tax expense from the exercise of stock options	(216)	
Other, net	15	2
Changes in assets and liabilities:		
Accounts receivable	1,931	(79)
Prepaid expenses and other current assets	(2,873)	(1,552)
Other assets	(282)	1,188
Accounts payable	3,021	4,705
Accrued liabilities	(2,822)	4,176
Deferred revenue	34,850	25,420
Other long-term liabilities	1,177	4,943
Net cash provided by operating activities	72,014	84,090
Cash flows from investing activities		
Purchases of marketable securities	(57,170)	(35,609)
Proceeds from sale or disposal or maturity of marketable securities	72,042	50,000
Purchases of property and equipment	(10,922)	(12,629)
Intangible asset additions	(2,435)	(1,037)
Cash paid for acquisition		(61)
Decrease (increase) in restricted cash and deposits	1,488	(30)
Net cash provided by investing activities	3,003	634
Cash flows from financing activities		
Repayments of borrowings under credit facility		(22,500)
Proceeds from issuance of common stock upon option exercises	15,251	9,443
Income tax benefit from the exercise of stock options	216	
Payments of withholding taxes in connection with restricted stock unit vesting	(11,148)	(13,432)

Payment of debt issuance costs		(977)		(349)
Payment of contingent consideration		(226)		(29)
Dividend paid on common stock				(12,700)
Purchase of treasury stock		(14,732)		(22,799)
Net cash used in financing activities		(11,616)		(62,366)
Effect of exchange rate changes on cash and cash equivalents		(3,949)		1,099
Net increase in cash and cash equivalents		59,452		23,457
Cash and cash equivalents, beginning of period		100,960		123,143
Cash and cash equivalents, end of period	$	160,412	$	146,600
Supplemental disclosure of cash flow information				
Cash paid for interest	$	2	$	763
Cash paid (refunds received) for income taxes	$	1,468	$	(177)
Noncash investing and financing activities				
Acquisition of property and equipment through capital lease	$		$	136
Purchases of property and equipment included in accounts payable and accrued liabilities	$	2,269	$	890
Fair value of contingent consideration in connection with acquisition, included in accrued liabilities	$	27	$	2,500

See notes to condensed consolidated financial statements.

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LogMeIn, Inc.

Notes to Condensed Consolidated Financial Statements

1. Nature of the Business

LogMeIn, Inc. (the Company) provides a portfolio of cloud-based service offerings which make it possible for people and businesses to simply and securely connect to their workplace, colleagues and customers. The Company s product line includes AppGuru , BoldChat®, Cubby , join.me®, LastPass®, LogMeIn Pro®, LogMeIn® Central , LogMeIn Rescue®, LogMeIn® Rescue+Mobile , LogMeIn Backup®, LogMeIn for iOS, LogMeIn Hamachi®, Meldium , Xively and RemotelyAnywhere®. The Company is headquartered in Boston, Massachusetts with wholly-owned subsidiaries located in Australia, Bermuda, Brazil, Hungary, India, Ireland, Japan, the Netherlands and the United Kingdom.

On July 26, 2016, the Company entered into an agreement and plan of merger (the Merger Agreement) with Citrix Systems, Inc., (Citrix), and GetGo, Inc., (GetGo), a wholly-owned subsidiary of Citrix, pursuant to which the Company will combine with Citrix s GoTo family of products known as the GoTo Business in a Reverse Morris Trust transaction, which is referred to herein as the Merger. Following the Merger, Citrix s existing stockholders will own approximately 50.1% of the Company s outstanding shares on a fully diluted basis, while the Company s existing stockholders will own approximately 49.9% on a fully diluted basis. Based upon the reported closing price of the Company s common stock on the NASDAQ Global Select Market of $65.31 per share on July 25, 2016, the last trading day before the signing of the Merger Agreement, the estimated total value of the shares to be issued by the Company to Citrix stockholders in the Merger would have been approximately $1.8 billion. Based upon the reported closing price of the Company s common stock on the NASDAQ Global Select Market of $90.52 per share on September 6, 2016, the estimated total value of the shares to be issued by the Company to Citrix stockholders pursuant to the Merger would have been approximately $2.5 billion. The actual total value of the consideration to be paid by the Company in connection with the Merger will depend on the market price of shares of the Company common stock at the time of the closing of the Merger. The transaction, which has been unanimously approved by the Company s Board of Directors and the Board of Directors of Citrix, is expected to be generally tax-free to Citrix and its stockholders for U.S. federal income tax purposes.

The consummation of the Merger and its related transactions remain subject to the Company s stockholders approving the issuance of shares in connection with the Merger, the receipt of certain regulatory approvals and other customary closing conditions, including receipt of opinions of counsel with respect to the tax-free nature of the proposed transaction. On September 26, 2016, the Company announced the early termination of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act for the proposed Merger. The transaction is expected to close in the first quarter of 2017. If the Merger Agreement is terminated under certain circumstances, the Company may be required to pay Citrix a termination fee of $62 million or may under other circumstances be required to reimburse Citrix up to $10 million for certain expenses in connection with the Merger.

The Company expects to incur significant one-time costs in connection with the Merger in 2016 and into 2017, including approximately $45 million to $50 million of transaction-related fees and expenses, including legal, accounting and other professional fees and transition and integration-related expenses. During the nine months ended September 30, 2016, the Company incurred $9.8 million of transaction-related and integration-related fees and expenses and expects to incur an additional $9 million of these expenses during the remainder of 2016.

2. Summary of Significant Accounting Policies

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

Unaudited Interim Condensed Consolidated Financial Statements The accompanying condensed consolidated financial statements and the related interim information contained within the notes to the condensed consolidated financial statements are unaudited and have been prepared in accordance with GAAP and applicable rules and regulations of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. The accompanying unaudited condensed consolidated financial statements should be read along with the Company s audited financial statements included in the Company s Annual Report on Form 10-K, filed with the Securities and Exchange Commission on February 19, 2016. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited financial statements and in the opinion of management, reflect all adjustments, consisting of normal and recurring adjustments, necessary for the fair presentation of the Company s financial position, results of operations and cash flows for the interim periods presented. The results for the interim periods presented are not necessarily indicative of future results. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

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

Marketable Securities The Company s marketable securities are classified as available-for-sale and are carried at fair value with the unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive loss in equity. Realized gains and losses and declines in value judged to be other than temporary are included as a component of earnings based on the specific identification method. Fair value is determined based on quoted market prices. At December 31, 2015 and September 30, 2016, marketable securities consisted of U.S. government agency securities and corporate bonds that have remaining maturities within two years and have an aggregate amortized cost of $85.3 million and $70.6 million, respectively. The securities have an aggregate fair value of $85.3 million and $70.6 million, including $10,000 and $74,000 of unrealized gains and $53,000 and $43,000 of unrealized losses, at December 31, 2015 and September 30, 2016, respectively.

Revenue Recognition The Company derives revenue primarily from subscription fees related to its premium subscription software services and to a lesser extent, the delivery of professional services, primarily related to its Internet of Things business. Revenues are reported net of applicable sales and use tax, value-added tax and other transaction taxes imposed on the related transaction.

Revenue from the Company s premium services is recognized on a daily basis over the subscription term as the services are delivered, provided that there is persuasive evidence of an arrangement, the fee is fixed or determinable and collectability is deemed reasonably assured. Subscription periods range from monthly to ten years, but are generally one year in duration. The Company s software cannot be run on another entity s hardware and customers do not have the right to take possession of the software and use it on their own or another entity s hardware.

The Company s multi-element arrangements typically include subscription and professional services, which may include development services. The Company evaluates each element within the arrangement to determine if they can be accounted for as separate units of accounting. If the delivered item or items have value to the customer on a standalone basis, either because they are sold separately by any vendor or the customer could resell the delivered item or items on a standalone basis, the Company has determined that the deliverables within these arrangements qualify for treatment as separate units of accounting. Accordingly, the Company recognizes revenue for each delivered item or items as a separate earnings process commencing when all of the significant performance obligations have been performed and when all of the revenue recognition criteria have been met. Professional services revenue recognized as a separate earnings process under multi-element arrangements has been immaterial to date.

In cases where the Company has determined that the delivered items within its multi-element arrangements do not have value to the customer on a stand-alone basis, the arrangement is accounted for as a single unit of accounting and the related consideration is recognized ratably over the estimated customer life, commencing when all of the significant performance obligations have been delivered and when all of the revenue recognition criteria have been met. Revenue from multi-element arrangements accounted for as a single unit of accounting which do not have value to the customer has been immaterial to date.

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

For the three and nine months ended September 30, 2015 and 2016, no customers accounted for more than 10% of revenue. As of December 31, 2015 and September 30, 2016, no customers accounted for more than 10% of accounts receivable.

Goodwill Goodwill is the excess of the acquisition price over the fair value of the tangible and identifiable intangible net assets acquired. The Company does not amortize goodwill, but performs an impairment test of goodwill annually or whenever events and circumstances indicate that the carrying amount of goodwill may exceed its fair value. The Company operates as a single operating segment with one reporting unit and consequently evaluates goodwill for impairment based on an evaluation of the fair value of the Company as a whole. As of December 31, 2015, the fair value of the Company as a whole significantly exceeded the carrying amount of the Company. Through September 30, 2016, no impairments have occurred.

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

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, including intangible assets, may not be recoverable. When such events occur, the Company compares the carrying amounts of the assets to their undiscounted expected future cash flows. If this comparison indicates that there is impairment, the amount of the impairment is calculated as the difference between the carrying value and fair value. Through September 30, 2016, the Company recorded no material impairments.

Foreign Currency Translation The functional currency of operations outside the United States of America is deemed to be the currency of the local country, unless otherwise determined that the United States dollar would serve as a more appropriate functional currency given the economic operations of the entity. Accordingly, the assets and liabilities of the Company s foreign subsidiaries are translated into United States dollars using the period-end exchange rate and income and expense items are translated using the average exchange rate during the period. Cumulative translation adjustments are reflected as a separate component of equity. Foreign currency transaction gains and losses are charged to operations. The Company had foreign currency losses of $0.5 million and gains of $1.0 million for the three and nine months ended September 30, 2015, respectively, and foreign currency losses of $0.2 million and $0.7 million for the three and nine months ended September 30, 2016, respectively, included in other (expense) income in the condensed consolidated statements of operations.

Stock-Based Compensation The Company values all stock-based compensation, including grants of stock options and restricted stock units, at fair value on the date of grant and recognizes the expense over the requisite service period, which is generally the vesting period of the award, for those awards expected to vest, on a straight-line basis. The Company uses the with-or-without method to determine when it will realize excess tax benefits from stock-based compensation. Under this method, the Company will realize these excess tax benefits only after it realizes the tax benefits of net operating losses from operations.

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

The Company evaluates its uncertain tax positions based on a determination of whether and how much of a tax benefit taken by the Company in its tax filings is more likely than not to be realized. Potential interest and penalties associated with any uncertain tax positions are recorded as a component of income tax expense. As of December 31, 2015 and September 30, 2016, the Company has provided a liability for $0.9 million and $1.3 million, respectively, for uncertain tax positions. These uncertain tax positions would impact the Company s effective tax rate if recognized.

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

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Revenues:				
United States	$ 48,721	$ 60,713	$ 137,194	$ 177,440
United Kingdom	5,683	6,530	15,692	19,239
International all other	15,169	17,860	42,630	51,424
Total revenue	$ 69,573	$ 85,103	$ 195,516	$ 248,103

The Company s revenue by service cloud (product grouping) is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Revenues:				
Collaboration cloud	$ 22,930	$ 30,240	$ 63,148	$ 85,837
Identity and Access Management cloud	23,718	30,524	65,718	88,268
Service and Support cloud	22,363	23,871	64,783	72,233
Other	562	468	1,867	1,765
Total revenue	$ 69,573	$ 85,103	$ 195,516	$ 248,103

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

In the ordinary course of business, the Company enters into agreements with certain customers that contractually obligate the Company to provide indemnifications of varying scope and terms with respect to certain matters including, but not limited to, losses arising out of the breach of such agreements or claims alleging that the Company s products infringe third-party patents, copyrights, or trademarks. The term of these indemnification obligations is generally perpetual. The maximum potential amount of future payments the Company could be required to make under these indemnification obligations is, in many cases, unlimited. Through September 30, 2016, the Company has not experienced any losses related to these indemnification obligations.

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Net Income (Loss) Per Share Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per share is computed by dividing net income (loss) by the sum of the weighted average number of common shares outstanding during the period and the weighted average number of potential common shares outstanding from the assumed exercise of stock options and the vesting of restricted stock units. For the three months ended September 30, 2016, the Company incurred a net loss and therefore, the effect of the Company s outstanding common stock equivalents were not included in the calculation of diluted loss per share as they were anti-dilutive. Accordingly, basic and dilutive net loss per share for the period were identical.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Options to purchase common shares		418		
Restricted stock units	238	1,473	238	106
Total options and restricted stock units	238	1,891	238	106

For the three months ended September 30, 2016, the Company recorded a net loss of $0.7 million and all outstanding options to purchase common shares and restricted stock units have been excluded from the computation of diluted net loss per share as they had an anti-dilutive impact.

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

	Three months ended September 30,		Nine months ended September 30,	
	2015	2016	2015	2016
Basic:				
Net income (loss)	$ 5,563	$ (657)	$ 8,323	$ 776
Weighted average common shares outstanding, basic	24,955	25,401	24,733	25,230
Net income (loss) per share, basic	$ 0.22	$ (0.03)	$ 0.34	$ 0.03
Diluted:				
Net income (loss)	$ 5,563	$ (657)	$ 8,323	$ 776
Weighted average common shares outstanding	24,955	25,401	24,733	25,230
Add: Common stock equivalents	813		945	779
	25,768	25,401	25,678	26,009

Weighted average common shares outstanding, diluted								
Net income (loss) per share, diluted	$	0.22	$	(0.03)	$	0.32	$	0.03

Recently Issued Accounting Pronouncements On May 28, 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), its final standard on revenue from contracts with customers. ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the revenue model to contracts within its scope, an entity identifies the contract(s) with a customer, identifies the performance obligations in the contract, determines the transaction price, allocates the transaction price to the performance obligations in the contract and recognizes revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 applies to all contracts with customers that are within the scope of other topics in the FASB Accounting Standards Codification. Certain of ASU 2014-09 s provisions also apply to transfers of nonfinancial assets, including in-substance nonfinancial assets that are not an output of an entity s ordinary activities (i.e., property plant and equipment, real estate or intangible assets). Existing accounting guidance applicable to these transfers has been amended or superseded. ASU 2014-09 also requires significantly expanded disclosures about revenue recognition. ASU 2014-09 is effective for the Company on January 1, 2018, with early adoption permitted, but not earlier than January 1, 2017. The Company is currently assessing the potential impact of the adoption of ASU 2014-09 on its consolidated financial statements.

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On February 25, 2016, the FASB issued ASU 2016-02, *Leases* (ASU 2016-02) *,* which will require lessees to recognize most leases on their balance sheet as a right-of-use asset and a lease liability. Leases will be classified as either operating or finance, and classification will be based on criteria similar to current lease accounting, but without explicit bright lines. The guidance is effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years, and early adoption is permitted. The Company is currently assessing the impact of the adoption of ASU 2016-02 on its consolidated financial statements.

On March 30, 2016, the FASB issued ASU 2016-09, *Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* (ASU 2016-09), which includes multiple provisions intended to simplify various aspects of the accounting for share-based payments, and is expected to impact net income, EPS, and the statement of cash flows. The guidance is effective for annual reporting periods beginning after December 15, 2016 and interim periods within those fiscal years, and early adoption is permitted. The Company is currently assessing the impact of the adoption of ASU 2016-09 on its consolidated financial statements.

On June 16, 2016, the FASB issued ASU 2016-13, *Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (ASU 2016-13). The purpose of ASU 2016-13 is to require a financial asset measured on the amortized cost basis to be presented at the net amount expected to be collected. Credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. The guidance is effective for annual reporting periods beginning after December 15, 2019 and interim periods within those fiscal years. Early adoption is permitted for annual periods beginning after December 15, 2018, and interim periods therein. This guidance is not expected to have a material impact on the Company s consolidated financial statements.

On August 26, 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* (ASU 2016-15). The purpose of ASU 2016-15 is to reduce the diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The guidance is effective for annual reporting periods beginning after December 15, 2017 and interim periods within those fiscal years, and early adoption is permitted. The Company adopted this guidance in the third quarter of 2016 and there was no material impact on its consolidated financial statements.

On October 24, 2016, the FASB issued ASU 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory (ASU 2016-16).* The purpose of ASU 2016-16 is to simplify the income tax accounting of an intra-entity transfer of an asset other than inventory and to record its effect when the transfer occurs. The guidance is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods and early adoption is permitted. The Company is currently assessing the potential impact of the adoption of ASU 2016-16 on its consolidated financial statements.

3. Fair Value of Financial Instruments

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

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

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

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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

	Fair Value Measurements at December 31, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash equivalents money market funds	$ 10,138	$	$	$ 10,138
Cash equivalents bank deposits		1		1
Short-term marketable securities:				
U.S. government agency securities	50,237	17,994		68,231
Corporate bond securities		17,053		17,053
Contingent consideration liability			2,028	2,028

	Fair Value Measurements at September 30, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash equivalents money market funds	$ 25,368	$	$	$ 25,368
Short-term marketable securities:				
U.S. government agency securities	43,574	9,508		53,082
Corporate bond securities		17,527		17,527
Contingent consideration liability			2,500	2,500

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

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The Company s Level 3 liability at September 30, 2016 consists of contingent consideration payable in connection with the October 15, 2015 acquisition of Marvasol, Inc. (d/b/a LastPass), as described in Note 4 below. Up to $2.5 million of the LastPass contingent consideration is based on the achievement of certain bookings goals, the fair value of which was estimated at $2.0 million as of December 31, 2015. The fair value of contingent consideration was estimated by applying a probability based model, which utilizes inputs that are unobservable in the market. Changes in the fair value of the contingent consideration liability was reflected in acquisition-related costs in general and administrative expense. The fair value of the LastPass contingent consideration liability of $2.5 million was paid in October 2016. A reconciliation of the beginning and ending Level 3 liability is as follows:

	Nine Months Ended September 30, 2016	
Balance beginning of period	$	2,028
Payments		(30)
Change in fair value of contingent consideration liability		502
Balance end of period	$	2,500

4. Acquisitions

In the nine months ended September 30, 2015 and 2016, acquisition-related costs were $3.8 million and $16.9 million, respectively, including $3.4 million and $6.7 million, respectively, of contingent retention-based bonus expense related to the Company s 2014 and 2015 acquisitions, which are typically earned over the first two years following the acquisition. The Company paid $6.0 million during the nine months ended September 30, 2016 for contingent retention-based bonuses related to the Company s 2014 and 2015 acquisitions. Included in the nine months ended September 30, 2016 is $9.8 million of acquisition-related costs associated with the proposed Merger.

LastPass

On October 15, 2015, the Company acquired all of the outstanding equity interests in LastPass, a Fairfax, Virginia-based provider of an identity and password management service, for $107.6 million, net of cash acquired, plus contingent payments totaling up to $15.0 million which are expected to be paid over a two year period following the date of acquisition. The operating results of LastPass, which are included in the condensed consolidated financial statements beginning on the acquisition date, are comprised of $5.0 million and $13.2 million of revenue and $6.9 million and $18.0 million of expenses for the three and nine months ended September 30, 2016, including amortization of acquired intangible assets of $1.5 million and $4.7 million, contingent retention-based bonuses of $1.7 million and $5.2 million and a contingent consideration fair value adjustment of $0.5 million for the nine months ended September 30, 2016, respectively.

The following table summarizes the fair value (in thousands) of the assets acquired and liabilities assumed at the date of acquisition:

Cash	$	2,518

Accounts receivable	639
Property and equipment	40
Deferred tax asset	3,050
Current and other assets	134
Intangible assets:	
Completed technology	29,400
Customer relationships	23,900
Trade name and trademark	3,000
Deferred revenue	(6,600)
Accrued expenses	(66)
Deferred tax liability	(23,478)
Goodwill	79,617
Total purchase price	112,154
Liability for contingent consideration	(2,000)
Total cash paid	$ 110,154

The LastPass stock purchase agreement obligates the Company to make additional contingent and retention-based bonus payments totaling up to $12.5 million to employees and former LastPass stockholders now employed by the Company on the first and second anniversaries of the acquisition date, contingent upon their continued employment and, for the first anniversary payment only, the achievement of certain bookings goals. The Company has concluded that the contingent payment arrangement is a compensation arrangement and is accruing the maximum payout ratably over the performance period, as it believes it is probable that the criteria will be met. The stock purchase agreement also includes

non-retention based payments of $2.5 million to LastPass stockholders which are contingent on the achievement of certain bookings goals, which the Company has concluded is contingent consideration and is being accounted for as part of the purchase price. This contingent consideration liability was recorded at its fair value of $2.0 million at the acquisition date. The Company assessed the probability of the bookings goals being met and at what level each reporting period. As of September 30, 2016, the contingent consideration liability was $2.5 million and was paid in October 2016.

The goodwill recorded in connection with this transaction is primarily related to the expected synergies to be achieved related to the Company s ability to leverage its IT management offerings, customer base, sales force and IT management business plan with LastPass product, technical expertise and customer base. All goodwill and intangible assets acquired are not deductible for income tax purposes.

The Company recorded a long-term deferred tax asset of $3.1 million primarily related to net operating losses that were acquired as a part of the acquisition. The Company recorded a long-term deferred tax liability of $23.5 million primarily related to the amortization of intangible assets which cannot be deducted for tax purposes.

The unaudited financial information in the table below summarizes the combined results of operations of the Company and LastPass, on a pro forma basis, as though the companies had been combined. The pro forma information for the period presented includes the effects of business combination accounting resulting from the acquisition as though the acquisition had been consummated as of the beginning of 2014, including amortization charges from acquired intangible assets; interest expense on borrowings and lower interest income in connection with the Company funding the acquisition with existing cash and investments and borrowings under its credit facility; the exclusion of acquisition-related costs of the Company and LastPass; the inclusion of expense related to contingent and retention-based bonuses assuming full achievement of the financial metric and retention requirements ($7.0 million in 2014 and $5.5 million in 2015), offset by the exclusion of LastPass historical bonuses paid to LastPass non-stockholder employees in 2015 in connection with the acquisition close of $6.1 million; and the related tax effects. The pro forma financial information is presented for comparative purposes only and is not necessarily indicative of the results of operations that actually would have been achieved if the acquisition had taken place at the beginning of 2014.

Unaudited Pro Forma Financial Information

	Three Months Ended September 30, 2015		**Nine Months Ended September 30, 2015**	
	Pro Forma	**As Reported**	**Pro Forma**	**As Reported**
	(in thousands, except per share amounts)		**(in thousands, except per share amounts)**	
Revenue	$ 73,212	$ 69,573	$ 205,257	$ 195,516
Net income	$ 4,954	$ 5,563	$ 5,853	$ 8,323
Earnings per share Basic	$ 0.20	$ 0.22	$ 0.24	$ 0.34
Earnings per share Diluted	$ 0.19	$ 0.22	$ 0.23	$ 0.32

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5. Goodwill and Intangible Assets

There was no change in the carrying amount of goodwill for the nine months ended September 30, 2016.

Intangible assets consist of the following (in thousands):

		December 31, 2015			September 30, 2016		
	Estimated Useful Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Identifiable intangible assets:							
Trade names and trademarks	1-11 years	$ 3,806	$ 824	$ 2,982	$ 3,806	$ 922	$ 2,884
Customer relationships	5-8 years	29,129	4,089	25,040	29,129	7,925	21,204
Customer backlog	4 months	120	120		120	120	
Domain names	5 years	915	665	250	916	769	147
Software	4 years	299	299		299	299	
Completed technology	3-9 years	46,503	6,893	39,610	46,503	10,324	36,179
Technology and know-how	3 years	3,176	3,176		3,176	3,176	
Documented know-how	4 years	280	127	153	280	180	100
Non-Compete agreements	5 years	162	114	48	162	150	12
Internally developed software	3 years	6,754	3,247	3,507	7,791	4,605	3,186
		$ 91,144	$ 19,554	$ 71,590	$ 92,182	$ 28,470	$ 63,712

The Company capitalized $0.5 million and $0.3 million during the three months ended September 30, 2015 and 2016, respectively, and $2.2 million and $1.0 million during the nine months ended September 30, 2015 and 2016, respectively, of costs related to internally developed computer software to be sold as a service incurred during the application development stage and is amortizing these costs over the expected lives of the related services.

The Company is amortizing its intangible assets over the estimated useful lives noted above based upon the pattern in which their economic benefit will be realized, or if this pattern cannot be reliably determined, using the straight-line method over their estimated useful lives. Amortization expense for intangible assets was $1.3 million and $2.9 million for the three months ended September 30, 2015 and 2016, respectively, and $3.8 million and $8.9 million for the nine months ended September 30, 2015 and 2016, respectively. Amortization relating to software, completed technology, technology and know-how, documented know-how and internally developed software is recorded within cost of revenues and the amortization of trade name and trademark, customer relationships, customer backlog, domain names and non-compete agreements is recorded within operating expenses.

Future estimated amortization expense for intangible assets at September 30, 2016 is as follows (in thousands):

Amortization Expense (Years Ending December 31)	Amount
2016 (three months ending December 31)	$ 2,917
2017	11,696

2018	11,249
2019	8,511
2020	7,616
Thereafter	21,723
Total	$ 63,712

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6. Accrued Liabilities

Accrued liabilities consisted of the following (in thousands):

	December 31, 2015	September 30, 2016
Marketing programs	$ 4,323	$ 6,748
Payroll and payroll-related	11,459	11,070
Professional fees	1,782	1,593
Acquisition-related	6,942	8,180
Other accrued liabilities	7,168	8,346
Total accrued liabilities	$ 31,674	$ 35,937

Acquisition-related costs include transaction, transition and integration-related fees and expenses and contingent bonus costs.

7. Income Taxes

For the three months ended September 30, 2015 and 2016, the Company recorded a provision of $1.8 million, on pre-tax earnings of $7.4 million and a provision of $0.1 million, on a pre-tax loss of $0.6 million, respectively. For the nine months ended September 30, 2015 and 2016, the Company recorded a provision of $2.4 million, on pre-tax earnings of $10.7 million, and a provision of $0.4 million, on pre-tax earnings of $1.2 million, respectively. The effective income tax rate for the nine months ended September 30, 2015 is lower than the U.S. federal statutory rate of 35% primarily due to profits earned in certain foreign jurisdictions, primarily the Company s Irish subsidiaries, which are subject to significantly lower tax rates than the U.S. federal statutory rate. The effective income tax rate for the nine months ended September 30, 2016 is higher than the U.S. federal statutory rate of 35% due to the expected non-deductibility of certain transaction costs related to the proposed Merger, partially offset by profits earned in certain foreign jurisdictions, primarily our Irish subsidiaries.

As of December 31, 2015 and September 30, 2016, the Company maintained a full valuation allowance related to the deferred tax assets of its Hungarian subsidiary. This entity has historical losses and the Company concluded it was not more likely than not that these deferred tax assets are realizable.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The Company s income tax returns from 2010 are open to examination by federal, state, and/or foreign tax authorities. In the normal course of business, the Company and its subsidiaries are examined by various taxing authorities. The Company regularly assesses the likelihood of additional assessments by tax authorities and provides for these matters as appropriate. Audits by tax authorities typically involve examination of the deductibility of certain permanent items, limitations on net operating losses and tax credits.

In connection with a tax audit of a foreign subsidiary, the Company received an assessment in the second quarter of 2016 challenging a tax position taken by the entity. The Company believes that it is more likely than not that its position will be upheld. If the Company s position is not upheld, its potential liability could be up to $2 million.

Although the Company believes its tax estimates are appropriate, the final determination of tax audits could result in material changes in its estimates. The Company has recorded a liability related to uncertain tax positions of $0.9 million and $1.3 million as of December 31, 2015 and September 30, 2016, respectively. The Company s policy is to record estimated interest and penalties related to the underpayment of income taxes or unrecognized tax benefits as a component of its income tax provision. The Company recognized $0 and $21,000 of interest expense for the nine months ended September 30, 2015 and 2016, respectively.

8. Common Stock and Equity

The Company s Board of Directors approved a $75 million share repurchase program on October 20, 2014. Share repurchases are made from time-to-time in the open market, in privately negotiated transactions or otherwise, in accordance with applicable securities laws and regulations. The timing and amount of any share repurchases are determined by the Company s management based on its evaluation of market conditions, the trading price of the stock, regulatory requirements and other factors. The share repurchase program may be suspended, modified or discontinued at any time at the Company s discretion without prior notice.

For the three months ended September 30, 2016, the Company repurchased 45,562 shares of its common stock at an average price of $75.98 per share for a total cost of $3.5 million. There were no shares repurchased during the three months ended September 30, 2015. For the nine months ended September 30, 2015 and 2016, the Company repurchased 249,400 and 416,474 shares of its common stock at an average price of $59.07 and $54.74 per share for a total cost of $14.7 million and $22.8 million, respectively. At September 30, 2016, $33.5 million remained available under the Company s share repurchase program.

On July 26, 2016, the Company announced that its Board of Directors declared a special cash dividend of $0.50 per share of common stock, payable to the Company s stockholders of record as of August 8, 2016. The dividend was paid on August 26, 2016 and totaled $12.7 million. The Company intends to declare and pay two additional special cash dividends of $0.50 per share of common stock, as

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permitted by the Merger Agreement. On October 27, 2016, the Company announced that the second special cash dividend of $0.50 per share of common stock would be payable on November 22, 2016 to stockholders of record on November 7, 2016. The third dividend is expected to be declared and paid shortly before the consummation of the Merger, subject to the Merger Agreement being in effect. The Merger Agreement also permits the Company to declare additional dividends as follows: (1) in the event the closing of the Merger does not occur on or before March 31, 2017, the Company may pay an additional dividend of $0.50 per share with respect to the completed first quarter of calendar year 2017; (2) in the event the closing of the Merger does not occur on or before June 30, 2017, the Company may pay an additional dividend of $0.50 per share with respect to the completed second quarter of calendar year 2017; and (3) in the event the closing of the Merger does not occur on or before September 30, 2017, the Company may pay an additional dividend of $0.50 per share with respect to the completed third quarter of calendar year 2017.

9. Stock Incentive Plan

The Company s 2009 Stock Incentive Plan (2009 Plan) is administered by the Board of Directors and Compensation Committee, which have the authority to designate participants and determine the number and type of awards to be granted and any other terms or conditions of the awards. The Company awards restricted stock units as the principal equity incentive award. Restricted stock units with time-based vesting conditions generally vest over a three-year period while restricted stock units with market-based vesting conditions generally vest over two or three-year periods. Until 2012, the Company generally granted stock options as the principal equity incentive award. Options generally vest over a four-year period and expire ten years from the date of grant. Certain stock-based awards provide for accelerated vesting if the Company experiences a change in control. As of September 30, 2016, there were 3.4 million shares available for grant under the 2009 Plan.

The following table summarizes stock option activity (shares and intrinsic value in thousands):

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding, January 1, 2016	768	$ 30.74	5.4	$ 27,942
Granted				
Exercised	(347)	27.19		$ 13,526
Forfeited	(3)	21.58		
Outstanding, September 30, 2016	418	$ 33.77	5.1	$ 23,594
Exercisable at December 31, 2015	598	$ 30.54	5.0	$ 21,881
Exercisable at September 30, 2016	323	$ 38.39	5.4	$ 16,821

The aggregate intrinsic value was calculated based on the positive differences between the fair value of the Company s common stock of $67.10 per share on December 31, 2015 and $90.39 per share on September 30, 2016, or at time of exercise, and the exercise price of the options.

During the three and nine months ended September 30, 2016, the Company granted 88,270 and 732,688 restricted stock units, respectively, of which 88,270 and 678,188 have time-based vesting conditions and 0 and 54,500 have market-based vesting conditions, respectively. Restricted stock units with time-based vesting conditions are valued on the grant date using the grant date closing price of the underlying shares. The Company recognizes the expense on a straight-line basis over the requisite service period of the restricted stock unit, which is generally three years. An additional 27,000 and 36,200 market-based restricted stock units were earned and issued during the three and nine months ended September 30, 2016, respectively.

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Since 2013, the Company has granted to certain key executives restricted stock unit awards with market-based vesting conditions, which are tied to the individual executive s continued employment with the Company throughout the applicable performance period and the level of the Company s achievement of a pre-established relative total shareholder return, or TSR, goal, as measured over an applicable performance period ranging from two to three years as compared to the TSR realized for that same period by the Russell 2000 Index (the TSR Units). In February and March 2016, the Company granted TSR Units with a target number of underlying shares of 37,500 and 17,000, respectively, but the actual number of shares that may be earned under these TSR Units can range from 0% to 200% of the target number of shares awarded, or up to 75,000 and 34,000 shares, respectively, based on the Company s level of achievement of its relative TSR goal for the applicable performance period. Compensation cost for TSR Units is recognized on a straight-line basis over the requisite service period and is recognized regardless of the actual number of awards that are earned based on the market condition.

The assumptions used in the Monte Carlo simulation model for the 2016 TSR Unit grants include (but are not limited to) the following:

	February 2016 Grant	May 2016 Grant
Risk-free interest rate	0.89%	1.02%
Volatility	40%	37%

The following table summarizes restricted stock unit activity, including performance-based TSR Units (shares in thousands):

	Number of shares Underlying Restricted Stock Units	Weighted Average Grant Date Fair Value
Unvested as of January 1, 2016	1,438	$ 54.37
Restricted stock units granted	769	62.06
Restricted stock units vested	(644)	46.80
Restricted stock units forfeited	(90)	56.04
Unvested as of September 30, 2016	1,473	$ 61.31

Included in both restricted stock units granted and vested in the table above are 36,200 TSR Units earned above the target number of underlying shares initially granted.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Cost of revenue	$ 314	$ 536	$ 1,132	$ 1,774

Research and development	1,193	1,476	4,051	4,702
Sales and marketing	3,117	4,398	7,972	12,876
General and administrative	2,044	2,589	6,080	7,975
	$ 6,668	$ 8,999	$ 19,235	$ 27,327

As of September 30, 2016, there was $65.1 million of total unrecognized share-based compensation cost, net of estimated forfeitures, related to unvested stock awards which are expected to be recognized over a weighted average period of 2.1 years. The total unrecognized share-based compensation cost will be adjusted for future changes in estimated forfeitures.

10. Commitments and Contingencies

Operating Leases The Company has operating lease agreements for offices in the United States, Hungary, Australia, the United Kingdom, Ireland and India that expire at various dates through 2028.

In December 2015, the Company amended its current lease for its Budapest, Hungary office space to provide for an expansion of leased space and to extend the term of the lease. The term of the amended lease began in June 2016 and extends through June 2021. The aggregate amount of minimum lease payments to be made over the term of the lease is approximately $8.4 million (EUR 7.5 million). The lease agreement required a bank guarantee of $0.6 million (EUR 0.5 million). The bank guarantee is classified as restricted cash.

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In December 2014, the Company entered into a lease for new office space in Boston, Massachusetts which began in December 2015 and extends through June 2028. The aggregate amount of minimum lease payments to be made over the term of the lease is approximately $47.0 million. Pursuant to the terms of the lease, the landlord was responsible for making certain improvements to the leased space up to an agreed upon cost to the landlord. Any excess costs for these improvements were billed by the landlord to the Company as additional rent. These excess costs total $3.4 million, all of which were paid as of September 30, 2016. The lease required a security deposit of $3.3 million in the form of an irrevocable, unsecured standby letter of credit. The lease includes an option to extend the original term of the lease for two successive five year periods.

Rent expense under all leases was $1.8 million and $3.0 million for the three months ended September 30, 2015 and 2016, respectively, and $5.7 million and $8.9 million for the nine months ended September 30, 2015 and 2016, respectively. The Company records rent expense on a straight-line basis for leases with scheduled escalation clauses or free rent periods.

The Company also enters into hosting services agreements with third-party data centers and internet service providers that are subject to annual renewal. The aggregate hosting fees incurred under these arrangements totaled $1.8 million and $2.6 million for the three months ended September 30, 2015 and 2016, respectively and $4.8 million and $7.2 million for the nine months ended September 30, 2015 and 2016, respectively.

Future minimum lease payments under non-cancelable operating and capital leases including commitments associated with the Company s hosting services arrangements are approximately as follows at September 30, 2016 (in thousands):

Years Ending December 31	
2016 (three months ending December 31)	$ 4,733
2017	15,271
2018	12,202
2019	12,120
2020	11,820
Thereafter	46,470
Total minimum lease payments	$ 102,616

Litigation The Company routinely assesses its current litigation and/or threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss in situations where the Company assesses the likelihood of loss as probable.

On September 2, 2016, Meetrix IP, LLC (Meetrix) filed a complaint against the Company in the U.S. District Court for the Western District of Texas (Case No. 1:16-cv-1034). The complaint, which was served upon the Company on September 22, 2016, alleges that the Company s join.me service infringes upon U.S. Patent Nos. 9,253,332, 9,094,525 and 8,339,997, each of which are allegedly owned by Meetrix and which Meetrix asserts relate to audio-video conferencing collaboration. The complaint seeks monetary damages in an unspecified amount, attorneys fees and costs, and additional relief as is deemed appropriate by the court. The Company believes it has meritorious defenses to these claims and intends to defend the lawsuit vigorously. Given the inherent unpredictability of litigation and the fact that this litigation is still in its early stages, the Company is unable to predict the outcome of this litigation or reasonably estimate a possible loss or range of loss associated with this litigation at this time.

On April 24, 2015, the Company entered into a Settlement Agreement with Sensory Technologies, LLC, or Sensory, whereby Sensory agreed to assign its JOIN® trademark to the Company and the parties agreed to mutually release each other from any and all claims related to the complaint filed by Sensory against the Company in the U.S. District Court for the Southern District of Indiana on August 26, 2014. In the second quarter of 2015, the Company paid Sensory a one-time fee of $8.3 million, $4.7 million of which was reimbursed by the Company s insurance provider, in connection with the Settlement Agreement. The Company believed that the JOIN® trademark had de minimis value and therefore expensed $3.6 million in the first quarter of 2015 as legal settlement expense, which was paid in the second quarter of 2015.

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

11. Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of foreign currency translation adjustments and changes in unrealized losses and gains (net of tax) on marketable securities. For the purposes of comprehensive income disclosures, the Company does not record tax provisions or benefits for the net changes in the foreign currency translation adjustment, as the Company intends to reinvest permanently undistributed earnings of its foreign subsidiaries. Accumulated other comprehensive loss is reported as a component of stockholders equity and was comprised of cumulative translation adjustment losses of $5.2 million as of December 31, 2015 and September 30, 2016, and unrealized losses (net of tax) on marketable securities of $27,000 and unrealized gains (net of tax) of $19,000, respectively. There were no material reclassifications to earnings in the nine months ended September 30, 2016.

12. Credit Facility

On February 18, 2015, the Company entered into a multi-currency credit agreement with a syndicate of banks, financial institutions and other lending entities (the Credit Agreement), pursuant to which a secured revolving credit facility of up to $100.0 million in the aggregate was made available to the Company. On January 22, 2016, the Company entered into the First Amendment to the Credit Agreement, pursuant to which the Company exercised its option to increase the credit facility to up to $150.0 million in the aggregate with the existing lenders and an additional lender and amended the Credit Agreement to provide the Company with an option to further increase the credit facility by an additional $50.0 million, which, if exercised, would provide the Company with access to a secured revolving credit facility of up to $200.0 million. The credit facility is available to the Company on a revolving basis during the period from February 18, 2015 through February 18, 2020. The Company may prepay the loans or terminate or reduce the commitments in whole or in part at any time, without premium or penalty, subject to certain conditions and costs in the case of Eurodollar rate loans. The Company repaid $7.5 million in March, April and July 2016 reducing its outstanding debt balance from $60.0 million to $37.5 million as of September 30, 2016. On October 24, 2016, the Company repaid an additional $7.5 million of outstanding borrowings. The Company and its subsidiaries expect to use the credit facility for general corporate purposes, including, but not limited to, the potential acquisition of complementary products or businesses, share repurchases, as well as for working capital.

Loans under the credit facility bear interest at variable rates which reset every 30 to 180 days depending on the rate and period selected by the Company as described below. As of September 30, 2016, the annual rate on the $37.5 million revolving loan was 2.06% and was renewed at 2.06% on October 24, 2016. The average interest rate on borrowings outstanding for the period ending September 30, 2016 was 1.98%. The quarterly commitment fee on the undrawn portion of the credit facility ranges from 0.20% to 0.30% per annum, based upon the Company s total leverage ratio. As of September 30, 2016, the fair value of the credit facility approximated its book value.

The Credit Agreement contains customary affirmative and negative covenants, including covenants that limit or restrict the Company and its subsidiaries ability to, among other things, incur indebtedness, grant liens, merge or consolidate, dispose of assets, change the nature of its business, make investments and acquisitions, pay dividends or make distributions, or enter into certain transactions with affiliates, in each case subject to customary and other exceptions for a credit facility of this size and type, each as further described in the Credit Agreement. The Credit Agreement also imposes limits on capital expenditures of the Company and its subsidiaries and requires the Company to maintain a maximum total leverage ratio (not greater than 2.75:1.00) and a minimum interest coverage ratio (not less than 3.00:1.00), each as further defined in the Credit Agreement. As of September 30, 2016, the total leverage ratio was 0.52:1.00, the minimum interest coverage ratio was 71.7:1.00 and the Company was in compliance with all financial and operating covenants of the Credit Agreement.

Any failure to comply with the financial or operating covenants of the Credit Agreement would prevent the Company from being able to borrow additional funds, and would constitute a default, permitting the lenders to, among other things, accelerate the amounts outstanding, including all accrued interest and unpaid fees, under the credit facility and to terminate the credit facility.

As of September 30, 2016, the Company had $0.9 million of origination costs recorded in other assets. The Company incurred $1.0 million of origination costs for the period ending December 31, 2015 in connection with entering into the Credit Agreement. The Company incurred an additional $0.3 million of origination costs in connection with the First Amendment to the Credit Agreement executed in January 2016. As permitted by FASB issued ASU 2015-15, the Company has elected to present debt issuance costs as an asset and subsequently amortize the deferred debt issuance costs ratably over the term of the credit facility.

13. Subsequent Events

On October 27, 2016, the Company announced that the Board of Directors declared a second special cash dividend of $0.50 per share of common stock (or approximately $12.7 million in the aggregate), as permitted by the Merger Agreement. The dividend will be payable on November 22, 2016 to stockholders of record on November 7, 2016.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and the related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and the audited condensed consolidated financial statements and notes thereto and management s discussion and analysis of financial condition and results of operations for the year ended December 31, 2015 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission, or SEC, on February 19, 2016. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the section titled Risk Factors, set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and elsewhere in this Report. The forward-looking statements in this Quarterly Report on Form 10-Q represent our views as of the date of this Quarterly Report on Form 10-Q. We anticipate that subsequent events and developments will cause our views to change. However, while we may elect to update these forward-looking statements at some point in the future, we have no current intention of doing so except to the extent required by applicable law. You should, therefore, not rely on these forward-looking statements as representing our views as of any date subsequent to the date of this Quarterly Report on Form 10-Q.

Overview

LogMeIn simplifies how people connect to their colleagues, employees, devices and the world around them. With millions of users worldwide, our cloud-based solutions make it possible for people and companies to connect and engage with their workplace, colleagues, customers and products anywhere, anytime. Our services are focused on high growth markets such as Identity and Access Management, Collaboration and the Internet of Things and are delivered via the cloud as hosted services, commonly called software-as-a-service, or SaaS.

We offer both free and fee-based, or premium, subscription software services. Sales of our premium subscription software services are generated through word-of-mouth referrals, web-based advertising, online search, off-line advertising, broadcast advertising, the conversion of free users and expiring free trials to paid subscriptions and direct marketing to new and existing customers. We derive our revenue principally from subscription fees from SMBs, IT service providers, mobile carriers, customer service centers, original equipment manufacturers, or OEMs, and consumers and to a lesser extent, from the delivery of professional services primarily related to our Internet of Things business. The majority of our customers subscribe to our services on an annual basis. Our revenue is driven primarily by the number and type of our premium subscription software services to which our paying customers subscribe. For the nine months ended September 30, 2016, we generated revenues of $248.1 million, compared to $195.5 million for the nine months ended September 30, 2015, an increase of 27%. Revenue from LastPass, which we acquired in the fourth quarter of 2015, was $13.2 million for the nine months ended September 30, 2016.

We reported GAAP net income of $8.3 million and $0.8 million for the nine months ended September 30, 2015 and 2016, respectively, which includes the impact of a legal settlement in the first quarter of 2015, our acquisition of LastPass in the fourth quarter of 2015, and transaction-related and integration-related fees and expenses in connection with the proposed Merger (described below) announced early in the third quarter of 2016. Our operating results for the nine months ended September 30, 2015 and 2016 include acquisition-related expenses of $3.8 million and $16.9 million, respectively, amortization of acquired intangible assets of $3.0 million and $7.6 million, respectively, and litigation-related expenses of $4.9 million for the nine months ended September 30, 2015. We continued to generate

strong cash flows from operations of $72.0 million and $84.1 million for the nine months ended September 30, 2015 and 2016, respectively. As of September 30, 2016, we had cash, cash equivalents and short-term marketable securities of $217.2 million, an increase of $8.8 million from December 31, 2015. During the nine months ended September 30, 2016, we repaid $22.5 million of the $60.0 million borrowed under our credit facility in October 2015 to fund our acquisition of LastPass, repurchased $22.8 million of our common stock pursuant to our share repurchase program, and paid a cash dividend of $12.7 million to our common stockholders.

On July 26, 2016, we entered into an agreement and plan of merger, which we refer to as the Merger Agreement, with Citrix Systems, Inc., or Citrix, and GetGo, Inc., or GetGo, a wholly-owned subsidiary of Citrix, pursuant to which we will combine with Citrix s GoTo family of products known as the GoTo Business in a Reverse Morris Trust transaction, which we refer to herein as the Merger. Following the Merger, Citrix s stockholders will own approximately 50.1% of all of our outstanding shares on a fully diluted basis, while our existing stockholders will own approximately 49.9% of our shares on a fully diluted basis. Based upon the reported closing price of our common stock on the NASDAQ Global Select Market of $65.31 per share on July 25, 2016, the last trading day before signing of the Merger Agreement, the estimated total value of the shares to be issued by us to Citrix stockholders in the Merger would have been approximately $1.8 billion. Based upon the reported closing price of our common stock on the NASDAQ Global Select Market of $90.52 per share on September 6, 2016, the estimated total value of the shares to be issued by us to Citrix stockholders pursuant to the Merger would have been approximately $2.5 billion. The actual total value of the consideration to be paid by us in connection with the Merger will depend on the market price of shares of our common stock at the time of the closing of the Merger. The transaction, which has been unanimously approved by our Board of Directors and the Board of Directors of Citrix is expected to be generally tax-free to Citrix and its stockholders for U.S. federal income tax purposes.

The consummation of the Merger and the related transactions are subject to our stockholders approving the issuance of shares in connection with the Merger, the receipt of certain regulatory approvals and other customary closing conditions, including receipt of opinions of counsel with respect to the tax-free nature of the proposed transaction. On September 26, 2016, we announced the early termination of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act for the proposed Merger. The transaction is expected to close in the first quarter of 2017. If the Merger Agreement is terminated under certain circumstances we may be required to pay Citrix Systems, Inc. a termination fee of $62 million or may under other circumstances be required to reimburse Citrix Systems, Inc. up to $10 million for certain expenses in connection with the Merger.

We expect to incur significant one-time costs in connection with the Merger in 2016 and into 2017, including approximately $45 million to $50 million of transaction, transition, and integration-related fees and expenses, including legal, accounting and other professional fees. During the nine months ended September 30, 2016, we incurred $9.8 million of transaction, transition, and integration-related fees and expenses and we expect to incur an additional $9 million of these expenses during the remainder of 2016.

On July 26, 2016, we also announced that our Board of Directors declared a special cash dividend of $0.50 per share of common stock. The dividend was paid on August 26, 2016 and totaled $12.7 million. We intend to declare and pay two additional special cash dividends of $0.50 per share of common stock, as permitted by the Merger Agreement. On October 27, 2016, we announced that the second special cash dividend of $0.50 per share of common stock would be payable on November 22, 2016 to stockholders of record on November 7, 2016. The third dividend is expected to be declared and paid shortly before the consummation of the Merger, subject to the Merger Agreement being in effect. The Merger Agreement also permits us to declare additional dividends as follows: (1) in the event the closing of the Merger does not occur on or before March 31, 2017, we may pay an additional dividend of $0.50 per share with respect to the completed first quarter of calendar year 2017; (2) in the event the closing of the Merger does not occur on or before June 30, 2017, we may pay an additional dividend of $0.50 per share with respect to the completed second quarter of calendar year 2017; and (3) in the event the closing of the Merger does not occur on or before September 30, 2017, we may pay an additional dividend of $0.50 per share with respect to the completed third quarter of calendar year 2017.

Under our stock repurchase program, shares may be repurchased from time-to-time in the open market, which may include the use of 10b5-1 trading plans, or in privately negotiated transactions, in accordance with applicable securities and stock exchange rules. For the three months ended September 30, 2016, we repurchased 45,562 shares of our common stock at an average price of $75.98 per share for a total cost of $3.5 million. There were no shares repurchased during the three months ended September 30, 2015. For the nine months ended September 30, 2015 and 2016 we repurchased 249,400 and 416,474 shares of our common stock at an average price of $59.07 and $54.74 per share for a total cost of $14.7 million and $22.8 million, respectively. At September 30, 2016, $33.5 million remained available under our share repurchase program.

Certain Trends and Uncertainties

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

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

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

Failure to complete the previously announced Merger could adversely impact the market price of our common stock as well as our business and operating results. This risk, as well as risks associated with the Merger, are identified further in Risk Factors Risks Related to the Transactions of this Quarterly Report on Form 10-Q and elsewhere in this report.

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

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

Sources of Revenue

We derive our revenue primarily from subscription fees for our premium services from enterprise customers, SMBs, IT service providers, mobile carriers, customer service centers, OEMs and consumers and to a lesser extent, from the delivery of professional services primarily related to our Internet of Things business. The majority of our customers subscribe to our services on an annual basis and pay in advance, typically with a credit card, for their subscription. A smaller percentage of our customers subscribe to our services on a monthly basis through either month-to-month commitments or annual commitments that are then paid monthly with a credit card. We initially record a subscription fee as deferred revenue and then recognize it ratably, on a daily basis, over the life of the subscription period. Typically, a subscription automatically renews at the end of a subscription period unless the customer specifically terminates it prior to the end of the period. For the three months ended September 30, 2016, our gross annualized renewal rate was approximately 75%. We calculate our gross renewal rate on an annualized dollar basis across all product lines as of the end of each period. We expect our gross renewal rate to remain relatively consistent as we continue to invest in our products, customer support organization, and related retention programs.

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Our revenue by service cloud (product grouping) is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Revenues:				
Collaboration cloud	$ 22,930	$ 30,240	$ 63,148	$ 85,837
Identity and Access Management cloud	23,718	30,524	65,718	88,268
Service and Support cloud	22,363	23,871	64,783	72,233
Other	562	468	1,867	1,765
Total revenue	$ 69,573	$ 85,103	$ 195,516	$ 248,103

Employees

We have increased our number of full-time employees to 1,109 at September 30, 2016 as compared to 1,006 at December 31, 2015 and 964 at September 30, 2015.

Cost of Revenue and Operating Expenses

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

Cost of Revenue. Cost of revenue consists primarily of costs associated with our data center operations, customer support centers and our Xively professional services team. Included in these costs are wages and benefits for personnel, telecommunications, hosting fees, hardware and software maintenance costs, consulting fees associated with outsourced customer support staffing and professional services team projects, depreciation associated with our data centers and contingent bonus expense related to our acquisitions (see Note 4 to the Condensed Consolidated Financial Statements). Additionally, amortization expense associated with the acquired software, technology and documented know-how, as well as internally developed software is included in cost of revenue. The expenses related to hosting our services and supporting our free and premium customers are dependent on the number of customers who subscribe to our services and the complexity and redundancy of our services and hosting infrastructure. The expenses related to our professional services team are primarily driven by our investment in and efforts to support the growth of our Internet of Things business. We expect cost of revenue expenses to increase in absolute dollars but remain relatively constant as a percentage of revenue as we continue to invest in our data center infrastructure and operations and customer support efforts.

Research and Development. Research and development expenses consist primarily of wages and benefits for development personnel, contingent bonus expense related to our acquisitions, rent expense primarily related to our offices in Hungary and Boston, consulting fees associated with outsourced development projects, travel-related costs for development personnel, and depreciation of assets used in development. Our research and development efforts are focused on both improving ease of use and functionality of our existing services, as well as developing new offerings. The majority of our research and development employees are located in our development centers in Hungary. Therefore, a majority of research and development expense is subject to fluctuations in foreign exchange rates. We

capitalized costs of $2.2 million and $1.0 million for the nine months ended September 30, 2015 and 2016, respectively, related to internally developed computer software to be sold as a service, which were incurred during the application development stage. The majority of research and development costs have been expensed as incurred. We expect that research and development expenses will increase in absolute dollars as we continue to enhance and expand our services but will remain relatively constant as a percentage of revenue.

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

General and Administrative. General and administrative expenses consist primarily of wages and benefits for management, human resources, internal IT support, legal, finance and accounting personnel, professional fees, insurance and other corporate expenses, including acquisition-related expenses. We expect that general and administrative expenses related to personnel, recruiting, internal information systems, audit, accounting and insurance costs will increase in absolute dollars but will remain relatively constant as a percentage of revenue as we continue to support the growth of our business. We expect that acquisition-related expenses will increase both in absolute dollars and as a percentage of revenue over the remainder of 2016 and into 2017 in conjunction with the Merger. General and administrative expenses could increase if we incur litigation-related expenses associated with our defense against legal claims.

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Critical Accounting Policies

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

Revenue recognition;

Income taxes;

Goodwill and acquired intangible assets;

Stock-based compensation; and

Loss contingencies.

Results of Consolidated Operations

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2016	2015	2016
Revenue	100%	100%	100%	100%
Cost of revenue	12	13	13	14
Gross profit	88	87	87	86
Operating expenses:				
Research and development	15	17	15	17
Sales and marketing	49	46	53	50
General and administrative	12	22	12	16
Legal settlements				