Five9, Inc.
Form 10-Q
November 01, 2016
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016
OR
o 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: 001-36383

Five9, Inc.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	94- 3394123
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

Bishop Ranch 8
4000 Executive Parkway, Suite 400
San Ramon, CA 94583
(Address of Principal Executive Offices) (Zip Code)
(925) 201-2000
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes: x No: o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes: x No: o
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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer	o	Accelerated Filer	x
Non-accelerated filer	o (Do not check if a smaller reporting Company)	Smaller Reporting Company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes: o No: x
As of October 25, 2016, there were 52,968,430 shares of the Registrant's common stock, par value $0.001 per share, outstanding.

Table of Contents

FIVE9, INC.
FORM 10-Q
TABLE OF CONTENTS

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS	2
PART I. FINANCIAL INFORMATION	
ITEM 1. Financial Statements	3
Condensed Consolidated Balance Sheets (Unaudited)	3
Condensed Consolidated Statements of Operations and Comprehensive Loss (Unaudited)	4
Condensed Consolidated Statements of Cash Flows (Unaudited)	5
Notes to Condensed Consolidated Financial Statements (Unaudited)	6
ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	18
Overview	18
Key Operating and Financial Performance Metrics	20
Key Components of Our Results of Operations	21
Results of Operations for the Three and Nine Months Ended September 30, 2016 and 2015	23
Liquidity and Capital Resources	26
Critical Accounting Policies and Estimates	27
Off Balance Sheet Arrangements	27
Contractual Obligations	27
ITEM 3. Quantitative and Qualitative Disclosure about Market Risk	28
ITEM 4. Controls and Procedures	28
PART II. OTHER INFORMATION	
ITEM 1. Legal Proceedings	30
ITEM 1A. Risk Factors	30
ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds	55
ITEM 3. Defaults Upon Senior Securities	55
ITEM 4. Mine Safety Disclosures	56
ITEM 5. Other Information	56
ITEM 6. Exhibits	57
SIGNATURES	58

Table of Contents

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which involve substantial risks and uncertainties. These statements reflect the current views of our senior management with respect to future events and our financial performance. These forward-looking statements include statements with respect to our business, expenses, strategies, losses, growth plans, product and client initiatives, market growth projections, and our industry. Statements that include the words “expect,” “intend,” “plan,” “believe,” “project,” “forecast,” “estimate,” “may,” “should,” “an similar statements of a future or forward-looking nature identify forward-looking statements for purposes of the federal securities laws or otherwise.

Forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause our actual results to differ materially from those indicated in these statements. These factors include the information set forth under the caption “Risk Factors” and elsewhere in this report, including the following:

- our quarterly and annual results may fluctuate significantly, may not fully reflect the underlying performance of our business and may result in decreases in the price of our common stock;
- if we are unable to attract new clients or sell additional services and functionality to our existing clients, our revenue and revenue growth will be harmed;
- our recent rapid growth may not be indicative of our future growth, and even if we continue to grow rapidly, we may fail to manage our growth effectively;
- failure to adequately expand our sales force could impede our growth;
- security breaches and improper access to or disclosure of our data or our clients’ data, or other cyber attacks on our systems, could result in litigation and regulatory risk, harm our reputation and adversely affect our business;
- the markets in which we participate are highly competitive, and if we do not compete effectively, our operating results could be harmed;
- if we fail to manage our technical operations infrastructure, our existing clients may experience service outages, our new clients may experience delays in the deployment of our solution and we could be subject to, among other things, claims for credits or damages;
- if our existing clients terminate their subscriptions or reduce their subscriptions and related usage, our revenues and gross margins will be harmed and we will be required to spend more money to grow our client base;
- we sell our solution to larger organizations that require longer sales and implementation cycles and often demand more configuration and integration services or customized features and functions that we may not offer, any of which could delay or prevent these sales and harm our growth rates, business and operating results;
- because a significant percentage of our revenue is derived from existing clients, downturns or upturns in new sales will not be immediately reflected in our operating results and may be difficult to discern;
- we rely on third-party telecommunications and internet service providers to provide our clients and their customers with telecommunication services and connectivity to our cloud contact center software and any failure by these service providers to provide reliable services could subject us to, among other things, claims for credits or damages;
- we have a history of losses and we may be unable to achieve or sustain profitability;
- we may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs; and
- failure to comply with laws and regulations could harm our business and our reputation.

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this report. If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, our actual results may differ materially from what we anticipate. You should not place undue reliance on our forward-looking statements. Any forward-looking statements you read in this report reflect our views only as of the date of this report with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. We undertake no obligation to update any forward-looking statements made in this report to reflect events or circumstances after the date of this report or to reflect new information or the occurrence of unanticipated events,

except as required by law.

Table of Contents

PART I. FINANCIAL INFORMATION
ITEM 1. Financial Statements
FIVE9, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	September 30, 2016 (Unaudited)	December 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	$ 57,333	$58,484
Accounts receivable, net	12,899	10,567
Prepaid expenses and other current assets	4,097	2,184
Total current assets	74,329	71,235
Property and equipment, net	13,690	13,225
Intangible assets, net	1,657	2,041
Goodwill	11,798	11,798
Other assets	1,225	934
Total assets	$ 102,699	$99,233
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 3,609	$2,569
Accrued and other current liabilities	10,500	7,911
Accrued federal fees	5,873	5,684
Sales tax liability	1,307	1,262
Revolving line of credit	—	12,500
Notes payable	1,070	7,212
Capital leases	5,634	4,972
Deferred revenue	8,838	6,413
Total current liabilities	36,831	48,523
Revolving line of credit — less current portion	32,594	—
Sales tax liability — less current portion	1,591	1,915
Notes payable — less current portion	470	17,327
Capital leases — less current portion	4,902	4,606
Other long-term liabilities	532	582
Total liabilities	76,920	72,953
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, $0.001 par value; 5,000 shares authorized, no shares issued and outstanding at September 30, 2016 and December 31, 2015	—	—
Common stock, $0.001 par value; 450,000 shares authorized, 52,967 shares and 51,165 shares issued and outstanding at September 30, 2016 and December 31, 2015, respectively	53	51
Additional paid-in capital	192,415	180,649
Accumulated deficit	(166,689)	(154,420)
Total stockholders' equity	25,779	26,280
Total liabilities and stockholders' equity	$ 102,699	$99,233

See accompanying notes to condensed consolidated financial statements.

3

Table of Contents

FIVE9, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(Unaudited, in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Revenue	$40,982	$ 32,287	$117,883	$ 92,835
Cost of revenue	17,790	14,812	51,164	43,860
Gross profit	23,192	17,475	66,719	48,975
Operating expenses:				
Research and development	6,041	5,473	17,642	17,079
Sales and marketing	12,925	10,797	38,268	31,322
General and administrative	6,143	6,087	18,561	19,389
Total operating expenses	25,109	22,357	74,471	67,790
Loss from operations	(1,917)	(4,882)	(7,752)	(18,815)
Other income (expense), net:				
Interest expense	(961)	(1,235)	(3,357)	(3,529)
Extinguishment of debt	(1,026)	—	(1,026)	—
Interest income and other	12	119	(66)	72
Total other income (expense), net	(1,975)	(1,116)	(4,449)	(3,457)
Loss before income taxes	(3,892)	(5,998)	(12,201)	(22,272)
Provision for (benefit from) income taxes	(2)	50	68	48
Net loss	$(3,890)	$ (6,048)	$(12,269)	$ (22,320)
Net loss per share:				
Basic and diluted	$(0.07)	$ (0.12)	$(0.24)	$ (0.45)
Shares used in computing net loss per share:				
Basic and diluted	52,708	50,369	52,078	49,931
Comprehensive Loss:				
Net loss and comprehensive loss	$(3,890)	$ (6,048)	$(12,269)	$ (22,320)

See accompanying notes to condensed consolidated financial statements.

Table of Contents

FIVE9, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Nine Months Ended September 30,	
	2016	2015
Cash flows from operating activities:		
Net loss	$(12,269)	$ (22,320)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	6,302	5,525
Provision for doubtful accounts	58	157
Stock-based compensation	6,927	6,010
Loss on disposal of property and equipment	1	10
Loss on extinguishment of debt	1,026	—
Amortization of debt discount and issuance costs	221	260
Accretion of interest	11	—
Others	(10)	40
Changes in operating assets and liabilities:		
Accounts receivable	(2,383)	(1,149)
Prepaid expenses and other current assets	(1,927)	(957)
Other assets	(25)	(178)
Accounts payable	1,039	(1,329)
Accrued and other current liabilities	2,749	788
Accrued federal fees and sales tax liability	(90)	161
Deferred revenue	2,449	192
Other liabilities	(75)	(83)
Net cash provided by (used in) operating activities	4,004	(12,873)
Cash flows from investing activities:		
Purchases of property and equipment	(973)	(689)
(Increase) Decrease in restricted cash	(60)	806
Purchase of short-term investments	—	(20,000)
Proceeds from maturity of short-term investments	—	40,000
Net cash (used in) provided by investing activities	(1,033)	20,117
Cash flows from financing activities:		
Proceeds from exercise of common stock options	4,050	419
Proceeds from sale of common stock under ESPP	792	680
Repayments of notes payable	(23,866)	(2,622)
Proceeds from revolving line of credit	32,594	—
Payment of prepayment penalty and related fees	(368)	—
Payments for debt issuance costs	(206)	—
Payments of capital leases	(4,618)	(4,509)
Repayments on revolving line of credit	(12,500)	—
Net cash used in financing activities	(4,122)	(6,032)
Net (decrease) increase in cash and cash equivalents	(1,151)	1,212
Cash and cash equivalents:		
Beginning of period	58,484	58,289
End of period	$57,333	$ 59,501
Non-cash investing and financing activities:		
Equipment obtained under capital lease	$5,548	$ 4,193

Equipment purchased and unpaid at period-end	13	84

See accompanying notes to the condensed consolidated financial statements.

Table of Contents

FIVE9, INC.
Notes to Condensed Consolidated Financial Statements (Unaudited)
1. Description of Business and Summary of Significant Accounting Policies
Five9, Inc. and its wholly-owned subsidiaries (the “Company”) is a provider of cloud software for contact centers. The Company was incorporated in Delaware in 2001 and is headquartered in San Ramon, California. The Company has offices in Europe and Asia, which primarily provide research, development, sales, marketing, and client support services.
Basis of Presentation
The accompanying condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015. All intercompany transactions and balances have been eliminated in consolidation.
Use of Estimates
The preparation of condensed consolidated financial statements in accordance 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 condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. The significant estimates made by management affect revenue, the allowance for doubtful accounts, intangible assets, goodwill, loss contingencies, including the Company’s accrual for federal fees and sales tax liability, accrued liabilities, stock-based compensation, provision for income taxes and uncertain tax positions. Management periodically evaluates such estimates and they are adjusted prospectively based upon such periodic evaluation. Actual results could differ from those estimates.
Significant Accounting Policies
The Company’s significant accounting policies are disclosed in its Annual Report on Form 10-K for the year ended December 31, 2015. During the nine months ended September 30, 2016, there were no changes to the Company's significant accounting policies.
Recently Adopted Accounting Pronouncements
In August 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-15, Classification of Certain Cash Receipts and Cash Payments (Topic 230), which addresses eight classification issues related to the statement of cash flows, including those for debt prepayment or debt extinguishment costs. ASU 2016-15 is effective for the Company in its first quarter of 2018, with early adoption permitted. As permitted by ASU 2016-15, the Company early-adopted this new guidance at the beginning of the third quarter of 2016 and applied it prospectively. No prior periods were retrospectively adjusted.
In November 2015, the FASB issued ASU No. 2015-17, Balance Sheet Classification of Deferred Taxes. This ASU eliminates the requirement for companies to present deferred tax assets and liabilities as current and noncurrent on the balance sheet and, instead, requires companies to classify all deferred tax assets and liabilities as noncurrent. As permitted by ASU 2015-17, the Company early-adopted this new guidance at the beginning of the fourth quarter of 2015 and applied it prospectively. No prior periods were retrospectively adjusted.
In April 2015, the FASB issued ASU No. 2015-05, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement. The ASU provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service

Table of Contents

contract. The ASU does not change the accounting for a customer's accounting for service contracts. A company can elect to adopt the ASU either prospectively or retrospectively. The Company adopted this guidance prospectively beginning in the first quarter of 2016 and the adoption did not have a material effect on its condensed consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The ASU requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by this ASU. In August 2015, the FASB issued ASU No. 2015-15, Interest—Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, which clarifies that the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The Company adopted this guidance retrospectively beginning in the first quarter of 2016 and the adoption did not have a material effect on its condensed consolidated financial statements for the prior periods or the current period reported.

Recent Accounting Pronouncements Not Yet Effective

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which requires measurement and recognition of expected credit losses for certain types of financial assets held. ASU 2016-13 is effective for the Company in its first quarter of 2020, and earlier adoption is permitted beginning in the first quarter of 2019. The Company is currently evaluating the impact of ASU 2016-13 on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. This ASU simplifies several aspects of the accounting for share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The guidance is effective for the Company beginning in the first quarter of 2017, with early application permitted. The Company is currently assessing the effect the guidance will have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). Under the new guidance, a lessee will be required to recognize assets and liabilities for both finance, or capital, and operating leases with lease terms of more than 12 months. The ASU also will require disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. Lessor accounting will remain largely unchanged from current GAAP. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach that includes a number of optional practical expedients that entities may elect to apply. This guidance is effective for the Company beginning in the first quarter of 2019. Early adoption is permitted. The Company is currently assessing the effect the guidance will have on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. The new guidance requires management of public and private companies to evaluate whether there is substantial doubt about the entity's ability to continue as a going concern and, if so, disclose that fact. Management will also be required to evaluate and disclose whether its plans alleviate that doubt. The standard will be effective for the Company's annual period ending December 31, 2016 and interim and annual periods thereafter. Early adoption is permitted. The Company does not expect that the requirement will have an impact on its financial position, results of operations or cash flows.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers: Topic 606 and issued subsequent amendments to the initial guidance in August 2015, March 2016, April 2016 and May 2016 within ASU 2015-04, ASU 2016-08, ASU 2016-10 and ASU 2016-12, respectively (ASU 2014-09, ASU 2015-04, ASU 2016-08, ASU 2016-10 and ASU 2016-12 collectively, Topic 606). Topic 606 requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers and will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. Topic 606 defines a five-step

process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than are required under existing GAAP. Topic 606 is effective for the Company's annual and interim reporting periods beginning January 1, 2018 using either a retrospective or a

Table of Contents

cumulative effect transition method. The Company has not yet selected a transition method or determined the effect of these ASUs on its ongoing financial reporting.

2. Fair Value Measurements

The Company carries cash equivalents consisting of money market funds at fair value on a recurring basis. Fair value is based on the price that would be received from selling an asset in an orderly transaction between market participants at the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

Level 1 — Observable inputs which include unadjusted quoted prices in active markets for identical assets.

Level 2 — Observable inputs other than Level 1 inputs, such as quoted prices for similar assets, quoted prices for identical or similar assets in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are based on management's assumptions, including fair value measurements determined by using pricing models, discounted cash flow methodologies or similar techniques.

The fair value of assets carried at fair value was determined using the following inputs (in thousands):

	September 30, 2016	
	Total	Level 1
Assets		
Cash equivalents		
Money market funds	$20,061	$20,061

	December 31, 2015	
	Total	Level 1
Assets		
Cash equivalents		
Money market funds	$20,010	$20,010

3. Financial Statement Components

Cash and cash equivalents consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Cash	$ 37,272	$ 38,474
Money market funds	20,061	20,010
Cash and cash equivalents	$ 57,333	$ 58,484

Accounts receivable, net consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Trade accounts receivable	$ 12,057	$ 9,554
Unbilled trade accounts receivable, net of advance client deposits	853	1,028
Allowance for doubtful accounts	(11)	(15)
Accounts receivable, net	$ 12,899	$ 10,567

Table of Contents

Prepaid expenses and other current assets consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Prepaid expenses	$ 3,494	$ 1,800
Other current assets	603	384
Prepaid expenses and other current assets	$ 4,097	$ 2,184

Property and equipment, net consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Computer and network equipment	$ 35,136	$30,277
Computer software	4,693	3,566
Internal-use software development costs	500	128
Furniture and fixtures	1,130	1,113
Leasehold improvements	624	619
Property and equipment	42,083	35,703
Accumulated depreciation and amortization	(28,393)	(22,478)
Property and equipment, net	$ 13,690	$13,225

Depreciation and amortization expense associated with property and equipment was $2.0 million and $5.9 million for the three and nine months ended September 30, 2016, respectively, and $1.7 million and $5.1 million for the three and nine months ended September 30, 2015, respectively.

Property and equipment capitalized under capital lease obligations consist primarily of computer and network equipment and were as follows (in thousands):

	September 30, 2016	December 31, 2015
Gross	$ 32,844	$27,302
Less: accumulated depreciation and amortization	(21,531)	(16,429)
Total	$ 11,313	$10,873

Accrued and other current liabilities consisted of the following (in thousands):

	September 30, 2016	December 31, 2015
Accrued compensation and benefits	$ 7,463	$ 5,718
Accrued expenses	3,037	2,193
Accrued and other current liabilities	$ 10,500	$ 7,911

4. Intangible Assets

The components of intangible assets were as follows (in thousands):

	September 30, 2016			December 31, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Developed technology	$2,460	$ (1,038)	$ 1,422	$2,460	$ (775)	$ 1,685
Customer relationships	520	(307)	213	520	(229)	291
Domain names	50	(30)	20	50	(22)	28
Non-compete agreements	140	(138)	2	140	(103)	37
Total	$3,170	$ (1,513)	$ 1,657	$3,170	$ (1,129)	$ 2,041

Table of Contents

Amortization expense related to intangible assets was $0.1 million and $0.4 million for the three and nine months ended September 30, 2016, respectively, and $0.1 million and $0.4 million for the three and nine months ended September 30, 2015, respectively.

As of September 30, 2016, the expected future amortization expense for intangible assets was as follows (in thousands):

Period	Expected Future Amortization Expense
Remainder of 2016	$ 119
2017	465
2018	442
2019	351
2020	280
Total	$ 1,657

5. Debt

2016 Loan and Security Agreement

On August 1, 2016 (the “Effective Date”), the Company entered into a loan and security agreement (the “2016 Loan and Security Agreement”) with the lenders party thereto and City National Bank, as agent for such lenders. The 2016 Loan and Security Agreement provides for a revolving line of credit (the “New Revolving Credit Facility”) of up to $50.0 million and matures on August 1, 2019. On the Effective Date, the Company borrowed $32.6 million under the 2016 Loan and Security Agreement. The proceeds were used to extinguish existing indebtedness under all prior Loan and Security Agreements and will be used for working capital and other general corporate purposes

Loans under the 2016 Loan and Security Agreement bear a variable annual interest rate of the prime rate plus 0.50%, subject to a 0.25% increase if our adjusted EBITDA is negative at the end of any fiscal quarter. The Company has agreed to pay a fee of 0.25% per annum on the unused portion of the revolving credit facility as well as an anniversary fee of $31,250 on each of the first and second anniversaries of the Effective Date. The Company is accreting the total estimation of unused fees and anniversary fees evenly over the full term of the 2016 Loan and Security Agreement. Under the terms of the 2016 Loan and Security Agreement, the outstanding balance cannot exceed the Company’s trailing four months of MRR (monthly recurring revenue including subscription and usage) multiplied by the average trailing 12 month dollar based retention rate (calculated on the same basis as in the Company’s periodic reports filed with the Securities and Exchange Commission). As of September 30, 2016, the outstanding principal balance under the 2016 Loan and Security Agreement was $32.6 million, which is included in 'Revolving line of credit — less current portion' in the condensed consolidated balance sheets. As of September 30, 2016, the amount available for additional borrowings was $17.4 million.

The Company incurred approximately $0.2 million in fees that were directly attributable to the issuance of this credit facility. These costs are deferred and included within 'Prepaid expenses and other current assets' and 'Other assets' in the Company's condensed consolidated balance sheets and being amortized to interest expense on a straight-line basis over three years starting from the Effective Date of the New Revolving Credit Facility.

The obligations of the Company under the 2016 Loan and Security Agreement are guaranteed by the Company’s subsidiary, Five9 Acquisition. The Company’s obligations under the 2016 Loan and Security Agreement and Five9 Acquisition’s obligations under its guaranty are secured by a first priority perfected security interest in and lien on substantially all of the Company’s and Five9 Acquisitions’ assets. The 2016 Loan and Security Agreement contains certain customary covenants, including the requirement that the Company maintain $25.0 million of unrestricted cash deposited with the lenders for the term of the agreement, a minimum liquidity ratio of unrestricted cash and accounts receivable to the outstanding amounts under the 2016 Loan and Security Agreement, as well as customary events of default. The Company was in compliance with these covenants as of September 30, 2016.

The Company recorded a $1.0 million loss on extinguishment of debt under the 2013 Loan and Security Agreement and the 2014 Loan and Security Agreement. The loss was comprised of $0.4 million in prepayment penalties, a $0.4

million write-off of unamortized debt discounts, and a $0.2 million write-off of unamortized debt issuance costs.

Table of Contents

2013 Loan and Security Agreement

Prior to entering into the 2016 Loan and Security Agreement on August 1, 2016, the Company had a revolving line of credit of up to $20.0 million ("Prior Revolving Credit Facility") under a loan and security agreement with a lender, which was entered into in March 2013 and last amended in December 2014 ("2013 Loan and Security Agreement"). The Prior Revolving Credit Facility carried a variable annual interest rate of the prime rate plus 0.50% and would mature on December 1, 2016.

The 2013 Loan and Security Agreement was collateralized by substantially all the assets of the Company. The balance outstanding could not exceed the lesser of (i) $20.0 million or (ii) an amount equal to the Company's monthly recurring revenue for the three months prior multiplied by the average Dollar-Based Retention Rate over the prior twelve months, less the amount accrued for the Company's Universal Service Fund ("USF") obligation (accrued federal fees). As of December 31, 2015, the outstanding principal balance under the Prior Revolving Credit Facility was $12.5 million, which is disclosed as a current liability, and the amount available for additional borrowings was $7.5 million. As of September 30, 2016, the Company had canceled and paid back all amounts due under the Prior Revolving Credit Facility.

In connection with its acquisition of SoCoCare in October 2013, the Company also borrowed $5.0 million under a term loan (the "Term Loan") under the 2013 Loan and Security Agreement in October 2013. Monthly interest-only payments were due on the advance at the prime rate plus 1.50% through September 2014. Principal and interest payments were due in equal monthly installments from October 2014 through the maturity of the Term Loan in March 2017. As December 31, 2015, $2.5 million in principal amount of this Term Loan was outstanding and is included as notes payable in the condensed consolidated balance sheets. As of September 30, 2016, the Company had canceled and paid back all amounts due under the Term Loan.

The 2013 Loan and Security Agreement contained certain covenants, including the requirement that the Company maintain $7.5 million of cash deposited with the lender for the term of the 2013 Loan and Security Agreement. The Company was in compliance with these covenants through the cancellation date of August 1, 2016. The 2013 Loan and Security Agreement remained senior to other debt, including the debt issued under the 2014 Loan and Security Agreement discussed below.

2014 Loan and Security Agreement

Prior to entering into the 2016 Loan and Security Agreement on August 1, 2016, the Company had a term loan facility of $30.0 million with a syndicate of two lenders ("Lenders"), which was entered into in February 2014 and amended in December 2014 and February 2015 (the "2014 Loan and Security Agreement"). The term loan facility was available to the Company in tranches. The first tranche for $20.0 million was advanced upon entering into the agreement. The remaining $10.0 million was available for drawdown by the Company until February 20, 2016 in $1.0 million increments, which expired on February 20, 2016. The Company incurred $0.4 million in debt costs in connection with borrowing the first tranche in February 2014. The term loan bore interest at a variable per annum rate equal to the greater of 10% or LIBOR plus 9%. Interest was due and payable on the last business day of each month during the term of the loan commencing in February 2014. Monthly principal payments were due beginning in February 2016 based on 1/60th of the outstanding balance at that time and would continue until all remaining principal outstanding under the term loan becomes due and payable in February 2019. As of December 31, 2015, $20.0 million of this loan facility was outstanding and is included as notes payable in the condensed consolidated balance sheets. As of September 30, 2016, the Company had canceled and paid back all borrowings under the 2014 Loan and Security Agreement.

The term loan was secured by substantially all the assets of the Company and was subordinate to the 2013 Loan and Security Agreement. The 2014 Loan and Security Agreement contained certain covenants and included the occurrence of a material adverse event, as defined in the agreement and determined by the Lenders, as an event of default. The Company was in compliance with these covenants through the effective cancellation date of August 1, 2016.

In connection with entering into the 2014 Loan and Security Agreement, the Company issued to the Lenders warrants to purchase 177,865 shares of common stock at $10.12 per share, which vest and become exercisable over a ten year term from the date of issuance, based on amounts drawn under the $30.0 million term loan facility. Based on the drawdown of $20.0 million in February 2014, 118,577 shares of common stock issuable under the warrants vested and

are exercisable by the Lenders. The fair value of these vested warrants of $1.0 million was recorded as a discount against the debt proceeds and was being recognized as additional interest expense over the term of the loan. The remaining 59,288 shares of common stock issuable under the warrants pertaining to the undrawn $10.0

Table of Contents

million did not vest and were no longer exercisable on February 20, 2016 when the $10.0 million was no longer available for borrowing.

Promissory Note

In July 2013, the Company issued a promissory note to the Universal Service Administrative Company ("USAC") for $4.1 million as a financing arrangement for that amount of accrued federal fees. The promissory note carried a fixed annual interest rate of 12.75% and was repayable in 42 equal monthly installments of principal and interest beginning in August 2013. As of September 30, 2016 and December 31, 2015, approximately $0.5 million and $1.5 million, respectively, of this promissory note was outstanding and is included as notes payable in the accompanying condensed consolidated balance sheets.

FCC Civil Penalty

In June 2015, the Company entered into a consent decree with the Federal Communications Commission ("FCC") Enforcement Bureau (Note 9), in which the Company agreed to pay a civil penalty of $2.0 million to the U.S. Treasury in twelve equal quarterly installments starting in July 2015 without interest. As a result, the Company discounted the $2.0 million liability, which was accrued in the third quarter of 2014 for the then tentative civil penalty, to its present value of $1.7 million at an annual interest rate of 12.75% to reflect the imputed interest and reclassified this discounted liability from 'Accrued federal fees' to 'Notes payable.' The $0.3 million discount was recorded as a reduction to general and administrative expense in the three months ended June 30, 2015 and is being recognized as interest expense over the payment term of the civil penalty. As of September 30, 2016 and December 31, 2015, the outstanding civil penalty payable was $1.2 million and $1.7 million, respectively, of which the net carrying value was $1.1 million and $1.4 million, respectively, and is included as 'Notes payable' in the accompanying condensed consolidated balance sheets.

As of September 30, 2016 and December 31, 2015, the Company’s outstanding debt is summarized as follows (in thousands):

	September 30, 2016	December 31, 2015
Term loan under 2014 Loan and Security Agreement	$ —	$ 20,000
Term loan under 2013 Loan and Security Agreement	—	2,500
Promissory note to USAC	470	1,459
FCC civil penalty	1,167	1,667
Total notes payable, gross	1,637	25,626
Less: discount	(108)	(1,087)
Total notes payable, net carrying value	1,529	24,539
Revolving line of credit	32,594	12,500
Interest accretion under 2016 line of credit	$ 11	$ —
Total debt, net carrying value	$ 34,134	$ 37,039
Less: current portion of debt *	(1,070)	(19,712)
Total debt, less current portion **	33,064	17,327

* Included in ‘Notes payable’ in the condensed consolidated balance sheets.
** Included in ‘Notes payable - less current portion’ and 'Revolving line of credit — less current portion' in the condensed consolidated balance sheets.

Table of Contents

Future principal payments of the Company's outstanding debt as of September 30, 2016 are as follows (in thousands):

Period	Amount to Mature
Remainder of 2016	$517
2017	786
2018	334
2019	32,594
Total	$34,231

6. Stockholders' Equity

Capital Structure

The Company is authorized to issue 450,000,000 shares of common stock with a par value of $0.001 per share. As of September 30, 2016 and December 31, 2015, the Company had 52,967,421 shares and 51,164,621 shares of common stock issued and outstanding, respectively.

The Company is also authorized to designate and issue up to 5,000,000 shares of preferred stock with a par value of $0.001 per share in one or more series without stockholder approval and to fix the rights, preferences, privileges and restrictions thereof. As of September 30, 2016 and December 31, 2015, the Company had no shares of preferred stock issued and outstanding.

Warrants

As of September 30, 2016 and December 31, 2015, the Company had outstanding warrants to purchase 131,597 and 190,885 shares of common stock, respectively, with a weighted-average exercise price of $9.89 per share and $9.96 per share, respectively. These warrants expire primarily in October 2023 and February 2024.

Common Stock Reserved for Future Issuance

Shares of common stock reserved for future issuance related to outstanding equity awards, common stock warrants, and employee equity incentive plans were as follows (in thousands):

	September 30, 2016
Stock options outstanding	5,626
Restricted stock units outstanding	2,096
Shares available for future grant under 2014 Plan	6,188
Shares available for future issuance under ESPP	1,258
Common stock warrants outstanding	132
Total shares of common stock reserved	15,300

Equity Incentive Plans

Prior to its initial public offering ("IPO"), the Company granted stock options under its Amended and Restated 2004 Equity Incentive Plan, as amended (the "2004 Plan").

In March 2014, the Company's board of directors and stockholders approved the 2014 Equity Incentive Plan ("2014 Plan") and 5,300,000 shares of common stock were reserved for issuance under the 2014 Plan. In addition, on the first day of each year beginning in 2015 and ending in 2024, the 2014 Plan provides for an annual automatic increase to the shares reserved for issuance in an amount equal to 5% of the total number of shares outstanding on December 31st of the preceding calendar year or a lesser number as determined by the Company's board of directors. Pursuant to the automatic annual increase, 2,558,231 and 2,466,124 additional shares were reserved under the 2014 Plan on January 1, 2016 and 2015, respectively.

No further grants were made under the 2004 Plan once the 2014 Plan became effective on April 3, 2014. Upon the effectiveness of the 2014 Plan, all shares reserved for future issuance under the 2004 Plan became available for issuance under the 2014 Plan. After the IPO, any forfeited or expired shares that would have otherwise returned to

Table of Contents

the 2004 Plan instead return to the 2014 Plan. As of September 30, 2016, 6,188,160 shares of common stock were available for future grant under the 2014 Plan.

The 2004 Plan and the 2014 Plan are described in the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

Stock Options

A summary of the Company's stock option activity during the nine months ended September 30, 2016 is as follows (in thousands, except years and per share data):

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding as of December 31, 2015	6,092	$ 4.58		
Options granted (weighted average grant date fair value of $4.07 per share)	742	8.66		
Options exercised	(920)	4.40		
Options forfeited or expired	(288)	6.83		
Outstanding as of September 30, 2016	5,626	$ 5.03	6.2	$ 60,000

The Company has computed the aggregate intrinsic value amounts disclosed in the above table based on the difference between the exercise price of the options and the closing market price of the Company's common stock of $15.68 per share as of September 30, 2016 for all in-the-money options outstanding.

Restricted Stock Units

A summary of the Company's restricted stock unit ("RSU") activity during the nine months ended September 30, 2016 is as follows (in thousands, except per share data):

	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Outstanding as of December 31, 2015	1,818	$ 5.01
RSUs granted	1,120	8.97
RSUs vested and released	(718)	5.44
RSUs forfeited	(124)	6.05
Outstanding as of September 30, 2016	2,096	$ 6.91

Employee Stock Purchase Plan

The Company's 2014 Employee Stock Purchase Plan ("ESPP") became effective on April 3, 2014 and is described in the Company's Annual Report on Form 10-K for the year ended December 31, 2015. The number of shares of common stock originally reserved for issuance under the ESPP was 880,000 shares, which will increase automatically each year, beginning on January 1, 2015 and continuing through January 1, 2024, by the lesser of (i) 1% of the total number of shares of the Company's common stock outstanding on December 31 of the preceding calendar year; (ii) 1,000,000 shares of common stock (subject to adjustment to reflect any split or combination of the Company's common stock); or (iii) such lesser number as determined by the Company's board of directors. Pursuant to the automatic annual increase, 511,646 additional shares were reserved under the ESPP on January 1, 2016. As of September 30, 2016, 1,258,442 shares of common stock were available for future grants under the ESPP.

During the three months ended September 30, 2016, no shares were purchased under the ESPP. During the nine months ended September 30, 2016, 164,310 shares were purchased on May 13, 2016 at a price of $4.82 per share under the ESPP.

14

Table of Contents

Stock-Based Compensation

Stock-based compensation expenses for the three and nine months ended September 30, 2016 and 2015 were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Cost of revenue	$357	$ 233	$951	$ 639
Research and development	547	475	1,510	1,389
Sales and marketing	626	448	1,604	1,430
General and administrative	989	789	2,862	2,552
Total stock-based compensation	$2,519	$ 1,945	$6,927	$ 6,010

As of September 30, 2016, unrecognized stock-based compensation expenses by award type, net of estimated forfeitures, and their expected weighted-average recognition periods are summarized in the following table (in thousands, except years).

	Stock Option	RSU	ESPP
Unrecognized stock-based compensation expense	$6,154	$12,124	$109
Weighted-average amortization period	2.3 years	2.9 years	0.1 years

The Company recognizes stock-based compensation expense that is calculated based upon awards ultimately expected to vest and, thus, stock-based compensation expense is reduced for estimated forfeitures. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. All stock-based compensation for equity awards granted to employees and non-employee directors is measured based on the grant date fair value of the award.

The Company values RSUs at the closing market price of its common stock on the date of grant. The Company estimates the fair value of each stock option and purchase right under the ESPP granted to employees on the date of grant using the Black-Scholes option-pricing model and using the assumptions noted in the below table. The weighted-average assumptions used to value stock options granted during the three and nine months ended September 30, 2016 and 2015 were as follows:

Stock Options	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Expected term (years)	6.1	6.1	6.0	6.1
Volatility	48%	48%	48%	49%
Risk-free interest rate	1.2%	1.6%	1.5%	1.5%
Dividend yield	—	—	—	—

7. Net Loss Per Share

Basic net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period, and excludes any dilutive effects of employee stock-based awards and warrants. Diluted net income per share is computed giving effect to all potentially dilutive common shares, including common stock issuable upon exercise of stock options and warrants and vesting of restricted stock. As the Company had net losses for the three and nine months ended September 30, 2016 and 2015, all potentially issuable common shares were determined to be anti-dilutive.

Table of Contents

The following table presents the calculation of basic and diluted net loss per share (in thousands, except per share data).

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Net loss	$(3,890)	$ (6,048)	$(12,269)	$ (22,320)
Weighted-average shares used in computing basic and diluted net loss per share	52,708	50,369	52,078	49,931
Basic and diluted net loss per share	$(0.07)	$ (0.12)	$(0.24)	$ (0.45)

The following securities were excluded from the calculation of diluted net loss per share attributable to common stockholders because their effect would have been anti-dilutive for the periods presented (in thousands).

	September 30, 2016	September 30, 2015
Stock options	5,626	6,553
Restricted stock units	2,096	1,606
ESPP	—	189
Common stock warrants	132	360
Total	7,854	8,708

8. Income Taxes

The provision for income taxes for the three and nine months ended September 30, 2016 was approximately $(2) thousand and $68 thousand, respectively. The provision for income taxes for the three and nine months ended September 30, 2015 was approximately $50 thousand and $48 thousand, respectively. The provision for or benefit from income taxes consisted primarily of foreign income taxes.

For the three and nine months ended September 30, 2016 and 2015, the provision for or benefit from income taxes differed from the statutory amount primarily due to the Company realizing no benefit for current year losses due to maintaining a full valuation allowance against its domestic and U.K. net deferred tax assets.

The realization of tax benefits of deferred tax assets is dependent upon future levels of taxable income, of an appropriate character, in the periods the items are expected to be deductible or taxable. Based on the available objective evidence, the Company does not believe it is more likely than not that the net deferred tax assets will be realizable. Accordingly, the Company has provided a full valuation allowance against the domestic and U.K. net deferred tax assets as of September 30, 2016 and December 31, 2015. There were no U.K. deferred tax assets as of December 31, 2015. The Company intends to maintain the remaining valuation allowance until sufficient positive evidence exists to support a reversal of, or decrease in, the valuation allowance. During the three and nine months ended September 30, 2016, there were no material changes to the total amount of unrecognized tax benefits.

9. Commitments and Contingencies

Commitments

The Company’s principal commitments consist of future payment obligations under capital leases to finance data centers and other computer and networking equipment purchases, operating lease agreements for office space, research and development, and sales and marketing facilities, and agreements with third parties to provide co-location hosting, telecommunication usage and equipment maintenance services. These commitments as of December 31, 2015 are disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, and did not change materially during the nine months ended September 30, 2016 except for the acquisition of certain additional data center and network equipment and software under multiple capital leases. As of September 30, 2016, the total minimum future payment commitments under these capital leases added during the nine months ended September 30, 2016 were approximately $6.2 million, of which $0.6 million is due in 2016, with the remainder of $5.6 million due over approximately 35 months.

Universal Services Fund Liability

During the third quarter of 2012, the Company determined that based on its business activities, it is classified as a telecommunications service provider for regulatory purposes and it should make direct contributions to the

federal USF and related funds based on revenues it receives from the resale of interstate and international telecommunications services. Previously, the Company had believed that the telecommunications services were an integral part of an information service that the Company provides via its software and had instead made indirect USF contributions via payments to its wholesale telecommunications service providers. In order to comply with the obligation to make direct contributions, the Company made a voluntary self-disclosure to the FCC Enforcement Bureau and registered with the USAC, which is charged by the FCC with administering the USF. The Company filed exemption certificates with its wholesale telecommunications service providers in order to eliminate its obligation to reimburse such wholesale telecommunications service providers for their USF contributions calculated on services sold to the Company.

The Company's registration with USAC subjects it to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to its late registration and past failure to recognize its obligation as a USF contributor and as an international carrier. The Company will be required to pay assessments for periods prior to the Company's registration. As of December 31, 2012, the total past due USF contribution being imposed by USAC and accrued by the Company for the period from 2003 through 2012 was $8.1 million, of which $4.7 million was undisputed and $3.4 million, including $0.8 million that pertains to 2003 through 2007, was disputed. While the Company is in administrative proceedings before the FCC to limit such back assessments to the period 2008 through 2012, it is possible that it will be required to pay back assessments for the period from 2003 through 2007. In 2013, the Company began remitting required contributions on a prospective basis directly to USAC.

In July 2013, the Company and USAC agreed to a financing arrangement for $4.1 million of the undisputed $4.7 million of the unpaid USF contributions whereby the Company issued to USAC a promissory note payable in the principal amount of the $4.1 million and paid off the remaining undisputed $0.6 million. The repayment terms of the promissory note payable are disclosed in Note 5. As of September 30, 2016 and December 31, 2015, the principal balance of the promissory note payable was $0.5 million and $1.5 million, respectively, and is included in the notes payable amounts on the condensed consolidated balance sheets. In addition to the promissory note payable, as of September 30, 2016 and December 31, 2015, the Company had an accrued liability for the disputed portion of the unpaid USF contributions and estimated interest and penalties of $5.2 million and $4.9 million, respectively, included in accrued federal fees on the condensed consolidated balance sheets. For the three and nine months ended September 30, 2016, the Company recorded interest and penalty expenses of $0.1 million and $0.3 million as a charge to general and administrative expense, which were related to its disputed unpaid USF obligations.

On June 12, 2015, in connection with the Company's disclosure to the FCC, the Company entered into a consent decree with the FCC Enforcement Bureau. In the consent decree, the Company agreed to pay a civil penalty of $2.0 million to the U.S. Treasury in twelve equal quarterly installments starting in July 2015 without interest (Note 5). In the third quarter of 2014, the Company accrued a $2.0 million liability for the then tentative civil penalty. The consent decree also requires the Company to adopt certain internal regulatory compliance monitoring and training requirements, and to report on the status of those compliance efforts to the FCC's Enforcement Bureau for three years. The Company's implementation of the internal regulatory compliance monitoring and training requirements were completed in August 2015, and its annual compliance reporting to the FCC will continue until June 2018.

State and Local Taxes and Surcharges

In April 2012, the Company commenced collecting and remitting sales taxes on sales of subscription services in all the U.S. states in which it determined it was obligated to do so. During the first quarter of 2015, the Company conducted an updated sales tax review of the taxability of sales of its subscription services. As a result, the Company determined that it may be obligated to collect and remit sales taxes on such sales in four additional states. Based on its best estimate of the probable sales tax liability in those four states relating to its sales of subscription services during the period 2011 through 2014, during the three months ended March 31, 2015, the Company recorded a general and administrative expense of $0.6 million as an immaterial out of period adjustment to accrue for such taxes.

During 2013, the Company analyzed its activities and determined it may be obligated to collect and remit various state and local taxes and surcharges on its usage-based fees. The Company had not remitted state and local taxes on usage-based fees in any of the periods prior to 2014 and therefore accrued a sales tax liability for this contingency. In January 2014, the Company commenced paying such taxes and surcharges to certain state authorities. In June 2014, the Company commenced collecting state and local taxes or surcharges on usage-based fees from its clients on a current basis and remitting such taxes to the applicable U.S. state taxing authorities.

16

Table of Contents

During the three months ended September 30, 2016 and 2015, respectively, the Company remitted $0.5 thousand and $0.1 million for its contingent sales taxes on both usage-based fees and sales of subscription services. During the nine months ended September 30, 2016 and 2015, the Company has remitted $0.3 million and $1.0 million, respectively, for its contingent sales taxes on both usage-based fees and sales of subscription services.

The Company recognized a $0.1 million gain and a $0.3 million gain for the three and nine months ended September 30, 2016, respectively, and $17 thousand expense and $1.0 million expense for the three and nine months ended September 30, 2015, respectively, as general and administrative expense related to its estimated sales tax liability on both usage-based fees and sales of subscription services in the U.S. and Canada, which was not being collected from its clients.

As of September 30, 2016 and December 31, 2015, the Company had total accrued liabilities of $2.2 million and $2.7 million, respectively, for such contingent sales taxes and surcharges that were not being collected from its clients but may be imposed by various taxing authorities, of which $0.1 million and $0.8 million were included in current "Sales tax liability" on the condensed consolidated balance sheets, respectively, and the remaining were included in non-current "Sales tax liability" on the condensed consolidated balance sheets. The Company's estimate of the probable loss incurred under this contingency is based on its analysis of the source location of its usage-based fees and the regulations and rules in each tax jurisdiction.

Legal Matters

The Company is involved in various legal and regulatory matters arising in the normal course of business. In management's opinion, resolution of these matters is not expected to have a material impact on the Company's consolidated results of operations, cash flows, or its financial position. However, due to the uncertain nature of legal matters, an unfavorable resolution of a matter could materially affect the Company's future consolidated results of operations, cash flows or financial position in a particular period.

The Company is currently involved in the following lawsuits as a defendant.

Melcher Litigation

On September 28, 2016, a complaint was filed in the United States District Court for the Southern District of California against Five9, Inc. ("Five9"), as the successor in interest to Face It, Corp. ("Face It"), and Lance Fried, a former Five9 employee who was the former Chief Executive Officer of Face It. The action, captioned Melcher, et al. v. Five9, Inc., et al., No. 16-cv-02440, was filed as a direct action by Carl Melcher, a purported former stockholder of Face It, and his related investment entity.

In the complaint, the plaintiffs allege that Face It repurchased the plaintiffs' stock in September 2013 before Five9 acquired Face It, and that in connection with the repurchase, Fried made material misstatements or omissions to Melcher, by failing to disclose that Face It allegedly was in concurrent discussions about a potential sale of the company to Five9. The complaint alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, as well as various claims under state law and common law. The complaint seeks to set aside Face It's September 2013 stock repurchase from the plaintiffs, as well as an unspecified amount of damages and an award of attorney's fees and costs, in addition to other relief.

While the Company does not believe that it is probable that a loss has been incurred, the ultimate resolution of the matter could potentially result in a loss. Management's best estimate of the low end of the range of the potential loss is zero. At this time, it is not possible to reasonably estimate the high end of the range of the potential loss, which could be material to the Company's results of operations. Accordingly, the Company has not accrued a loss related to this matter.

NobelBiz Litigation

On August 5, 2011, NobelBiz sent a letter to the Company asserting infringement of a patent related to virtual call centers. On April 3, 2012, NobelBiz filed a patent infringement lawsuit against the Company in the United States District Court for the Eastern District of Texas. The patent asserted in the complaint is different, but related, to the patent asserted in the original letter. The lawsuit, NobelBiz Inc. v. Five9, Inc., Case No. 6:12-cv-00243-LED, alleges that the Company's local caller ID management service infringes United States Patent No. 8,135,122, or the '122 patent. The '122 patent, titled "System and Method for Modifying Communication Information (MCI)," issued on March 13, 2012, and according to the complaint is alleged to relate to "a system for processing a telephone call from a call

originator (also referred to as a calling party) to a call target (also referred to as a receiving party), where the system accesses a database storing outgoing telephone numbers, selects a replacement telephone number from

Table of Contents

the outgoing telephone numbers based on the telephone number of the call target, and originates an outbound call to the call target with a modified outgoing caller identification (‘caller ID’).” NobelBiz seeks damages in the form of lost profits as well as injunctive relief. The lawsuit is one of several lawsuits filed by NobelBiz against various companies including TCN Inc., LiveVox, Inc. and Global Connect LLC. On March 28, 2013, the court granted the Company’s motion to transfer the case to the United States District Court for the Northern District of California. Subsequently, NobelBiz amended its complaint to add claims related to U.S. Patent No. 8,565,399, or the ‘399 patent, which is a continuation in the same family as the ‘122 patent and addresses the same technology. The Company responded to the complaint and amended complaint by asserting noninfringement and invalidity of the ‘122 and ‘399 patents. On January 16, 2015, the court issued an order regarding claim construction of the two patents-in-suit. On March 7, 2016, the court stayed the case pending an appeal in lawsuits involving NobelBiz, Global Connect and TCN that also involve the ‘122 and ‘399 patents. The appeal for those cases is likely to last until late 2016 or into 2017, after which time the lawsuit between NobelBiz and Five9 will resume and a new schedule will be entered by the Court.

The Company has investigated the claims alleged in the complaint and believes that it has good defenses to the claims. While the Company does not believe that it is probable that a loss has been incurred, the ultimate resolution of the matter could potentially result in a loss. Management’s best estimate of the low end of the range of the potential loss is zero. At this time, it is not possible to reasonably estimate the high end of the range of the potential loss, which could be material to the Company’s results of operations. Accordingly, the Company has not accrued a loss related to this matter.

Indemnification Agreements

In the ordinary course of business, the Company may provide indemnification of varying scope and terms to clients, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of breach of such agreements, services to be provided by the Company or from intellectual property infringement claims made by third parties. In addition, the Company has entered into indemnification agreements with its directors, officers and certain employees that require the Company, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. No demands have been made upon the Company to provide indemnification under such agreements and thus there are no claims that the Company is aware of that would have a material effect on the Company’s condensed consolidated balance sheets, condensed consolidated statements of operations and comprehensive loss, or condensed consolidated statements of cash flows.

10. Geographical Information

The following table is a summary of revenues by geographic region based on client billing address and has been estimated based on the amounts billed to clients during the periods (in thousands).

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
United States	$38,251	$ 29,987	$109,948	$ 86,353
International	2,731	2,300	7,935	6,482
Total revenue	$40,982	$ 32,287	$117,883	$ 92,835

The following table summarizes total property and equipment, net in the respective locations (in thousands).

	September 30, 2016	December 31, 2015
United States	$ 11,846	$ 10,939
International	1,844	2,286
Property and equipment, net	$ 13,690	$ 13,225

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

You should read the following discussion in conjunction with the condensed consolidated financial statements and notes thereto included elsewhere in this report and in our Annual Report on Form 10-K for the year ended December 31, 2015.

Overview

We are a pioneer and leading provider of cloud software for contact centers, facilitating approximately three billion interactions between our more than 2,000 clients and their customers per year. We believe we achieved this leadership position through our expertise and technology, which has empowered us to help organizations of all sizes transition from legacy on-premise contact center systems to our cloud solution. Our solution, which is comprised of our Virtual Contact Center, or VCC, cloud platform and applications, allows simultaneous management and optimization of customer interactions across voice, chat, email, web, social media and mobile channels, either directly or through our application programming interfaces, or APIs. Our VCC cloud platform routes each customer interaction to an appropriate agent resource, and delivers relevant customer data to the agent in real-time to optimize the customer experience. Unlike legacy on-premise contact center systems, our solution requires minimal up-front investment and can be rapidly deployed and adjusted depending on our client's requirements.

Table of Contents

Since founding our business in 2001, we have focused exclusively on delivering cloud contact center software. We initially targeted smaller contact center opportunities with our telesales team and, over time, invested in expanding the breadth and depth of the functionality of our cloud platform to meet the evolving requirements of our clients. In 2009, we made a strategic decision to expand our market opportunity to include larger contact centers. This decision drove further investments in research and development and the establishment of our field sales team to meet the requirements of these larger contact centers. We believe this shift has helped us diversify our client base while significantly enhancing our opportunity for future revenue growth. To complement these efforts, we have also focused on building client awareness and driving adoption of our solution through marketing activities, which include internet advertising, digital marketing campaigns, social marketing, trade shows, industry events and telemarketing.

We provide our solution through a SaaS business model with recurring subscriptions. We offer a comprehensive suite of applications delivered on our VCC cloud platform that are designed to enable our clients to manage and optimize both inbound and outbound interactions. We primarily generate revenue by selling subscriptions and related usage of our VCC cloud platform. We charge our clients monthly subscription fees for access to our solution, primarily based on the number of agent seats, as well as the specific functionalities and applications our clients deploy. We define agent seats as the maximum number of named agents allowed to concurrently access our solution. Our clients typically have more named agents than agent seats, and multiple named agents may use an agent seat, though not simultaneously. Substantially all of our clients purchase both subscriptions and related telephony usage from us. A small percentage of our clients subscribe to our platform but purchase telephony usage directly from wholesale telecommunications service providers. We do not sell telephony usage on a stand-alone basis to any client. The related usage fees are based on the volume of minutes for inbound and outbound interactions. We also offer bundled plans, generally for smaller deployments, where the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. We offer monthly, annual and multiple-year contracts to our clients, generally with 30 days' notice required for changes in the number of agent seats. Our clients can use this notice period to rapidly adjust the number of agent seats used to meet their changing contact center volume needs, including to reduce the number of agent seats to zero. As a general matter, this means that a client can effectively terminate its agreement with us upon 30 days' notice. Our larger clients typically choose annual contracts, which generally include an implementation and ramp period of several months. Fixed subscription fees, including bundled plans, are generally billed monthly in advance, while related usage fees are billed in arrears. For the three and nine months ended September 30, 2016, subscription and related usage fees accounted for 96% and 95% of our revenue, respectively. For the three and nine months ended September 30, 2015, subscription and related usage fees accounted for 96% and 97% of our revenue, respectively. The remainder was comprised of professional services revenue from the implementation and optimization of our solution.

Our revenue increased to $41.0 million and $117.9 million for the three and nine months ended September 30, 2016 from $32.3 million and $92.8 million for the three and nine months ended September 30, 2015. Revenue growth has primarily been driven by our larger clients. For each of the three and nine months ended September 30, 2016 and 2015, no single client accounted for more than 10% of our total revenue. As of September 30, 2016, we had over 2,000 clients across multiple industries. Our clients' subscriptions generally range in size from fewer than 10 agent seats to approximately 1,000 agent seats.

We have continued to make significant expenditures and investments, including in sales and marketing, research and development and infrastructure. We primarily evaluate the success of our business based on revenue growth, adjusted EBITDA and the efficiency and effectiveness of our investments. The growth of our business and our future success depend on many factors, including our ability to continue to expand our client base, particularly in larger opportunities, grow revenue from our existing client base, develop innovative products and features, and expand internationally. While these areas represent significant opportunities for us, they also pose risks and challenges that we must successfully address in order to sustain the growth of our business and improve our operating results. In order to pursue these opportunities, we anticipate that we will continue to expand our operations and headcount in the near term.

Due to our continuing investments to grow our business, increase our sales and marketing efforts, pursue new opportunities, enhance our solution and build our technology, we expect our cost of revenue and operating expenses to

increase in absolute dollars in future periods. However, we expect these expenses to decrease as a percentage of revenue as we grow our revenue and gain economies of scale by increasing our client base without direct incremental development costs and by utilizing more of the capacity of our data centers.

Table of Contents

Key Operating and Financial Performance Metrics

In addition to measures of financial performance presented in our condensed consolidated financial statements, we monitor the key metrics set forth below to help us evaluate growth trends, establish budgets, measure the effectiveness of our sales and marketing efforts and assess operational efficiencies.

Annual Dollar-Based Retention Rate

We believe that our Annual Dollar-Based Retention Rate provides insight into our ability to retain and grow revenue from our clients, and is a measure of the long-term value of our client relationships. Our Annual Dollar-Based Retention Rate is calculated by dividing our Retained Net Invoicing by our Retention Base Net Invoicing on a monthly basis, which we then average using the rates for the trailing twelve months for the period being presented. We define Retention Base Net Invoicing as recurring net invoicing from all clients in the comparable prior year period, and we define Retained Net Invoicing as recurring net invoicing from that same group of clients in the current period. We define recurring net invoicing as subscription and related usage revenue excluding the impact of service credits, reserves and deferrals. Historically, the difference between recurring net invoicing and our subscription and related usage revenue has been within 10%.

The following table shows our Annual Dollar-Based Retention Rate for the periods presented:

	Twelve Months Ended	
	September 30, 2016	September 30, 2015
Annual Dollar-Based Retention Rate	100%	95%

The increase in our Annual Dollar-Based Retention Rate from September 30, 2015 to September 30, 2016 was primarily due to our larger clients both increasing the number of agent seats and increasing the revenue per agent seat.

Adjusted EBITDA

We monitor adjusted EBITDA, a non-GAAP financial measure, to analyze our financial results and believe that it is useful to investors, as a supplement to U.S. GAAP measures, in evaluating our ongoing operational performance and enhancing an overall understanding of our past financial performance. We believe that adjusted EBITDA helps illustrate underlying trends in our business that could otherwise be masked by the effect of the income or expenses that we exclude from adjusted EBITDA. Furthermore, we use this measure to establish budgets and operational goals for managing our business and evaluating our performance. We also believe that adjusted EBITDA provides an additional tool for investors to use in comparing our recurring core business operating results over multiple periods with other companies in our industry.

Adjusted EBITDA should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with U.S. GAAP and our calculation of adjusted EBITDA may differ from that of other companies in our industry. We compensate for the inherent limitations associated with using adjusted EBITDA through disclosure of these limitations, presentation of our financial statements in accordance with U.S. GAAP and reconciliation of adjusted EBITDA to the most directly comparable U.S. GAAP measure, net loss. We calculate adjusted EBITDA as net loss before (1) depreciation and amortization, (2) stock-based compensation, (3) interest income, expense and other, (4) provision for income taxes, and (5) other unusual items that do not directly affect what we consider to be our core operating performance.

Table of Contents

The following table shows a reconciliation from net loss to Adjusted EBITDA for the periods presented (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Net loss	$(3,890)	$ (6,048)	$(12,269)	$ (22,320)
Non-GAAP adjustments:				
Depreciation and amortization [1]	2,140	1,840	6,302	5,525
Stock-based compensation [2]	2,519	1,945	6,927	6,010
Interest expense	961	1,235	3,357	3,529
Extinguishment of debt	1,026	—	1,026	—
Interest income and other	(12)	(119)	66	(72)
Provision for (benefit from) income taxes	(2)	50	68	48
Out of period adjustment for sales tax liability [3]	—	—	—	765
Adjusted EBITDA	$2,742	$ (1,097)	$5,477	$ (6,515)

(1) Depreciation and amortization expenses included in our results of operations are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Cost of revenue	$1,668	$ 1,470	$4,964	$ 4,467
Research and development	204	126	513	315
Sales and marketing	56	52	163	152
General and administrative	212	192	662	591
Total depreciation and amortization	$2,140	$ 1,840	$6,302	$ 5,525

(2) See Note 6 of the notes to the condensed consolidated financial statements for stock-based compensation expense included in our results of operations for the periods presented.

(3) Included in general and administrative expense. The 2015 amounts represent immaterial out of period adjustments recorded in the first two quarters of 2015 for 2011 through 2014.

Key Components of Our Results of Operations

Revenue

Our revenue consists of subscription and related usage as well as professional services. We consider our subscription and related usage to be recurring revenue. This recurring revenue includes fixed subscription fees for the delivery and support of our VCC cloud platform, as well as related usage fees. The related usage fees are based on the volume of minutes for inbound and outbound client interactions. We also offer bundled plans, generally for smaller deployments, where the client is charged a single monthly fixed fee per agent seat that includes both subscription and unlimited usage in the contiguous 48 states and, in some cases, Canada. We offer monthly, annual and multiple-year contracts for our clients, generally with 30 days' notice required for changes in the number of agent seats. Our clients can use this notice period to rapidly adjust the number of agent seats used to meet their changing contact center volume needs, including to reduce the number of agent seats to zero. As a general matter, this means that a client can effectively terminate its agreement with us upon 30 days' notice.

Fixed subscription fees, including plans with bundled usage, are generally billed monthly in advance, while variable usage fees are billed in arrears. Fixed subscription fees are recognized on a straight-line basis over the applicable term, predominantly the monthly contractual billing period. Support activities include technical assistance for our solution and upgrades and enhancements on a when and if available basis, which are not billed separately. Variable subscription related usage fees for non-bundled plans are billed in arrears based on client-specific per minute rate plans and are recognized as actual usage occurs. We generally require advance deposits from clients based on estimated usage. All fees, except usage deposits, are non-refundable.

21

Table of Contents

In addition, we generate professional services revenue from assisting clients in implementing our solution and optimizing its use. These services include application configuration, system integration and education and training services. Professional services are primarily billed on a fixed-fee basis and are typically performed by us directly. In limited cases, our clients choose to perform these services themselves or engage their own third-party service providers to perform such services. Professional services are recognized as the services are performed using the proportional performance method, with performance measured based on labor hours, provided all other criteria for revenue recognition are met.

Cost of Revenue

Our cost of revenue consists primarily of personnel costs (including stock-based compensation), fees that we pay to telecommunications providers for usage, USF contributions and other regulatory costs, depreciation and related expenses of our servers and equipment, costs to build out and maintain co-location data centers, allocated office and facility costs and amortization of acquired technology. Cost of revenue can fluctuate based on a number of factors, including the fees we pay to telecommunications providers, which vary depending on our clients' usage of our VCC cloud platform, the timing of capital expenditures and related depreciation charges and changes in headcount. We expect to continue investing in our network infrastructure and operations and client support function to maintain high quality and availability of service. Therefore, we expect our cost of revenue to increase in absolute dollars, although these expenses are expected to generally trend down as a percentage of our revenue over the next few years. As our business grows, we expect to continue to realize economies of scale in network infrastructure, personnel and client support.

Operating Expenses

We classify our operating expenses as research and development, sales and marketing, and general and administrative expenses.

Research and Development. Research and development expenses consist primarily of salary and related expenses (including stock-based compensation) for personnel related to the development of improvements and expanded features for our services, as well as quality assurance, testing, product management and allocated overhead. We expense research and development expenses as they are incurred except for internal-use software development costs that qualify for capitalization. We believe that continued investment in our solution is important for our future growth, and we expect research and development expenses to increase in absolute dollars in the foreseeable future, although these expenses are expected to generally trend down as a percentage of our revenue over the next few years.

Sales and Marketing. Sales and marketing expenses consist primarily of salaries and related expenses (including stock-based compensation) for employees in sales and marketing, sales commissions, as well as advertising, marketing, corporate communications, travel costs and allocated overhead. We expense the costs of sales commissions associated with the acquisition or renewal of client contracts as incurred in the period the contract is acquired or the renewal occurs. We believe it is important to continue investing in sales and marketing to continue to generate revenue growth. Accordingly, we expect sales and marketing expenses to increase in absolute dollars as we continue to support our growth initiatives, although these expenses are expected to generally trend down as a percentage of our revenue over the next few years.

General and Administrative. General and administrative expenses consist primarily of salary and related expenses (including stock-based compensation) for management, finance and accounting, legal, information systems and human resources personnel, professional fees, compliance costs, other corporate expenses and allocated overhead. We expect that general and administrative expenses will fluctuate in absolute dollars from period to period, although these expenses are expected to generally trend down as a percentage of our revenue over the next few years.

Other Expense, Net

Other expense, net consists primarily of interest expense associated with our debt and capital leases. We expect interest expense for our outstanding debt to decrease due to a lower interest rate for our New Revolving Credit Facility compared to the 2014 Loan and Security Agreement and the 2013 Loan and Security Agreement (see Note 5 of the notes to condensed consolidated financial statements included in this Form 10-Q). We expect interest expense for our capital leases to increase as a result of our continued capital spending funded by capital leases.

22

Table of Contents

Provision for Income Taxes

Our provision for income taxes consists primarily of corporate income taxes resulting from profits generated in foreign jurisdictions by our wholly-owned subsidiaries, along with state income taxes payable in the United States.

Results of Operations for the Three and Nine Months Ended September 30, 2016 and 2015

Based on the condensed consolidated statements of operations and comprehensive loss set forth in this quarterly report, the following table sets forth our operating results as a percentage of revenue for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenue	100 %	100 %	100 %	100 %
Cost of revenue	43 %	46 %	43 %	47 %
Gross profit	57 %	54 %	57 %	53 %
Operating expenses:				
Research and development	15 %	17 %	15 %	18 %
Sales and marketing	32 %	33 %	32 %	34 %
General and administrative	15 %	19 %	17 %	21 %
Total operating expenses	62 %	69 %	64 %	73 %
Loss from operations	(5)%	(15)%	(7)%	(20)%
Other income (expense), net:				
Interest expense	(2)%	(4)%	(3)%	(4)%
Extinguishment of debt	(3)%	— %	(1)%	— %
Interest income and other	1 %	— %	1 %	— %
Total other income (expense), net	(4)%	(4)%	(3)%	(4)%
Loss before income taxes	(9)%	(19)%	(10)%	(24)%
Provision for (benefit from) income taxes	— %	— %	— %	— %
Net loss	(9)%	(19)%	(10)%	(24)%

Revenue

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Revenue	$40,982	$32,287	$8,695	27%	$117,883	$92,835	$25,048	27%

The increase in revenue for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily attributable to our larger clients, driven by an increase in our sales and marketing activities and our improved brand awareness. For the three and nine months ended September 30, 2016 and 2015, the majority of our revenue was from our larger clients. Our average recurring revenue per agent seat within our larger clients increased slightly between these periods due mainly to increased sales of add on products.

Table of Contents

Cost of Revenue

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Cost of revenue	$17,790	$14,812	$2,978	20%	$51,164	$43,860	$7,304	17%
% of Revenue	43%	46%			43%	47%		

The increase in cost of revenue for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily due to a $0.9 million and a $2.9 million increase in cash-based personnel costs driven by increased headcount, a $0.6 million and a $1.6 million increase in third party hosted software costs due to increased client activities, a $0.3 million and a $1.2 million increase in USF contributions and other federal telecommunication service fees primarily due to increased client usage, and a $0.4 million and a $1.1 million increase in facility-related costs, respectively. The remainder of the increase was primarily due to our business growth and system implementations. These increases were offset in part by a $0.1 million and a $1.4 million decrease in telecommunication carrier costs relating to our clients' long distance call usage due to improved usage efficiencies.

Gross Profit

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Gross profit	$23,192	$17,475	$5,717	33%	$66,719	$48,975	$17,744	36%
% of Revenue	57%	54%			57%	53%		

The increase in gross margin for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily due to improved efficiencies in usage, economies of scale for subscription, and higher amounts charged for, and better efficiencies in, professional services.

Operating Expenses

Research and Development

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Research and development	$6,041	$5,473	$568	10%	$17,642	$17,079	$563	3%
% of Revenue	15%	17%			15%	18%		

The increase in research and development expenses for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily due to a $0.2 million and a $0.2 million increase in consulting expenses, a $0.1 million and $0.2 million increase in depreciation expenses, a $0.1 million and $0.2 million increase in travel expenses, and a $0.1 million and $0.1 million increase in stock-based compensation expenses, respectively. The increase during the nine months ended September 30, 2016 compared to the same period of 2015 was also due to a $0.2 million increase in facilities and allocated overhead costs, offset by a $0.4 million decrease in cash-based personnel-related costs.

24

Table of Contents

Sales and Marketing

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Sales and marketing	$12,925	$10,797	$2,128	20%	$38,268	$31,322	$6,946	22%
% of Revenue	32%	33%			32%	34%		

The increase in sales and marketing expenses for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily due to a $0.9 million and a $2.7 million increase in cash-based personnel-related costs, and a $0.8 million and a $2.1 million increase in commissions paid to sales personnel, respectively, driven by the growth in sales and bookings of our solution. For the nine months ended September 30, 2016 compared to the same period of 2015, the increase was also driven by a $1.0 million increase in discretionary and other marketing-related expenses. These increases as well as the remainder of the increase were primarily due to the execution of our growth strategy to acquire new clients, grow the number of agent seats within our existing client base and establish brand awareness.

General and Administrative

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
General and administrative	$6,143	$6,087	$56	1%	$18,561	$19,389	$(828)	(4)%
% of Revenue	15%	19%			17%	21%		

The increase in general and administrative expenses for the three months ended September 30, 2016 compared to the same period of 2015 was primarily due to an increase of $0.3 million in cash-based personnel-related costs and an increase of $0.2 million in stock-based compensation costs, offset in part by decreases of $0.4 million in legal, state telecommunications taxes and audit costs.

The decrease in general and administrative expenses for the nine months ended September 30, 2016 compared to the same period of 2015 was primarily due to a $0.8 million immaterial out of period adjustment recorded in the first and the second quarters of 2015 for additional sales taxes for certain revenue earned during the period 2011 through the first quarter of 2015. In addition, for the nine months ended September 30, 2016 compared to the same period of 2015, we incurred increases of $0.4 million due to the one time benefit in the second quarter of 2015 related to our entry into a consent decree with the FCC and $0.3 million in stock-based compensation expense, offset by decreases of $0.4 million in state telecommunications taxes and $0.3 million in legal expenses.

Other Expense, Net

	Three Months Ended				Nine Months Ended			
	September 30, 2016	September 30, 2015	$ Change	% Change	September 30, 2016	September 30, 2015	$ Change	% Change
	(in thousands, except percentages)							
Interest expense	$(961)	$(1,235)	$274	(22)%	(3,357)	(3,529)	172	(5)%
Extinguishment of debt	(1,026)	—	(1,026)	(100)%	(1,026)	—	(1,026)	(100)%
Interest income and other	12	119	(107)	(90)%	(66)	72	(138)	(192)%
Total other income (expense), net	$(1,975)	$(1,116)	$(859)	77%	$(4,449)	$(3,457)	$(992)	29%
% of Revenue	(4)%	(4)%			(3)%	(4)%		

The increase in other expense, net for the three and nine months ended September 30, 2016 compared to the same periods of 2015 was primarily due to a $1.0 million loss on extinguishment of debt recorded in connection with the repayment of amounts due under the 2013 Loan and Security Agreement and the 2014 Loan and Security Agreement. The loss was comprised of $0.4 million in prepayment penalties, a $0.4 million write-off of unamortized debt discounts, and a $0.2 million write-off of unamortized debt issuance costs. This increase was partially offset by

Table of Contents

lower interest expense related to lower interest rates under the 2016 Loan and Security Agreement compared to the 2014 Loan and Security Agreement and the 2013 Loan and Security Agreement.

Liquidity and Capital Resources

To date, we have financed our operations primarily through sales of our solution, lease facilities and net proceeds from our equity and debt financings. As of September 30, 2016, we had cash and cash equivalents totaling $57.3 million.

As of September 30, 2016, we had a total of 32.6 million in principal amount outstanding under a revolving credit facility governed by our 2016 Loan and Security Agreement. On August 1, 2016, we entered into the 2016 Loan and Security Agreement with two lenders for the New Revolving Credit Facility of up to $50.0 million. The New Revolving Credit Facility matures in August 1, 2019. Under the terms of the New Revolving Credit Facility, the balance outstanding cannot exceed our trailing four months of MRR (monthly recurring revenue including subscription and usage) multiplied by the average trailing 12 month dollar based retention rate (calculated on the same basis as set forth in Item 2 of this report, see "Annual Dollar-Based Retention Rate"). The New Revolving Credit Facility carries a variable annual interest rate of the prime rate plus 0.50%, subject to a 0.25% increase if our adjusted EBITDA is negative at the end of any fiscal quarter. Upon the effectiveness of the 2016 Loan and Security Agreement, we immediately drew down $32.6 million and terminated the 2013 Loan and Security Agreement and the 2014 Loan and Security Agreement by repaying the aggregate outstanding principal, accrued interest and prepayment penalty balances thereunder of $32.4 million along with $0.2 million in administrative fees.

In addition, as of September 30, 2016, we had a $1.2 million FCC civil penalty payable to the U.S. Treasury and $0.5 million in outstanding principal amount under a promissory note with the USAC (see Note 5 of the notes to condensed consolidated financial statements included in this Form 10-Q).

We believe our existing cash and cash equivalents and the amount available for borrowing under our New Revolving Credit Facility (or any refinancing of the facility) will be sufficient to meet our working capital and capital expenditure needs at least through September 30, 2017. Our future capital requirements will depend on many factors including our growth rate, continuing market acceptance of our solution, client retention, ability to gain new clients, the timing and extent of spending to support development efforts, the expansion of sales and marketing activities and the introduction of new and enhanced offerings. We may also acquire or invest in complementary businesses, technologies and intellectual property rights, which may increase our future capital requirements, both to pay acquisition costs and to support our combined operations. We may raise additional equity or debt financing at any time. We may not be able to raise additional equity or debt financing on terms acceptable to us or at all. If we are unable to raise additional capital when desired or required, our business, operating results, and financial condition would be harmed. In addition, if our operating performance during the next twelve months is below our expectations, our liquidity and ability to operate our business could be harmed.

If we raise additional funds by issuing equity or equity-linked securities, the ownership of our existing stockholders will be diluted. If we raise additional funds through the incurrence of additional indebtedness, we will be subject to increased debt service obligations and could also be subject to new or additional restrictive covenants and other operating restrictions that could harm our ability to conduct our business.

Cash Flows

The following table summarizes our cash flows for the periods presented (in thousands, except percentages):

	Nine Months Ended September 30,		$ Change	% Change
	2016	2015		
Net cash provided by (used in) operating activities	$4,004	$ (12,873)	$16,877	(131)%
Net cash (used in) provided by investing activities	(1,033)	20,117	(21,150)	(105)%
Net cash used in financing activities	(4,122)	(6,032)	1,910	(32)%
Net (decrease) increase in cash and cash equivalents	$(1,151)	$ 1,212	$(2,363)	(195)%

Cash Flows from Operating Activities

Cash provided by or used in operating activities is primarily influenced by our personnel-related expenditures, datacenters and telecommunications carrier costs, office and facility related costs, USF contributions and other

26

Table of Contents

regulatory costs and the amount and timing of client payments. If we continue to improve our financial results, we expect net cash provided by operating activities to increase. Our largest source of operating cash inflows is cash collections from our clients for subscription and related usage services. Payments from clients for these services are typically received monthly.

During the nine months ended September 30, 2016, net cash provided by operating activities was $4.0 million as compared to net cash used by operating activities of $12.9 million for the same period of 2015. The improvement was primarily due to a $12.6 million decrease in net loss after adjusting for non-cash expenses and a $4.3 million favorable change in net cash flows resulting from changes in operating assets and liabilities.

During the nine months ended September 30, 2016, cash inflows from changes in operating assets and liabilities included a $2.4 million increase in deferred revenue primarily attributable to increased billings, a $2.7 million increase in accrued and other liabilities primarily for ESPP withholdings for employees due to timing of ESPP purchase, additional employee paid-time-off liability due to timing, and sales commissions driven by the growth in sales and bookings of our solution, and a $1.0 million increase in accounts payable related to timing of liabilities and payments. Cash outflows from changes in operating assets and liabilities included primarily a $1.9 million increase in prepaid expenses and other current assets primarily related to long-term maintenance contracts and annual subscription fees on third-party licensed technology and insurance policies, and a $2.4 million increase in accounts receivable due to increased sales.

During the nine months ended September 30, 2015, cash outflows from changes in operating assets and liabilities included primarily a $1.3 million decrease in accounts payable related to timing of liabilities and payments, a $1.1 million increase in accounts receivable due to increased sales, and a $1.0 million increase in prepaid expenses and other current assets primarily related to long-term maintenance contracts and annual subscription fees for third-party SaaS services. Cash inflows from changes in operating assets and liabilities was primarily due to a $0.8 million increase in accrued and other liabilities primarily for ESPP withholdings for employees due to the timing of ESPP purchases, for accrued bonus and commission driven by our improved sales and financial performance, and for personnel costs due to increase in employee headcount.

Cash Flows from Investing Activities

Net cash used in investing activities in the nine months ended September 30, 2016 was primarily for purchase of property and equipment.

Net cash provided by investing activities of $20.1 million in the nine months ended September 30, 2015 was primarily from proceeds of $40.0 million from maturity of short-term investments and a $0.8 million decrease in restricted cash due to the release of two letters of credit related to our office lease obligation and an insurance policy, offset in part by purchase of short-term investments of $20.0 million and purchase of property and equipment of $0.7 million.

Cash Flows from Financing Activities

During the nine months ended September 30, 2016, cash used in financing activities of $4.1 million was primarily for repayments of $36.9 million on notes payable and our revolving line of credit as part of our cancellation of the 2013 Loan and Security Agreement and the 2014 Loan and Security Agreement, as well as $4.6 million in payments under our capital lease obligations. Cash outflows were offset in part by cash received from the $32.6 million drawdown under the New Revolving Credit Facility, stock option exercises of $4.1 million and proceeds of $0.8 million from the sale of common stock under our employee stock purchase plan.

During the nine months ended September 30, 2015, cash used in financing activities of $6.0 million was primarily for repayments of $7.1 million on our capital lease and notes payable obligations, offset in part by cash received from stock option exercises of $0.4 million and proceeds of $0.7 million from the sale of common stock under our employee stock purchase plan.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

We believe our critical accounting policies involve the greatest degree of judgment and complexity and have the greatest potential impact on our condensed consolidated financial statements. Our critical accounting policies are disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015. During the nine months ended September 30, 2016, our critical accounting policies did not materially change. Please see Note 1 of Notes to the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Off Balance Sheet Arrangements

As of September 30, 2016, we did not have any off balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K, such as the use of unconsolidated subsidiaries, structured finance, special purpose entities or variable interest entities.

Contractual Obligations

Our principal contractual obligations consist of future payment obligations under debt, capital leases to finance data centers and other computer and networking equipment, operating leases for office space, research and development, and sales and marketing facilities, and agreements with third parties to provide co-location hosting, telecommunication usage and equipment maintenance services. These commitments as of December 31, 2015 are disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015, and did not change during the nine months ended September 30, 2016 except for the acquisition of certain additional data center and network equipment and software under multiple capital leases. As of September 30, 2016, total minimum future payment commitments under these capital leases added during the nine months ended September 30, 2016 were approximately $6.2 million, of which $0.6 million is due in 2016, with the remainder due over approximately 35 months thereafter. In August 2016, we also entered into the New Revolving Credit Facility under the 2016 Loan and Security Agreement and canceled the 2013 Loan and Security Agreement and 2014 Loan and Security Agreement. See “Liquidity and Capital Resources.”

Table of Contents

ITEM 3. Quantitative and Qualitative Disclosure about Market Risk

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

Interest Rate Sensitivity

As of September 30, 2016, we had cash and cash equivalents of $57.3 million that were held primarily in cash or money-market funds. We hold our cash and cash equivalents for working capital purposes. Declines in interest rates would reduce future interest income. For the three and nine months ended September 30, 2016, the effect of a hypothetical 10% increase or decrease in overall interest rates would not have had a material impact on our interest income. The carrying amount of our cash equivalents reasonably approximates fair value. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of our money-market funds, we believe that we do not have any material exposure to changes in the fair value of our cash equivalents as a result of changes in interest rates.

As of September 30, 2016, we had a total of $32.6 million in outstanding borrowings under our variable interest rate debt or financing agreements. See Note 5 of the notes to condensed consolidated financial statements of this Form 10-Q for a detailed discussion of our indebtedness. For each of the three and nine months ended September 30, 2016, a hypothetical 10% increase in the interest rates under these agreements would have increased our interest expense by approximately $33 thousand and $0.2 million, respectively.

Foreign Currency Risk

The functional currency of our foreign subsidiaries is the U.S. dollar. Substantially all of our sales are denominated in U.S. dollars, and therefore our revenue is not currently subject to material direct foreign currency risk. However, if the U.S. dollar strengthens relative to other currencies, such strengthening could have an indirect effect on our sales to the extent it raises the cost of our solution to non-U.S. clients and thereby could reduce demand. A weaker U.S. dollar could have the opposite effect. The precise indirect effect of currency fluctuations is difficult to measure or predict because our sales are influenced by many factors in addition to the impact of such currency fluctuations.

Our operating expenses are primarily denominated in the currencies of the countries in which our operations are located, which are primarily the U.S., the Philippines, Russia, and the U.K. Our consolidated results of operations and cash flows are, therefore, subject to fluctuations due to changes in foreign currency exchange rates and may be adversely affected in the future due to changes in foreign currency exchange rates. To date, we have not entered into any hedging arrangements with respect to foreign currency risk or other derivative financial instruments. During the three and nine months ended September 30, 2016, the effect of a hypothetical 10% change in foreign currency exchange rates applicable to our business would have had a maximum impact of approximately $0.2 million and $0.6 million, respectively, on our operating results.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of September 30, 2016.

Based on management’s evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2016, our disclosure controls and procedures were designed, and were effective, to provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms, and that such information is accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosures.

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures

28

Table of Contents

must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Changes in Internal Control over Financial Reporting

During the three months ended September 30, 2016, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

We are subject to certain legal and regulatory proceedings described below, and from time to time may be involved in a variety of claims, lawsuits, investigations and proceedings relating to contractual disputes, intellectual property rights, employment matters, regulatory compliance matters and other litigation matters.

Melcher Litigation

On September 28, 2016, a complaint was filed in the United States District Court for the Southern District of California against Five9, Inc. ("Five9"), as the successor in interest to Face It, Corp. ("Face It"), and Lance Fried, a former Five9 employee who was the former Chief Executive Officer of Face It. The action, captioned Melcher, et al. v. Five9, Inc., et al., No. 16-cv-02440, was filed as a direct action by Carl Melcher, a purported former stockholder of Face It, and his related investment entity.

In the complaint, the plaintiffs allege that Face It repurchased the plaintiffs' stock in September 2013 before Five9 acquired Face It, and that in connection with the repurchase, Fried made material misstatements or omissions to Melcher, by failing to disclose that Face It allegedly was in concurrent discussions about a potential sale of the company to Five9. The complaint alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, as well as various claims under state law and common law. The complaint seeks to set aside Face It's September 2013 stock repurchase from the plaintiffs, as well as an unspecified amount of damages and an award of attorney's fees and costs, in addition to other relief.

The outcome of litigation and regulatory claims cannot be predicted with certainty, may be expensive and cause distraction to our management, even if we are ultimately successful, and could harm our future results of operations, cash flows and financial condition.

NobelBiz Litigation

On August 5, 2011, NobelBiz sent a letter to us asserting infringement of a patent related to virtual call centers. On April 3, 2012, NobelBiz filed a patent infringement lawsuit against us in the United States District Court for the Eastern District of Texas. The patent asserted in the complaint is different, but related, to the patent asserted in the original letter. The lawsuit, NobelBiz Inc. v. Five9, Inc., Case No. 6:12-cv-00243-LED, alleges that our local caller ID management service infringes United States Patent No. 8,135,122, or the '122 patent. The '122 patent, titled "System and Method for Modifying Communication Information (MCI)," issued on March 13, 2012, and according to the complaint is alleged to relate to "a system for processing a telephone call from a call originator (also referred to as a calling party) to a call target (also referred to as a receiving party), where the system accesses a database storing outgoing telephone numbers, selects a replacement telephone number from the outgoing telephone numbers based on the telephone number of the call target, and originates an outbound call to the call target with a modified outgoing caller identification ('caller ID')." NobelBiz seeks damages in the form of lost profits as well as injunctive relief. The lawsuit is one of several lawsuits filed by NobelBiz against various companies including TCN Inc., LiveVox, Inc. and Global Connect LLC. On March 28, 2013, the court granted our motion to transfer the case to the United States District Court for the Northern District of California. Subsequently, NobelBiz amended its complaint to add claims related to U.S. Patent No. 8,565,399, or the '399 patent, which is a continuation in the same family as the '122 patent and addresses the same technology. We responded to the complaint and amended complaint by asserting noninfringement and invalidity of the '122 and '399 patents. On January 16, 2015, the court issued an order regarding claim construction of the two patents-in-suit. On March 7, 2016, the court stayed the case pending an appeal in lawsuits involving NobelBiz, Global Connect and TCN that also involve the '122 and '399 patents. The appeal for those cases is likely to last until late 2016 or into 2017, after which time the lawsuit between NobelBiz and Five9 will resume and a new schedule will be entered by the Court.

The outcome of litigation and regulatory claims cannot be predicted with certainty, may be expensive and cause distraction to our management, even if we are ultimately successful, and could harm our future results of operations, cash flows and financial condition.

ITEM 1A. Risk Factors

Our operations and financial results are subject to various risks and uncertainties. You should consider carefully the risks and uncertainties described below, together with all of the other information in this report. If any

30

Table of Contents

of the following risks or other risks actually occur, our business, financial condition, results of operations, and future prospects could be materially harmed, and the price of our common stock could decline.

The following description of the risk factors associated with our business includes any material changes to and supersedes the description of the risk factors associated with our business previously disclosed in Part II, Item 1A of our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2016.

Risks Related to Our Business and Industry

Our quarterly and annual results may fluctuate significantly, may not fully reflect the underlying performance of our business and may result in decreases in the price of our common stock.

Our quarterly and annual results of operations, including our revenues, profitability and cash flow have varied, and may vary significantly in the future, and period-to-period comparisons of our operating results may not be meaningful. Accordingly, the results of any one quarter or period should not be relied upon as an indication of future performance. Our quarterly and annual financial results may fluctuate as a result of a variety of factors, many of which are outside our control and, as a result, may not fully reflect the underlying performance of our business. Fluctuation in quarterly and annual results may harm the value of our common stock. Factors that may cause fluctuations in our quarterly and annual results include, without limitation:

- market acceptance of our solution;
- our ability to attract new clients and grow our business with existing clients;
- client renewal rates;
- our ability to adequately expand our sales force
- changes in strategic and client relationships;
- the amount and timing of costs and expenses related to the maintenance and expansion of our business, operations and infrastructure;
- the timing and success of new product and feature introductions by us or our competitors or any other change in the competitive dynamics of our industry, including consolidation among competitors, clients or strategic partners;
- network outages or security breaches, which may result in the loss of clients, client credits and harm to our reputation;
- seasonal factors that may cause our revenues in the first half of a year to be relatively lower than our revenues in the second half of a year;
- inaccessibility or failure of our cloud contact center software due to failures in the products or services provided by third parties;
- the timing of recognition of revenues;
- increases or decreases in the elements of our solution or pricing changes upon any renewals of client agreements;
- changes in our pricing policies or those of our competitors;
- the level of professional services and support we provide our clients;
- the components of our revenue;
- the addition or loss of key clients, including through acquisitions or consolidations;
- general economic, industry and market conditions;
- the timing of costs and expenses related to the development or acquisition of technologies or businesses and potential future charges for impairment of goodwill from acquired companies;
- compliance with, or changes in, the current and future regulatory environment;
- the hiring, training and retention of key employees;
- litigation or other claims against us;
- our ability to obtain additional financing; and
- advances and trends in new technologies and industry standards.

Table of Contents

If we are unable to attract new clients or sell additional services and functionality to our existing clients, our revenue and revenue growth will be harmed.

To increase our revenue, we must add new clients, add additional agent seats and sell additional functionality to existing clients, and encourage existing clients to renew their subscriptions on terms favorable to us. As our industry matures, as our clients experience seasonal trends in their business, or as competitors introduce lower cost and/or differentiated products or services that are perceived to compete favorably with ours, our ability to add new clients and renew, maintain or upsell existing clients based on pricing, cost of ownership, technology and functionality could be impaired. As a result, we may be unable to renew our agreements with existing clients, attract new clients or grow or maintain our business with existing clients, which could harm our revenue and growth.

Furthermore, a portion of our revenue is generated by acquiring domestic and international telecommunications minutes from wholesale telecommunication service providers and reselling those minutes to our clients. As a result, we must resell more minutes if telecommunications rates decrease to maintain our level of usage revenue.

Our recent rapid growth may not be indicative of our future growth, and if we continue to grow rapidly, we may fail to manage our growth effectively.

For the three months ended September 30, 2016, our revenue was $41.0 million, which increased by $8.7 million, or 27%, from $32.3 million for the same period of 2015. For the nine months ended September 30, 2016, our revenue was $117.9 million, which increased by $25.0 million, or 27%, from $92.8 million for the same period of 2015. For the years ended December 31, 2015, 2014 and 2013, our revenue was $128.9 million, $103.1 million and $84.1 million, respectively, representing year-over-year growth of 25% and 23%, respectively. In the future, as our revenue increases, our annual revenue growth rate may decline. We believe growth of our revenue depends on a number of factors, including our ability to:

- compete with other vendors of cloud-based enterprise contact center systems to capture market share from providers of legacy on-premise systems;
- increase our existing clients' use of our solution and further develop our partner ecosystem;
- strengthen and improve our solution through significant investments in research and development and the introduction of new and enhanced solutions
- introduce our solution to new markets outside the United States and increase global awareness of our brand; and
- selectively pursue acquisitions.

If we are not successful in achieving these objectives, our revenue may be harmed. In addition, we plan to continue to invest in future growth, including expending substantial financial and other resources on:

- sales and marketing, including a significant expansion of our sales and professional services organization;
- our technology infrastructure, including systems architecture, management tools, scalability, availability, performance and security, as well as disaster recovery measures;
- solution development, including investments in our solution development team and the development of new solutions, as well as new applications and features for existing solutions;
- international expansion; and
- general administration, including legal, regulatory compliance and accounting expenses.

Moreover, we continue to expand our headcount and operations. We grew from 630 employees as of December 31, 2014 to 739 employees as of September 30, 2016. We anticipate that we will continue to expand our operations and headcount in the near term. This growth has placed, and future growth will place, a significant strain on our management, administrative, operational and financial resources and infrastructure. Our success will depend in part on our ability to manage this growth effectively. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. Failure to effectively manage growth could result in difficulty or delays in adding new clients, declines in quality or client satisfaction, increases in costs, system failures, difficulties in introducing new features or solutions, the need for more capital than we anticipate or other operational difficulties, and any of these difficulties could harm our business performance and results of operations.

The expected addition of new employees and the capital investments that we anticipate will be necessary to manage our anticipated growth will make it more difficult for us to generate earnings or offset any future revenue

32

Table of Contents

shortfalls by reducing costs and expenses in the short term. If we fail to manage our anticipated growth, we will be unable to execute our business plan successfully.

Failure to adequately expand our sales force will impede our growth.

We will need to continue to expand and optimize our sales infrastructure in order to grow our client base and business. We plan to continue to aggressively expand our sales force, both domestically and internationally. Identifying and recruiting qualified personnel and training them in the use and sale of our solution requires significant time, expense and attention. It can take several months before our sales representatives are fully trained and productive. Our business may be harmed if our efforts to expand and train our sales force do not generate a corresponding increase in revenues. In particular, if we are unable to hire, develop and retain talented sales personnel or if new sales personnel are unable to achieve desired productivity levels in a reasonable period of time, we may not be able to realize the expected benefits of this investment or increase our revenues.

The markets in which we participate are highly competitive, and if we do not compete effectively, our operating results could be harmed.

The market for contact center solutions is highly competitive. Generally, we do not have long-term contracts with our clients and our clients can terminate our service and switch to competitors' offerings on short notice.

We currently compete with large legacy technology vendors that offer on-premise enterprise telephony and contact center systems, such as Avaya and Cisco, and legacy on-premise software companies that come from a computer-telephony integration ("CTI") heritage, such as Aspect, Genesys, and Interactive Intelligence (which recently announced it was being acquired by Genesys). These companies are supplementing their traditional on-premise contact center systems with cloud offerings, either through acquisition or in-house development. Additionally, we compete with vendors that historically provided other contact center services and technologies and expanded to offer cloud contact center software. These companies include inContact (which has announced it was being acquired by NICE Ltd.) and LiveOps. We also face competition from smaller contact center service providers with specialized contact center software offerings. Our actual and potential competitors may enjoy competitive advantages over us, including greater name recognition, longer operating histories and larger marketing budgets, as well as greater financial or technical resources. With the introduction of new technologies and market entrants, we expect competition to intensify in the future.

Some of our competitors can devote significantly greater resources than we can to the development, promotion and sale of their products and services and many have the ability to initiate or withstand substantial price competition. Current or potential competitors may also be acquired by third parties with significantly greater resources, such as NICE Ltd.'s acquisition of inContact and Genesys' acquisition of Interactive Intelligence. In addition, many of our competitors have stronger name recognition, longer operating histories, established relationships with clients, more comprehensive product offerings, larger installed bases and major distribution agreements with consultants, system integrators and resellers. Our competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their product offerings or resources and ability to compete. If our competitors' products, services or technologies become more accepted than our solution, if they are successful in bringing their products or services to market earlier than ours, or if their products or services are less expensive or more technologically capable than ours, our revenues could be harmed. Pricing pressures and increased competition could result in reduced sales and revenues, reduced margins and loss of, or a failure to maintain or improve, our competitive market position, any of which could harm our business.

If we fail to manage our technical operations infrastructure, our existing clients may experience service outages, our new clients may experience delays in the deployment of our solution and we could be subject to, among other things, claims for credits or damages.

Our success depends in large part upon the capacity, stability and performance of our operations infrastructure. From time to time, we have experienced interruptions in service, and may experience such interruptions in the future. These service interruptions may be caused by a variety of factors, including infrastructure changes, human or software errors, viruses, security attacks, fraud, spikes in client usage and denial of service issues. In some instances, we may not be able to identify the cause or causes of these performance problems within an acceptable period of time. Our failure to achieve or maintain expected performance levels, stability and security could harm our relationships with

our clients, result in claims for credits or damages, damage our reputation and significantly reduce client demand for our solution and harm our business.

Any future service interruptions could:

Table of Contents

- cause our clients to seek credits or damages for losses incurred;
- cause existing clients to cancel or elect not to renew their contracts;
- affect our reputation as a reliable service provider;
- make it more difficult for us to attract new clients or expand our business with existing clients; or
- require us to replace existing equipment.

We have experienced significant growth in the number of agents and interactions that our infrastructure supports. As the number of agent seats within our client base grows and our clients' use of our service increases, we will be required to make additional investments in our capacity to maintain adequate stability and performance, the availability of which may be limited or the cost of which may be prohibitive. In addition, we need to properly manage our operations infrastructure in order to support version control, changes in hardware and software parameters and the evolution of our solution. If we do not accurately predict or improve our infrastructure requirements to keep pace with growth in our business, our business could be harmed.

If our existing clients terminate their subscriptions or reduce their subscriptions and related usage, our revenues and gross margins will be harmed and we will be required to spend more money to grow our client base.

We expect to continue to derive a significant portion of our revenues from existing clients. As a result, retaining our existing clients is critical to our future operating results. We offer monthly, annual and multiple-year contracts to our clients, with 30 days’ notice generally required for changes in the number of agent seats or termination of their contracts. Subscriptions and related usage by our existing clients may decrease if:

- clients are not satisfied with our services, prices or the functionality of our solution;
- the stability, performance and security of our hosting infrastructure and hosting services are not satisfactory;
- our clients’ business declines due to industry cycles, seasonality, business difficulties or other reasons;
- competition increases from other contact center providers;
- alternative technologies, products or features emerge that we do not provide;
- our clients or potential clients experience financial difficulties;
- the volume of minutes for inbound and outbound interactions between our clients and their customers decreases; or
- the U.S. or global economy declines.

If our existing clients’ subscriptions and related usage decrease or are terminated, we will need to spend more money to acquire new clients to maintain our existing level of revenues. We incur significant costs and expenses, including sales and marketing expenses, to acquire new clients, and those costs and expenses are an important factor in determining our net profitability. There can be no assurance that our efforts to acquire new clients will be successful.

The loss of one or more of our key clients, or a failure to renew our subscription agreements with one or more of our key clients, could harm our ability to market our solution.

We rely on our reputation and recommendations from key clients in order to market and sell our solution. The loss of any of our key clients, or a failure of some of them to renew or to continue to recommend our solution, could have a significant impact on our revenues, reputation and our ability to obtain new clients. In addition, acquisitions of our clients could lead to cancellation of our contracts with those clients, thereby reducing the number of our existing and potential clients.

Our growth depends in part on the success of our strategic relationships with third parties and our failure to successfully grow and manage these relationships could harm our business.

We leverage strategic relationships with third parties, such as CRM providers, Workforce Optimization, or WFO, providers, other technology providers, system integrators, and telephony providers. For example, our CRM and system integrator relationships provide significant lead generation for new client opportunities. As we grow our business, we will continue to depend on both existing and new strategic relationships. Our competitors may be more successful than we are in establishing or expanding relationships with third parties or may provide incentives to third parties to favor their products over our solution. These strategic partners may cease to recommend our solution to prospective clients due to actual or perceived lack of features, technological issues or failures, reputational concerns, economic incentives, or other factors, which would harm our business, financial conditions and operations.

34

Table of Contents

Furthermore, there has and continues to be a significant amount of consolidation in our industry and adjacent industries, if our partners are acquired, fail to work effectively with us or go out of business, they may no longer support or promote our solution, or may be less effective in doing so, which could harm our business, financial condition and operations. If we are unsuccessful in establishing or maintaining our strategic relationships with third parties, or these partners fail to recommend our solution, our ability to compete in the marketplace or to grow our revenues could be impaired and our operating results may suffer. Even if we are successful, we cannot assure you that these relationships will result in increased client usage of our solution or increased revenue.

In addition, identifying new partners, and negotiating and documenting relationships with them, requires significant time and resources. As the complexity of our solution and our third-party relationships increases, the management of those relationships and the negotiation of contractual terms sufficient to protect our rights and limit our potential liabilities will become more complicated. We also license technology from certain third-party partners, including through OEM relationships. Certain of these agreements permit either party to terminate all or a portion of the relationship without cause at any time and for any reason. If one of these agreements is terminated by the other party, we would have to find an alternative source or develop new technology ourselves, either of which could cause delays in our ability to offer our solution or certain product features to our clients, result in increased expense and harm our business. Our inability to successfully manage and maintain these complex relationships or negotiate sufficient contractual terms could harm our business.

Our clients may fail to comply with the terms of their agreements, necessitating action by us to collect payment, or may terminate their subscriptions for our solution.

If clients fail to pay us under the terms of our agreements or fail to comply with the terms of our agreements, including compliance with regulatory requirements, we may terminate clients, lose revenue, be unable to collect amounts due to us, be subject to legal or regulatory action and incur costs in enforcing the terms of our contracts, including litigation. Some of our clients may seek bankruptcy protection or other similar relief and fail to pay amounts due to us, seek reimbursement for amounts already paid, or pay those amounts more slowly, either of which could harm our operating results, financial position and cash flow.

We sell our solution to larger organizations that require longer sales and implementation cycles and often demand more configuration and integration services or customized features and functions that we may not offer, any of which could delay or prevent these sales and harm our growth rates, business and operating results.

As we continue to target our sales efforts at larger organizations, we face greater costs, longer sales and implementation cycles and less predictability in completing our sales. These larger organizations typically require more configuration and integration services, which increases our upfront investment in sales and deployment efforts, with no guarantee that these clients will subscribe to our solution or increase the scope of their subscription. Furthermore, with larger organizations, we must provide greater levels of education regarding the use and benefits of our solution to a broader group of people. As a result of these factors, we must devote a significant amount of sales support and professional services resources to individual clients and prospective clients, thereby increasing the cost and time required to complete sales. Our typical sales cycle for larger organizations is four to five months, but can be significantly longer, and we expect that our average sales cycle may increase as sales to larger organizations continue to grow as a percentage of our business. Longer sales cycles could cause our operating and financial results to be less predictable and to fluctuate from period to period. In addition, many of our clients that are larger organizations initially deploy our solution to support only a portion of their contact center agents. Our success depends on our ability to increase the number of agent seats and the number of applications utilized by larger organizations over time. There is no guarantee that these clients will increase their subscriptions for our solution. If we do not expand our initial relationships with larger organizations, the return on our investments in sales and deployment efforts for these clients will decrease and our business may suffer.

Furthermore, we may not be able to provide the configuration and integration services that larger organizations typically require. For example, our solution does not currently permit clients to modify our software code, but instead requires them to use our set of application programming interfaces, or APIs. If prospective clients require customized features or functions that we do not offer, and that would be difficult for them to deploy themselves, they will need to use our services or third-party service providers or we may lose sales opportunities with larger organizations and our

business could suffer.

Table of Contents

Because a significant percentage of our revenue is derived from existing clients, downturns or upturns in new sales will not be immediately reflected in our operating results and may be difficult to discern.

We generally recognize subscription revenue from clients monthly as services are delivered. As a result, a significant percentage of the subscription revenue we report in each quarter is derived from existing clients. Consequently, a decline in new subscriptions in any single quarter will likely have only a small impact on our revenue results for that quarter. However, the cumulative impact of such declines could harm our revenues in future quarters. Accordingly, the effect of significant downturns in sales and market acceptance of our solution, and potential changes in our pricing policies or renewal rates, will typically not be reflected in our results of operations until future periods. We also may be unable to adjust our cost structure to reflect the changes in revenue, resulting in lower margins and earnings. In addition, our subscription model makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new clients will be recognized over time as services are delivered. For example, many of our clients initially deploy our solution to support only a portion of their contact center agents. Any increase to our revenue and the value of these existing client relationships will only be reflected in our results of operations if and when these clients increase the number of agent seats and the number of components of our solution over time.

We rely on third-party telecommunications and internet service providers to provide our clients and their customers with telecommunication services and connectivity to our cloud contact center software and any failure by these service providers to provide reliable services could subject us to, among other things, claims for credits or damages.

We rely on third-party telecommunication service providers to provide our clients and their customers with telecommunication services. These telephony services include the public switched telephone network, or PSTN, telephone numbers, call termination and origination services, and local number portability for our clients. In addition, we depend on our internet bandwidth suppliers to provide uninterrupted and error-free service through their telecommunications networks. We exercise little control over these third-party providers, which increases our vulnerability to problems with the services they provide. If any of these service providers fail to provide reliable services, or terminate or increase the cost of the services that we and our clients depend on, we may be required to switch to another service provider. Delays caused by switching our technology to another service provider, if available, and qualifying this new service provider could materially harm our client relationships, business, financial condition and operating results.

Due to our reliance on these service providers, when problems occur, it may be difficult to identify the source of the problem. Service disruption or outages, whether caused by our service, the products or services of our third-party service providers, or our clients' or their customers' equipment and systems, may result in loss of market acceptance of our solution and any necessary repairs or other remedial actions may force us to incur significant costs and expenses. Any failure on the part of third-party service providers to achieve or maintain expected performance levels, stability and security could harm our relationships with our clients, result in claims for credits or damages, damage our reputation, significantly reduce client demand for our solution and seriously harm our financial condition and operating results.

We have a history of losses and we may be unable to achieve or sustain profitability.

We have incurred significant losses in each period since our inception in 2001. We incurred net losses of $3.9 million and $12.3 million in the three and nine months ended September 30, 2016, respectively, and a net loss of $25.8 million in the year ended December 31, 2015. As of September 30, 2016, we had an accumulated deficit of $166.7 million. These losses and our accumulated deficit reflect the substantial investments we have made to develop our solution and acquire new clients. We expect the dollar amount of our costs and expenses to increase in the future as revenue increases, although at a slower rate. We expect our losses to continue for the foreseeable future as we continue to develop and expand our business. Furthermore, to the extent we are successful in increasing our client base, we may also incur increased losses because costs associated with acquiring clients are generally incurred up front, while revenues are recognized over the course of the client relationship. We also have negative gross margins on our professional services, which are expected to continue in the future. In addition, as a public company, we incur significant legal, accounting and other expenses. You should not consider our historical or recent growth in revenues as necessarily indicative of our future performance. Accordingly, we cannot assure you that we will achieve profitability in the future nor that, if we do become profitable, we will sustain profitability.

36

Table of Contents

If the market for cloud contact center software solutions develops more slowly than we expect or declines, our business could be harmed.

The cloud contact center software market is not as mature as the market for legacy on-premise contact center systems, and it is uncertain whether cloud contact center solutions will achieve and sustain high levels of client demand and market acceptance. Our success will depend to a substantial extent on the widespread adoption of cloud contact center software solutions as a replacement for legacy on-premise systems. Many larger organizations have invested substantial technical, personnel and financial resources to integrate legacy on-premise contact center systems into their businesses and, therefore, may be reluctant or unwilling to migrate to cloud contact center solutions such as ours. It is difficult to predict client adoption rates and demand for our solution, the future growth rate and size of the cloud contact center software market, or the entry of competitive products and services. The expansion of the cloud contact center software market depends on a number of factors, including the refresh rate for legacy on-premise systems, cost, performance and perceived value associated with cloud contact center software solutions, as well as the ability of providers of cloud contact center software solutions to address security, stability and privacy concerns. If we or other cloud contact center solution providers experience security incidents, loss of client data, disruptions in service or other problems, the market for cloud contact center software products, solutions and services as a whole, including our solution, may be harmed. If cloud contact center software solutions do not achieve widespread adoption, or there is a reduction in demand for such solutions caused by a lack of client acceptance, enhanced product offerings from on-premise providers, technological challenges, weakening economic conditions, security or privacy concerns, competing technologies and products, decreases in corporate spending or otherwise, it could result in decreased revenues and our business could be harmed.

Shifts over time or from quarter-to-quarter in the mix of sizes or types of organizations that purchase our solution or changes in the components of our solution purchased by our clients could affect our gross margins and operating results.

Our strategy is to sell our solution to both smaller and larger organizations. Our gross margins can vary depending on numerous factors related to the implementation and use of our solution, including the features and number of agent seats purchased by our clients and the level of usage and professional services and support required by our clients. For example, our larger clients typically require more professional services and because our professional services offerings typically have negative margins, any increase in sales of professional services could harm our gross margins and operating results. We also have lower margins on our usage revenues. Sales to larger organizations may also entail longer sales cycles and more significant selling efforts. Selling to smaller clients may involve smaller contract sizes, fewer upsell opportunities, a higher likelihood of contract terminations, fewer potential agent seats and greater credit risk and uncertainty. If the mix of organizations that purchase our solution, or the mix of solution components purchased by our clients, changes unfavorably, our revenues and gross margins could decrease and our operating results could be harmed.

We depend on data centers operated by third parties and any disruption in the operation of these facilities could harm our business.

We host our solution at data centers located in Santa Clara, California; Atlanta, Georgia; Slough, England and Amsterdam, The Netherlands. Any failure or downtime in one of our data center facilities could affect a significant percentage of our clients. While we control and have access to our servers and all of the components of our network that are located in our external data centers, we do not control the operation of these facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, or if one of our data center operators is acquired, closes, suffers financial difficulty or is unable to meet our growing capacity needs, we may be required to transfer our servers and other infrastructure to new data center facilities, and we may incur significant costs and service interruptions in connection with doing so.

Our data centers are subject to various points of failure. Problems with cooling equipment, generators, uninterruptible power supply, routers, switches, or other equipment, whether or not within our control, could result in service interruptions for our clients as well as equipment damage. Our data centers are subject to disasters such as earthquakes, floods, fires, hurricanes, acts of terrorism, sabotage, break-ins, acts of vandalism and other events, which

could cause service interruptions or the operators of these data centers to close their facilities for an extended period of time or permanently. The destruction or impairment of any of our data center facilities could result in significant downtime for our solution and the loss of client data. Because our ability to attract and retain clients depends on our providing clients with highly reliable service, even minor interruptions in our service could harm our business, revenues and reputation. Additionally, in connection with the continuing expansion of our existing data

Table of Contents

center facilities, there is an increased risk that service interruptions may occur as a result of server addition, relocation or other issues.

Our data centers are also subject to increased power costs. We may not be able to pass on any increase in power costs to our clients, which could reduce our operating margins.

Our recent growth makes it difficult to evaluate and predict our current business and future prospects.

While we have been in existence since 2001, much of our growth has occurred in recent years. Our recent growth may make it difficult for investors to evaluate our current business and our future prospects. We have encountered and will continue to encounter risks and difficulties frequently experienced by growing companies in rapidly changing industries, including increasing and unforeseen expenses as we continue to grow our business.

Our ability to forecast our future operating results is limited and subject to a number of uncertainties, including our ability to predict revenue levels, and plan for and model future growth. We have encountered and will continue to encounter risks and uncertainties frequently experienced by growing companies in rapidly changing industries, such as the risks and uncertainties described in this report. If our assumptions regarding these risks and uncertainties, which we use to plan our business, are incorrect or change due to adjustments in our markets or our competitors and their product offerings, or if we do not address these risks successfully, our operating and financial results could differ materially from our expectations and our business could suffer.

If our solution fails, or is perceived to fail, to perform properly or if it contains technical defects, our reputation could be harmed, our market share may decline and we could be subject to product liability claims.

Our solution may contain undetected errors or defects that may result in failures or otherwise cause our solution to fail to perform in accordance with client expectations. Moreover, our clients could incorrectly implement or inadvertently misuse our products, which could result in client dissatisfaction and harm the perceived utility of our products and brand. Because our clients use our solution for mission-critical aspects of their business, any real or perceived errors or defects in, or other performance problems with, our solution may damage our clients' businesses and could significantly harm our reputation. If that occurs, we could lose future sales, or our existing clients could elect to cancel or not renew our solution, seek payment credits, seek damages against us, or delay or withhold payment to us, which could result in reduced revenues, an increase in our provision for uncollectible accounts and service credits, an increase in collection cycles for accounts receivable, and harm our financial results. Clients also may make indemnification or warranty claims against us, which could result in significant expense and risk of litigation. Product performance problems could result in loss of market share, failure to achieve market acceptance and the diversion of development resources.

Any product liability, intellectual property, warranty or other claims against us could damage our reputation and relationships with our clients, and could require us to spend significant time and money in litigation or pay significant settlements or damages. Although we maintain general liability insurance, including coverage for errors and omissions, this coverage may not be sufficient to cover liabilities resulting from such claims. Also, our insurers may disclaim coverage. Our liability insurance also may not continue to be available to us on reasonable terms, in sufficient amounts, or at all. Any contract or product liability claims successfully brought against us would harm our business. In addition, since telecommunications billing is inherently complex and requires highly sophisticated information systems to administer, our billing system may experience errors or we may improperly operate the system, which could result in the system incorrectly calculating the fees owed by our clients for our services or related taxes and administrative fees.

Security breaches and improper access to or disclosure of our data or our clients' data, or other cyber attacks on our systems, could result in litigation and regulatory risk, harm our reputation and adversely affect our business.

Our solution involves the storage and transmission of our clients' information, including information about our clients' customers or other information treated by our clients as confidential. Unauthorized access, security breaches or other cyber attacks could result in the loss of confidentiality, integrity and availability of information, or unauthorized use of our systems, leading to litigation, indemnity obligations, increased expenses, and other liability. Such incidents could also cause interruptions to the solution we provide, degrade the user experience, or cause users to lose confidence in our solution. While we have security measures in place to protect client information and minimize the probability of security breaches and other cyber attacks, if these measures fail as a result of a cyber-attack, other third-party action,

employee error, malfeasance or otherwise, and someone obtains unauthorized access to our clients' data, our reputation could be damaged, our business may suffer and we could incur significant liability. Because the techniques used to obtain unauthorized access or sabotage systems change frequently and

Table of Contents

generally are not identified until they are launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, third parties may attempt to fraudulently induce employees or users to disclose information in order to gain access to our data or our users' data. Moreover, any failure on the part of third parties, including our clients, to achieve or maintain security measures for their own systems could harm our relationships with our clients, result in claims against us for credits or damages, damage our reputation and significantly reduce client demand for our solution. Any or all of these issues could harm our ability to attract new clients, cause existing clients to cancel, reduce or not renew their subscriptions, result in reputational damage or subject us to third-party lawsuits, regulatory fines or other action or liability, including orders or consent decrees forcing us to modify our business practices, all of which could have a material and adverse effect on our business, reputation or financial results.

We are subject to many hazards and operational risks that can disrupt our business, some of which may not be insured or fully covered by insurance.

Our operations are subject to many hazards inherent in the cloud contact center software business, including:

- damage to third-party and our infrastructure and data centers, related equipment and surrounding properties caused by earthquakes, hurricanes, tornadoes, floods, fires and other natural disasters, explosions and acts of terrorism;
- security breaches;
- inadvertent damage from third parties; and
- other hazards that could also result in suspension of operations, personal injury and even loss of life.

These risks could result in substantial losses and the curtailment or suspension of our operations. For example, in the event of a major earthquake along the West Coast of the United States (where our corporate headquarters and one of our data centers are located), hurricane or tropical storm in the southeastern United States (where our other U.S. data center is located) or catastrophic events such as fire, power loss, telecommunications failure, cyber-attack, war or terrorist attack, we may be unable to continue our operations and may endure system and service interruptions, reputational harm, delays in product development, breaches of data security and loss of critical data, any of which could harm our business and operating results.

We are not insured against all claims, events or accidents that might occur. If a significant accident or event occurs that is not fully insured, if we fail to recover all anticipated insurance proceeds for significant accidents or events for which we are insured, or if we or our data center providers fail to reopen facilities damaged by such accidents or events, our operations and financial condition could be harmed. In addition to being denied coverage under existing insurance policies, we may not be able to maintain or obtain insurance of the type and amount we desire at reasonable rates.

The contact center software solutions market is subject to rapid technological change, and we must develop and sell incremental and new products in order to maintain and grow our business.

The contact center software solutions market is characterized by rapid changes in client requirements, frequent introductions of new and enhanced products and continuing and rapid technological advancement. To compete successfully, we must continue to design, develop, manufacture and sell new and enhanced contact center products, applications and features that provide increasingly higher capabilities, performance and stability at lower cost. If we are unable to develop or acquire new features for our existing solution or new applications that achieve market acceptance or that keep pace with technological developments, our business would be harmed. For example, we are focused on enhancing the reliability, features and functionality of our contact center solution to enhance its utility to our clients, particularly larger clients with complex, dynamic and global operations. The success of these enhancements depends on many factors, including timely development, introduction and market acceptance, as well as our ability to transition our existing clients to these new products, applications and features. Failure in this regard may significantly impair our revenue growth. In addition, because our solution is designed to operate on a variety of systems, we will need to continuously modify and enhance our solution to keep pace with changes in hardware, operating systems, the increasing trend toward multi-channel communications and other changes to software technologies. We may not be successful in developing or acquiring these modifications and enhancements or bringing them to market in a timely fashion. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could delay introduction of our solution and

increase our research and development expenses. Any failure of our solution to operate effectively with future network platforms and technologies could reduce the demand for our solution, result in client dissatisfaction and harm our business.

Table of Contents

Our ability to continue to enhance our solution is dependent on adequate research and development resources. If we are not able to adequately fund our research and development efforts, we may not be able to compete effectively and our business and operating results may be harmed.

In order to remain competitive, we must continue to develop new solution offerings and enhancements to our existing cloud contact center software. Maintaining adequate research and development personnel and resources to meet the demands of the market is essential. If we are unable to develop products, applications or features internally due to constraints, such as high employee turnover, insufficient cash, inability to hire sufficient research and development personnel or a lack of other research and development resources, we may miss market opportunities. Furthermore, many of our competitors expend considerably greater amounts on their research and development programs than we do, and those that do not may be acquired by larger companies that would allocate greater resources to our competitors' research and development programs. Our failure to devote adequate research and development resources or compete effectively with the research and development programs of our competitors could harm our business.

If we are unable to maintain the compatibility of our software with other products and technologies, our business would be harmed.

Our clients often integrate our solution with their business applications, particularly third-party CRM solutions. These third-party providers or their partners could alter their products so that our solution no longer integrates well with them, or they could delay or deny our access to technology releases that allow us to adapt our solution to integrate with their products in a timely fashion. If we cannot adapt our solution to changes in complementary technology deployed by our clients, it may significantly impair our ability to compete effectively.

Our business could be harmed if our clients are not satisfied with the professional services and technical support provided by us or our partners.

Our business depends on our ability to satisfy our clients, not only with respect to our solution, but also with the professional services and technical support that are required for our clients to implement and use our solution to address their business needs. Professional services and technical support may be performed by our own staff or, with respect to a select subset of our solution, by third parties. We will need to continue to expand and optimize our professional services and technical support in order to keep up with new client installations and ongoing service, which will take time and expense to implement. Identifying and recruiting qualified service personnel and training them in our solution is difficult and competitive and requires significant time, expense and attention. We may be unable to respond quickly enough to accommodate short-term increases in client demand for support services. We also may be unable to modify the format of our support services or change our pricing to compete with changes in support services provided by our competitors. Increased client demand for these services, without corresponding revenues, could increase our costs and harm our operating results. If a client is not satisfied with the deployment and ongoing services performed by us or a third party, then we could lose clients, miss opportunities to expand our business with these clients, incur additional costs, or lose, or suffer reduced margins on, our service revenue, any of which could damage our ability to grow our business. In addition, negative publicity related to our professional services and technical support, regardless of its accuracy, may damage our business by affecting our ability to compete for new business with current and prospective clients.

Sales to clients outside the United States or with international operations and our international sales efforts and operations support expose us to risks inherent in international sales and operations.

A key element of our growth strategy is to expand our international sales efforts and develop a worldwide client base. Because of our limited experience with international sales, our international expansion may not be successful and may not produce the return on investment we expect. To date, we have realized only a small portion of our revenues from clients outside the United States.

Our international employees are primarily located in the Philippines, where technical support, training and other professional services are performed, and Russia, where software development services are performed. We have also started to ramp sales, marketing and support personnel in the U.K. to maintain and support our European data centers and to provide service and support to clients in certain countries of the European Union. Operating in international markets requires significant resources and management attention and subjects us to intellectual property, regulatory, economic and political risks that are different from those in the United States. As we increase our international sales

efforts and continue our other international operations, we will face risks in doing business internationally that could harm our business, including:

- the need to establish and protect our brand in international markets;

Table of Contents

- the need to localize and adapt our solution for specific countries, including translation into foreign languages and associated costs and expenses;
- difficulties in staffing and managing foreign operations, particularly hiring and training qualified sales and service personnel;
- different pricing environments, longer sales and accounts receivable payment cycles and collections issues;
- weaker protection for intellectual property and other legal rights than in the U.S. and practical difficulties in enforcing intellectual property and other rights outside of the U.S.;
- increased risk of piracy, counterfeiting and other misappropriation of our intellectual property in our locations outside the U.S.;
- new and different sources of competition;
- general economic conditions in international markets;
- fluctuations in the value of the U.S. dollar and foreign currencies, which may make our solution more expensive in other countries or may increase our costs, impacting our operating results when translated into U.S. dollars;
- compliance with customs duties, tariffs and other international trade complexities;
- compliance challenges related to the complexity of multiple, conflicting and changing governmental laws and regulations, including employment, tax, telecommunications and telemarketing laws and regulations;
- privacy and data protection laws and regulations that are complex, expensive to comply with and may require that client data be stored and processed in a designated territory;
- increased risk of international telecom fraud;
- laws and business practices favoring local competitors;
- compliance with U.S. laws and regulations for foreign operations, including the Foreign Corrupt Practices Act, the U.K. Bribery Act, import and export control laws, tariffs, trade barriers, economic sanctions and regulatory or contractual limitations on our ability to sell our solution in certain foreign markets, and the risks and costs of non-compliance;
- increased financial accounting and reporting burdens and complexities;
- restrictions on the transfer of funds;
- adverse tax consequences; and
- unstable economic and political conditions.

These risks could harm our international operations, increase our operating costs and hinder our ability to grow our international business and, consequently, our overall business and results of operations. In addition, if the political and military situation in Russia and the Ukraine significantly worsens, or if either Russia or the United States imposes significant new economic sanctions or restrictions, and we are restricted or precluded from continuing our software development operations in Russia, our costs could increase, and our product development efforts, business and results of operations could be significantly harmed.

In addition, compliance with laws and regulations applicable to our international operations increases our cost of doing business outside the United States. We may be unable to keep current with changes in foreign government requirements and laws as they change from time to time. Failure to comply with these regulations could harm our business. In many countries outside the United States it is common for others to engage in business practices that are prohibited by our internal policies and procedures or U.S. regulations applicable to us. Although we have implemented policies and procedures designed to ensure compliance with these laws and policies, there can be no assurance that all of our employees, contractors, strategic partners and agents will comply with these laws and policies. Violations of laws or key control policies by our employees, contractors, strategic partners or agents could result in delays in revenue recognition, financial reporting misstatements, fines, penalties, or prohibitions on selling our solution, any of which could harm our business.

The results of the United Kingdom’s referendum on withdrawal from the European Union may have a negative effect on global economic conditions, financial markets and our business.

In June 2016, a majority of voters in the United Kingdom elected to withdraw from the European Union in a national referendum, referred to as Brexit. The referendum was advisory, and the terms of any withdrawal are subject to a

negotiation period that could last at least two years after the government of the United Kingdom formally initiates a withdrawal process. Nevertheless, the referendum has created significant uncertainty about the

Table of Contents

future relationship between the United Kingdom and the European Union, including with respect to the laws and regulations that will apply as the United Kingdom and the European Union determine which European Union laws to replace or replicate in the event of a withdrawal. The referendum has also given rise to calls for the governments of other European Union member states to consider withdrawal.

Brexit has adversely affected and may continue to adversely affect global economic conditions and the stability of global financial markets. For example, Brexit introduced significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the strengthening of the U.S. dollar against foreign currencies in which we conduct business. The strengthening of the U.S. dollar relative to other currencies will make our solution more expensive to international clients and may adversely affect our international sales. Brexit could also cause disruptions to and create uncertainty surrounding our business, including affecting our relationships with our existing and future clients, owners of our data center facilities in the U.K. and The Netherlands and our data center partners' ability to retain and hire qualified employees, which could harm our business, business opportunities, results of operations, financial condition and cash flows.

We depend on our senior management team and the loss of one or more key employees or an inability to attract and retain highly skilled employees could harm our business and results of operations.

Our success largely depends upon the continued services of our key executive officers. We also rely on our leadership team in the areas of research and development, marketing, sales, services and general and administrative functions, and on mission-critical individual contributors. From time to time, there may be changes in our executive management team resulting from the hiring or departure of executives, which could disrupt our business. The loss of one or more of our executive officers or key employees could seriously harm our business. We currently do not maintain key person life insurance policies on any of our employees.

To execute our growth plan, we must attract and retain highly qualified personnel and we may incur significant costs to do so. Competition for these personnel is intense, especially for engineers with high levels of experience in designing and developing cloud software and for senior sales executives. We have, from time to time, experienced, and we expect to continue to experience, difficulty in hiring and retaining employees with appropriate qualifications. We invest significant time and expense in training our employees, which increases their value to competitors who may seek to recruit them and increases our costs. If we fail to attract new personnel or fail to retain and motivate our current personnel, our business and future growth prospects would be harmed. Many of the companies with which we compete for experienced personnel have greater resources than we have. If we hire employees from competitors or other companies, their former employers may attempt to assert that these employees or we have breached legal obligations, resulting in a diversion of our time and resources and, potentially, damages.

Volatility or lack of performance in the trading price of our common stock may also affect our ability to attract and retain qualified personnel because job candidates and existing employees often emphasize the value of the stock awards they receive in connection with their employment when considering whether to accept or continue employment. If the perceived value of our stock awards is low or declines, it may harm our ability to recruit and retain highly skilled employees.

If we fail to grow our marketing capabilities and develop widespread brand awareness cost effectively, our business may suffer.

Our ability to increase our client base and achieve broader market acceptance of our cloud contact center software solution will depend to a significant extent on our ability to expand our marketing operations. We plan to continue to dedicate significant resources to our marketing programs, including internet advertising, digital marketing campaigns, social marketing, trade shows, industry events, co-marketing with strategic partners and telemarketing. The effectiveness of our online advertising may vary in the future due to competition for key search terms, changes in search engine use and changes in the search algorithms used by major search engines. All of these efforts will continue to require us to invest significant financial and other resources in our marketing efforts.

In addition, we believe that developing and maintaining widespread awareness of our brand in a cost-effective manner, both in the United States and internationally, is critical to achieving widespread acceptance of our solution and attracting new clients. Brand promotion activities may not generate client awareness or increase revenues, and may not offset the costs and expenses we incur in building our brand. If we fail to successfully promote, maintain and

protect our brand, or incur substantial costs and expenses, we may fail to attract or retain clients necessary to realize a sufficient return on our brand-building efforts, or to achieve the widespread brand awareness that is critical for broad client adoption of our solution.

Table of Contents

We may not be able to secure additional financing on favorable terms, or at all, to meet our future capital needs.

To date, we have financed our operations primarily through sales of our solution, lease facilities and net proceeds from our equity and debt financings. We do not know when or if our operations will generate sufficient cash to fund our ongoing operations. In the future, we may require additional capital to respond to business opportunities, challenges, acquisitions, a decline in sales, increased regulatory obligations or unforeseen circumstances and may engage in equity or debt financings or enter into credit facilities.

We have a substantial amount of debt. As of September 30, 2016, we had approximately $32.6 million in principal amount outstanding under our New Revolving Credit Facility entered into on August 1, 2016 (see Note 5 of the notes to condensed consolidated financial statements under Part I - Item 1 and 'Liquidity and Capital Resources' under Part I - Item 2 of this Form 10-Q), $0.5 million outstanding under a promissory note with the USAC and a $1.2 million FCC civil penalty payable to the U.S. Treasury (see Note 5 of the notes to condensed consolidated financial statements under Part I - Item 1 of this Form 10-Q). The New Revolving Credit Facility is collateralized by substantially all of our assets and contains a number of covenants that limit our ability to, among other things, sell assets, make acquisitions or investments, incur debt, grant liens, pay dividends or make distributions, enter into transactions with our affiliates and use all of our available cash on hand and may prevent us from engaging in acts that may be in our best long-term interests. The amount of our current debt, our debt service obligations, the collateral pledged under the New Revolving Credit Facility and the covenants to which we are bound may prevent us from being able to timely secure additional debt or equity financing on favorable terms, or at all, or to pursue business opportunities, including potential acquisitions.

Any debt financing obtained by us in the future would cause us to incur additional debt service expenses and could include restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and pursue business opportunities. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution in their percentage ownership of our company, and any new equity securities we issue could have rights, preferences and privileges senior to those of holders of our common stock. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to grow and support our business and to respond to business challenges could be significantly limited.

Adverse economic conditions may harm our business.

Our business depends on the overall demand for cloud contact center software solutions and on the economic health of our current and prospective clients. In general, worldwide economic conditions remain unstable. The results of the United Kingdom’s referendum on withdrawal from the European Union, slow growth and economic uncertainty in the U.S. and in various parts of the world, and fluctuations in interest rates and foreign currency exchange rates, has added to the uncertainty regarding economic conditions generally. In addition to the United States, we plan to market and sell our solution in Europe, Asia and other international markets. If economic conditions, including currency exchange rates, in these areas and other key potential markets for our solution continue to remain uncertain or deteriorate further, clients may delay or reduce their contact center and overall information technology spending. If our clients experience economic hardship, this could reduce the demand for our solution, delay and lengthen sales cycles, lower prices for our solution, and lead to slower growth or even a decline in our revenues, operating results and cash flows.

We may acquire other companies or technologies or be the target of strategic transactions, which could divert our management’s attention, result in additional dilution to our stockholders and otherwise disrupt our operations and harm our operating results.

We may acquire or invest in businesses, applications or technologies that we believe could complement or expand our solution, enhance our technical capabilities or otherwise offer growth opportunities. The pursuit of potential acquisitions may divert the attention of management, and cause us to incur various costs and expenses in identifying, investigating and pursuing acquisitions, whether or not they are consummated. We may not be able to identify desirable acquisition targets or be successful in entering into an agreement with any particular target.

To date, the growth in our business has been primarily organic, and we have limited experience in acquiring other businesses, having only completed one small acquisition. In any future acquisitions, we may not be able to successfully integrate acquired personnel, operations and technologies, or effectively manage the combined business

following the acquisition. We also may not achieve the anticipated benefits from our future acquired businesses due to a number of factors, including:

- inability to integrate or benefit from acquisitions in a profitable manner;

Table of Contents

- unanticipated costs or liabilities associated with the acquisition, including legal claims arising from the activities of companies we acquire;
- incurrence of acquisition-related costs;
- difficulty converting the clients of the acquired business to our solution and contract terms, including disparities in the revenues, licensing, support or professional services model of the acquired company;
- difficulty integrating the accounting systems, operations and personnel of the acquired business;
- difficulties and additional costs and expenses associated with supporting legacy products and hosting infrastructure of the acquired business;
- diversion of management's attention from other business concerns;
- harm to our existing relationships with our partners and clients as a result of the acquisition;
- the loss of our or the acquired business's key employees;
- diversion of resources that could have been more effectively deployed in other parts of our business; and
- use of substantial portions of our available cash to consummate the acquisition.

In addition, a significant portion of the purchase price of companies we acquire may be allocated to acquired goodwill and other intangible assets, which must be assessed for impairment at least annually. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could harm our results of operations.

Acquisitions could also result in dilutive issuances of equity securities, the use of our available cash, or the incurrence of debt, which could harm our operating results. In addition, if an acquired business fails to meet our expectations, our operating results, business and financial condition may suffer.

In addition, we sometimes receive inquiries relating to potential strategic transactions, including from third parties who may seek to acquire us. We will continue to consider and discuss such transactions as we deem appropriate. Such potential transactions may divert the attention of management, and cause us to incur various costs and expenses in investigating and evaluating such transactions, whether or not they are consummated.

If we are unable to maintain and further develop effective internal control over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock may decrease.

As a public company, we are required to maintain internal control over financial reporting and to report any material weaknesses in such internal controls. Section 404 of the Sarbanes-Oxley Act of 2002 ("Section 404") requires that we evaluate and determine the effectiveness of our internal control over financial reporting and provide a management report on our internal control over financial reporting. However, our independent registered public accounting firm will not be required to formally attest to the effectiveness of our internal control over financial reporting pursuant to Section 404 until we are no longer an "emerging growth company," as defined by The Jumpstart Our Businesses Act of 2012 (the "JOBS Act").

In the future, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that our internal controls are effective. A "material weakness" is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

If we have material weaknesses in our internal control over financial reporting, we may not detect errors on a timely basis and our financial statements may be materially misstated. If we identify material weaknesses in our internal control over financial reporting, if we are unable to comply with the requirements of Section 404 in a timely manner, if we are unable to assert that our internal control over financial reporting is effective or if our independent registered public accounting firm is unable to attest that our internal control over financial reporting is effective, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock could decrease. We could also become subject to stockholder or other third-party litigation as well as investigations by the stock exchange on which our securities are listed, the SEC or other regulatory authorities, which could require additional financial and management resources and could result in fines, trading suspensions or other remedies.

Table of Contents

Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported operating results.

U.S. GAAP are subject to interpretation by the FASB, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. A change in accounting standards or practices can have a significant effect on our reported results and may even affect our financial statements completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and will occur in the future. Changes to existing rules or the questioning of current practices may harm our reported financial results or the way we account for or conduct our business.

For example, we recognize revenue in accordance with ASU 2009-13, Revenue Recognition (Topic 605) — Multiple-Deliverable Revenue Arrangements — a Consensus of the Emerging Issues Task Force (formerly known as EITF 08-01). In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, a new standard on the recognition of revenue from contracts with customers, which includes a single set of rules and criteria for revenue recognition to be used across all industries. Companies may use either a full retrospective or a modified retrospective approach to adopt ASU 2014-09. The new standard is effective for our annual and interim reporting periods beginning January 1, 2018. All companies that enter into contracts with customers to transfer goods or services will be affected in some way by ASU 2014-09. As a result of future interpretations or applications of existing and new accounting standards, including ASU 2014-09 and ASU 2009-13, the timing of our revenue recognition could change, which would cause fluctuations in our operating results.

In addition, certain factors have in the past and may in the future cause us to defer recognition of revenues. For example, the inclusion in our client contracts of material non-standard terms, such as acceptance criteria, could require the deferral of revenue. To the extent that such contracts become more prevalent in the future our revenue may be harmed.

Because of these factors and other specific requirements under U.S. GAAP for revenue recognition, we must have precise terms and conditions in our arrangements in order to recognize revenue when we deliver our solution or perform our professional services. Negotiation of mutually acceptable terms and conditions can extend our sales cycle, and we may accept terms and conditions that do not permit revenue recognition at the time of delivery.

We may not be able to utilize a significant portion of our net operating loss or research tax credit carryforwards, which could harm our profitability and financial condition.

As of December 31, 2015, we had federal and state net operating loss carryforwards due to prior period losses of $124.4 million and $85.2 million, respectively, which if not utilized will begin to expire in 2024 for federal purposes and began to expire in 2015 for state purposes. We also have research and development credit carryforwards of approximately $2.2 million and $1.8 million for federal and state income taxes, respectively, which if not utilized will begin to expire in 2022. If we are unable to generate sufficient taxable income to utilize our net operating loss and research tax credit carryforwards, these carryforwards could expire unused and be unavailable to offset future income tax liabilities, which could harm our profitability and financial condition.

In addition, under Section 382 of the Internal Revenue Code of 1986, as amended (“IRC Section 382”), our ability to utilize net operating loss carryforwards or other tax attributes, such as research tax credits, in any taxable year may be limited if we experience an “ownership change.” An IRC Section 382 “ownership change” generally occurs if one or more stockholders or groups of stockholders who own at least 5% of our stock increase their ownership by more than 50 percentage points over their lowest ownership percentage within a rolling three-year period. Similar rules may apply under state tax laws. We experienced an ownership change prior to 2014 and the disclosed amounts of our net operating losses and potential tax credits have been reduced for the effect of the IRC Section 382 limitations. Subsequent or future issuances or sales of our stock (including certain transactions involving our stock that are outside of our control) could cause an “ownership change” again, which would impose an annual limit on the amount of pre-ownership change net operating loss carryforwards and other tax attributes we can use to reduce our taxable income, potentially increasing and accelerating our liability for income taxes, and also potentially causing those tax attributes to expire unused. It is possible that such an ownership change could materially reduce our ability to use our net operating loss carryforwards or other tax attributes to offset taxable income, which could require us to pay more income taxes than if we were able to fully utilize our net operating loss carryforwards and harm our profitability.

45

Table of Contents

Risks Related to Our Intellectual Property

Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand.

Our success and ability to compete depend in part upon our intellectual property. As of September 30, 2016, our intellectual property portfolio included nine registered U.S. trademarks, ten issued U.S. patents, three pending U.S. patent applications and one registered U.S. copyright. As of September 30, 2016, we also had four issued patents, nine pending patent applications and fourteen limited trademark registrations outside the U.S. The expiration dates of our issued patents range from 2030 to 2034. We primarily rely on copyright, trade secret and trademark laws, trade secret protection and confidentiality or license agreements with our employees, clients, partners and others to protect our intellectual property rights. However, the steps we take to protect our intellectual property rights may be inadequate. We may not be able to obtain any further patents or trademarks, our current patents could be invalidated or our competitors could design their products around our patented technology, and our pending applications may not result in the issuance of patents or trademarks. We have pending patent applications and limited trademark registrations outside the U.S., and we may have to expend significant resources to obtain additional protection as we expand our international operations. Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in other countries, including Russia, where we have significant research and development operations, and the Philippines, where we have significant technical support, training and other professional services are performed, are uncertain and may afford little or no effective protection of our proprietary technology, and the risk of intellectual property misappropriation may be higher in these countries. Consequently, we may be unable to prevent our proprietary technology from being exploited abroad, which could affect our ability to expand into international markets or require costly efforts to protect our technology.

In order to protect our intellectual property rights, we may be required to spend significant resources to monitor and protect these rights. Litigation brought to protect and enforce our intellectual property rights could be costly, time consuming and distracting to management and could result in the impairment or loss of our intellectual property. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. Accordingly, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property. Our failure to secure, protect and enforce our intellectual property rights could substantially harm the value of our technology, solutions, brand and business.

We will likely continue to be subject to third-party intellectual property infringement claims.

There is considerable patent and other intellectual property development activity and litigation in our industry. Our success depends upon our not infringing upon the intellectual property rights of others. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our industry. From time to time, third parties have claimed that we are infringing upon their intellectual property rights. For example, on April 3, 2012, NobelBiz, Inc. (“NobelBiz”) filed a patent infringement lawsuit against us alleging that our local caller ID management service infringes United States Patent No. 8,135,122. Subsequently, NobelBiz amended its complaint to add claims related to U.S. Patent No. 8,565,399, which is a continuation in the same family as the prior patent and addresses the same technology. NobelBiz seeks damages in the form of lost profits as well as injunctive relief. See “Part II, ITEM 1. Legal Proceedings.” If NobelBiz is successful in its request for injunctive relief, we will have to stop providing the accused technology, enter into a license agreement with NobelBiz for the technology or modify our technology, any of which could harm our business. There can be no assurance that we (i) will prevail in this action, (ii) can develop non-infringing technology that is accepted in the market if we are enjoined from using the accused technology or (iii) will be able to negotiate favorable licensing terms with NobelBiz. There can also be no assurance that other actions alleging infringement by us of third-party patents will not be asserted or prosecuted against us.

Certain technology necessary for us to provide our solution may be patented, copyrighted or otherwise protected by other parties either now or in the future. In such case, we would have to negotiate a license for the use of that technology. We may not be able to negotiate such a license at a price that is acceptable, or at all. The existence of such a patent, copyright or other protections, or our inability to negotiate a license for any such technology on acceptable terms, could force us to cease using such technology and offering solutions incorporating such technology.

Others have claimed, or in the future may claim, that our solution and underlying technology infringe or violate their intellectual property rights. However, we may be unaware of the intellectual property rights that others may claim cover some or all of our technology or solution. Any claims or litigation could cause us to incur

Table of Contents

significant costs and expenses and, if successfully asserted against us, could require that we pay substantial damages or ongoing royalty payments, require that we refrain from using, manufacturing or selling certain offerings or features or using certain processes, prevent us from offering our solution or certain features thereof, or require that we comply with other unfavorable terms, any of which could harm our business and operating results. We may also be obligated to indemnify our clients or business partners or pay substantial settlement costs, including royalty payments, in connection with any such claim or litigation and to obtain licenses, modify applications, or refund fees, which could be costly. Even if we were to prevail in such a dispute, any litigation regarding our intellectual property could be costly and time consuming and divert the attention of our management and key personnel from our business operations.

We employ third-party licensed software for use in or with our solution, and the inability to maintain these licenses or errors in the software we license could result in increased costs, or reduced service levels, which could harm our business.

Our solution incorporates certain third-party software obtained under licenses from other companies. We anticipate that we will continue to rely on such software and development tools from third parties in the future. Although we believe that there are commercially reasonable alternatives to the third-party software we currently license, this may not always be the case, or it may be difficult or costly to transition to other providers. In addition, integration of the software used in our solution with new third-party software may require significant work and require substantial investment of our time and resources. To the extent that our solution depends upon the successful operation of third-party software in conjunction with our software, any undetected errors or defects in this third-party software could prevent the deployment or impair the functionality of our solution, delay new product or solution introductions, result in increased costs, or a failure of our solution and injure our reputation. Our use of additional or alternative third-party software would require us to enter into license agreements with third parties and to integrate such software to our solution.

There can be no assurance that the technology licensed by us will continue to provide competitive features and functionality or that licenses for technology currently utilized by us or other technology that we may seek to license in the future, will be available to us at a reasonable cost or on commercially reasonable terms, or at all. Third-party licensors may also be acquired or go out of business, which could preclude us from continuing to use such technology. The loss of, or inability to maintain, existing licenses could result in lost product features, as well as implementation delays or reductions until equivalent technology or suitable alternative solutions could be developed, identified, licensed and integrated, and could increase our costs and harm our business.

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

Our solution includes software covered by open source licenses, which may include, for example, free general public use licenses, open source front-end libraries, open source stand-alone applications and open source applications. The terms of various open source licenses have not been interpreted by United States courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to market our solution. By the terms of certain open source licenses, we could be required to release the source code of our proprietary software, and to make our proprietary software available under open source licenses, if we combine our proprietary software with open source software in a certain manner. In the event that portions of our proprietary software are determined to be subject to an open source license, we could be required to publicly release the affected portions of our source code, re-engineer all or a portion of our technologies, or otherwise be limited in the licensing of our technologies, each of which could reduce or eliminate the value of our technologies and solutions. In addition to risks related to license requirements, usage of open source software can lead to greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of the software. Given the nature of open source software, there is also a risk that third parties may assert copyright and other intellectual property infringement claims against us based on our use of certain open source software programs. Many of the risks associated with the usage of open source software cannot be eliminated, and could harm our business.

Risks Related to Regulatory Matters

Failure to comply with laws and regulations could harm our business and our reputation.

Our business is subject to regulation by various federal, state, local and foreign governmental agencies, including agencies responsible for monitoring and enforcing employment and labor laws, workplace safety, environmental laws, consumer protection laws, anti-bribery laws, import/export controls, federal securities laws and

Table of Contents

tax laws and regulations. In certain jurisdictions, these regulatory requirements may be more stringent than those in the United States and in other circumstances these requirements may be more stringent in the United States. Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, mandatory recalls, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties or injunctions. If any governmental sanctions, fines or penalties are imposed, or if we do not prevail in any possible civil or criminal litigation, our business, operating results, financial condition and our reputation could be harmed. In addition, responding to any action will likely result in a significant diversion of management's attention and resources and an increase in professional fees. Enforcement actions and sanctions could further harm our business, operating results, financial condition and our reputation.

Alleged or actual failure to comply with the constantly evolving legal and contractual environment surrounding calling consumers and wireless phone numbers by other companies or our competitors or governmental or private enforcement actions related thereto, could harm our business, financial condition, results of operations and cash flows.

The legal and contractual environment surrounding calling consumers and wireless phone numbers is constantly evolving. In the United States, two federal agencies, the Federal Trade Commission, or FTC, and the FCC, and various states have laws including, at the federal level, the Telephone Consumer Protection Act of 1991, or TCPA, that restrict the placing of certain telephone calls and texts to residential and wireless telephone subscribers by means of automatic telephone dialing systems, prerecorded or artificial voice messages and fax machines. These laws require companies to institute processes and safeguards to comply with these restrictions. Some of these laws, where a violation is established, can be enforced by the FTC, FCC, State Attorneys General, or private party litigants. In these types of actions, the plaintiff may seek damages, statutory penalties, costs and/or attorneys' fees.

We have designed our solution to comply with these laws. To the extent that our solution is viewed by clients or potential clients as less functional, or more difficult to deploy or use, because of our solution's compliance features, we may lose market share to competitors that do not include similar compliance safeguards. Our contractual arrangements with our clients who use our solution to place calls also expressly require them to comply with all such laws and to indemnify us for any failure to do so. We take reasonable steps to confirm such compliance. Even with these efforts, it is possible that the FTC, FCC, private litigants or others may attempt to hold our clients, or us as a software provider, responsible for alleged violations of these laws. It also is possible that we may not successfully enforce or collect upon our contractual indemnities from our clients. Additionally, these laws, and any changes to them or the interpretation thereof, that further restrict calling consumers, including to wireless phone numbers, adverse publicity regarding the alleged or actual failure by companies, including our clients and competitors, to comply with such laws or governmental or private enforcement actions related thereto, could result in a reduction in the use of our solution by our clients and potential clients, which could harm our business, financial condition, results of operations and cash flows.

Increased taxes on our service may increase our clients' cost of using our service and/or increase our costs and reduce our profit margins to the extent the costs are not passed through to our clients, and we may be subject to liabilities for past sales and other taxes, surcharges and fees.

Prior to 2012, we did not collect or remit U.S. state or local sales, use, gross receipts, excise and utility user taxes, fees or surcharges on our solution.

During 2011, we analyzed our activities and determined that we were obligated to collect sales taxes on sales of our subscription services in certain U.S. states. Accordingly, we registered with those states and, in 2012, commenced paying past-due amounts and collecting sales taxes from our clients and remitting such taxes to the applicable state taxing authorities. During the first quarter of 2015, we conducted an updated review of the taxability of sales of our subscription services and identified four additional U.S. states where we may be obligated to collect and remit sales taxes.

During 2013, we analyzed our activities and determined that we may be obligated to collect and remit sales, excise and utility user taxes, as well as surcharges as a communications service provider, and pay gross receipts taxes, on our usage-based fees in certain U.S. states and municipalities. We neither collected nor remitted state and local taxes or surcharges on usage-based fees in any of the periods prior to 2014. Based on our ongoing assessment of our U.S. state and local tax collection and remittance obligations in respect of usage-based fees, in 2014, we registered for tax and

regulatory purposes in all U.S. states where we determined such registration is proper and commenced collecting and remitting applicable state and local taxes and surcharges on such fees.

Table of Contents

Prior to 2016, we had not collected taxes for our sales in Canada. During the second quarter of 2015, we reviewed the taxability of our sales in Canada and determined that we were obligated to collect from our Canadian clients and remit to the Canadian federal and certain provincial governments VAT and/or PST. We commenced collecting and remitting such taxes in January 2016.

We have accrued a contingent liability of $2.2 million for our best estimate of the probable amount of taxes and surcharges that may be imposed by various states and municipalities on our activities, including our usage-based and subscription services, prior to registration. This contingent liability is based on our analysis of a number of factors, including the source location of our usage-based fees, the taxability of our subscription services and the rules and regulations in each state. The actual amount of state and local taxes and surcharges paid may differ from our estimates. See Note 9 of the notes to condensed consolidated financial statements.

While we have accrued for these potential liabilities in each period, such accruals are based on analyses of our business activities, the operation of our solution, applicable statutes, regulations and rules in each state and locality and estimates of sales subject to sales tax or other charges. State and local taxing and regulatory authorities may challenge our position and may decide to audit our business and operations with respect to state or local sales, use, gross receipts, excise and utility user taxes, fees or surcharges, which could result in our being liable for taxes, fees, or surcharges, as well as related penalties and interest, above our recorded accrued liability or additional liability for taxes, fees, or surcharges, as well as penalties and interest for our clients, which could harm our results of operations and our relationships with our clients. In addition, if our international sales grow, additional foreign countries may seek to impose sales or other tax collection obligations on us, which would increase our exposure to liability.

The applicability of state or local taxes, fees or surcharges relative to services such as ours is complex, ambiguous and subject to interpretation and change. If states enact new legislation or if taxing and regulatory authorities promulgate new rules or regulations or expand or otherwise alter their interpretations of existing rules and regulations, we could incur additional liabilities. In addition, the collection of additional taxes, fees or surcharges in the future could increase our prices or reduce our profit margins. Compliance with new or existing legislation, rules or regulations may also make us less competitive with those competitors who are not subject to, or choose not to comply with, such legislation, rules or regulations. We have incurred, and will continue to incur, substantial ongoing costs associated with complying with state or local tax, fee or surcharge requirements in the numerous markets in which we conduct or will conduct business.

We are subject to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to our late registration and past failure to recognize our obligation as a USF contributor and as an international carrier.

During the third quarter of 2012, we determined that based on our business activities, we are classified as a telecommunications service provider for regulatory purposes and we are required to make direct contributions to the USF based on revenue we receive from the resale of interstate and international telecommunications services. Previously, we had been advised that our telecommunications services were an integral part of an information service and accordingly made indirect USF contributions as an end user through payments to our wholesale telecommunications service providers. In order to comply with the obligation to make direct contributions, in November 2012, we made a voluntary self-disclosure to the FCC Enforcement Bureau and have registered with the USAC which is charged by the FCC with administering the USF. In April 2013, we began remitting required contributions on a prospective basis directly to USAC.

Our registration with USAC subjects us to assessments for unpaid USF contributions, as well as interest thereon and civil penalties, due to our late registration and past failure to recognize our obligation as a USF contributor and as an international carrier. We are required to pay assessments for periods prior to our registration. As of December 31, 2012, our total past due USF contribution being imposed by USAC and accrued by us for the period from 2003 through 2012 was $8.1 million, of which $4.7 million was undisputed and $3.4 million, including $0.8 million that pertains to 2003 through 2007, was disputed. As of September 30, 2016, we had a promissory note issued to USAC with an outstanding principal balance of $0.5 million for the undisputed portion and an accrued liability of $5.2 million for the disputed portion and estimated interest and penalties, which are included in notes payable amounts and accrued federal fees, respectively, in the condensed consolidated balance sheet. See Note 9 of the notes to condensed consolidated financial statements. Although we are in administrative proceedings before the FCC to limit such back

assessments to the period 2008 through 2012, it is possible that we will be required to pay back assessments for the period from 2003 to 2007. We have submitted two separate Requests for Review (a form of appeal) to the FCC's Wireline Bureau challenging the application of FCC rules to the assessments of USF fees for 2003 to 2007, and from 2008 to 2012. The FCC has not yet resolved either of those Requests for Review. If the

Table of Contents

pending disputes are not resolved in our favor, it is possible that we will be required to pay additional back assessments for one or both of those periods. The first Request for Review, which relates to 2003 to 2007 fees, asks the FCC to apply its discretion and relieve us from paying USF fees for those aging fees. The second Request for Review, which applies to both periods, seeks to obtain credit for the indirect USF payments we have made since 2003 to our wholesale telecommunications service providers. If we are unsuccessful in obtaining credit from the FCC for these payments, we will seek reimbursement from our wholesale telecommunication service providers. We will face a regulatory and contractual challenge in seeking recovery or credit for our USF reimbursement payments previously made to our wholesale telecommunication service providers.

In 2012, we also determined that we were a provider of international telecommunications services and therefore we were required to secure from the FCC a section 214 international carrier authorization permitting such international telecommunications. We applied with the FCC for international carrier authority, which was granted on June 9, 2015. On June 12, 2015, in connection with our late registration with the USAC and past failure to recognize our obligation as a USF contributor and as an international carrier from 2003 to 2012, we entered into a consent decree with the FCC Enforcement Bureau. In the consent decree, we agreed to pay a civil penalty of $2.0 million to the U.S. Treasury in twelve equal quarterly installments starting in July 2015 without interest. In the third quarter of 2014, we had accrued a $2.0 million liability for the then tentative civil penalty, of which $1.2 million in principal remained outstanding as of September 30, 2016. The consent decree also requires us to adopt certain internal regulatory compliance monitoring and training requirements, and to report on the status of those compliance efforts to the FCC's Enforcement Bureau during a period of three years. Our implementation of the internal regulatory compliance monitoring and training requirements were completed in August 2015, and the annual compliance reporting to the FCC will continue until June 2018. To the extent that we do not comply with these obligations, we could be subject to further enforcement action, including fines and penalties, by the FCC. See Note 9 of the notes to condensed consolidated financial statements.

Our ongoing obligations to pay federal, state and local telecommunications contributions and taxes may decrease our price advantage over our competitors who have historically paid these contributions and taxes and could also make us less competitive with those competitors who are not subject to, or choose not to comply with, those requirements. In addition, if we are unable to continue to pass some or all of the cost of these contributions and taxes to our clients, our profit margins on the minutes we resell will decrease. Our federal contributions and tax obligations may significantly increase in the future, due to new interpretations by governing authorities, governmental budget pressures, changes in our business model or solutions or other factors.

If we do not comply with FCC rules and regulations, we could be subject to further FCC enforcement actions, fines, loss of licenses and possibly restrictions on our ability to operate or offer certain of our services.

Since our business is regulated by the FCC, we are subject to existing or potential FCC regulations relating to privacy, disability access, porting of numbers, USF contributions and other requirements. If we do not comply with FCC rules and regulations, we could be subject to further FCC enforcement actions, fines, loss of licenses and possibly restrictions on our ability to operate or offer certain of our services. Any further enforcement action by the FCC, which may be a public process, would hurt our reputation in the industry, possibly impair our ability to sell our services to clients and could harm our business and results of operations.

Among the regulations to which we are subject, we must comply (in whole or in part) with:

- the Communications Assistance for Law Enforcement Act, or CALEA, which requires covered entities to assist law enforcement in undertaking electronic surveillance;
- contributions to the USF which requires that we pay a percentage of our revenues resulting from the provision of interstate telecommunications services to support certain federal programs;
- payment of annual FCC regulatory fees based on our interstate and international revenues;
- rules pertaining to access to our services by people with disabilities and contributions to the Telecommunications Relay Services fund; and
- FCC rules regarding Customer Proprietary Network Information, or CPNI, which prohibit us from using such information without client approval, subject to certain exceptions.

If we do not comply with any current or future rules or regulations that apply to our business, we could be subject to additional and substantial fines and penalties, we may have to restructure our service offerings, exit

Table of Contents

certain markets, accept lower margins or raise the price of our services, any of which could ultimately harm our business and results of operations.

Reform of federal and state USF programs could increase the cost of our service to our clients, diminishing or eliminating our pricing advantage.

The FCC and a number of states are considering reform or other modifications to USF programs. The way we calculate our contribution may change if the FCC or certain states engage in reform or adopt other modifications. In April 2012, the FCC released a Further Notice of Proposed Rulemaking to consider reforms to the manner in which companies like us contribute to the federal USF program. In general, the Further Notice of Proposed Rulemaking is considering questions like: what companies should contribute, how contributions should be assessed, and methods to improve the administration of the system. We cannot predict the outcome of this proceeding nor its impact on our business at this time.

Should the FCC or certain states adopt new contribution mechanisms or otherwise modify contribution obligations that increase our contribution burden, we will either need to raise the amount we currently collect from our clients to cover this obligation or absorb the costs, which would reduce our profit margins. Furthermore, the FCC has ruled that states can require us to contribute to state USF programs. A number of states already require us to contribute, while others are actively considering extending their programs to include the solution we provide. Currently our USF contributions are borne by our clients which may result in our solution becoming less competitive as compared to those provided by our competitors.

Privacy concerns and domestic or foreign laws and regulations may reduce the demand for our solution, increase our costs and harm our business.

Our clients can use our solution to collect, use and store information, including personally identifiable information or other information treated as confidential, regarding their customers and potential customers. Federal, state and foreign government bodies and agencies have adopted, are considering adopting, or may adopt laws and regulations regarding the collection, use, storage and disclosure of such information obtained from consumers and individuals. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to us and the businesses of our clients may limit the use and adoption of our solution and reduce overall demand, or lead to significant fines, penalties or other regulatory liabilities such as orders or consent decrees forcing us to modify our business practices, as well as reputational damage or third-party lawsuits for any noncompliance with such privacy laws. Furthermore, privacy concerns may cause consumers to resist providing the personal data necessary to allow our clients to use our solution effectively. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our solution in certain industries or countries.

Domestic and international legislative and regulatory initiatives may harm our clients' ability to process, handle, store, use and transmit information, including demographic and personally identifiable information or other information treated as confidential, regarding their customers, which could reduce demand for our solution. These laws and regulations are still evolving and are likely to be in flux and subject to uncertain interpretation for the foreseeable future. Our business could be harmed if legislation or regulations are adopted, interpreted or implemented in a manner that is inconsistent from country to country and inconsistent with our current policies and practices, or those of our clients. In addition, foreign data protection, privacy, and consumer protection laws and regulations are often more stringent than those in the United States. In particular, the European Union and its member states traditionally have imposed greater legal obligations on companies that collect and process personal data.

In October 2015, the Court of Justice for the European Union invalidated the EU-US Safe Harbor program, or the Safe Harbor. The Safe Harbor provided participating U.S. companies with a legal basis to comply with EU data transfer regulations that would otherwise restrict the transfer of personal data by our customers from the European Union to us in the United States. Some of our clients relied on the Safe Harbor to transfer the personal data of their customers located in the EU to the United States. Other clients relied on legally recognized alternative mechanisms such as standard contractual clauses issued by the European Commission (commonly referred to as "model contracts") or binding corporate resolutions to make such transfers. We relied on the use of standard contractual clauses issued by the European Commission before the invalidation of the Safe Harbor Program in October 2015, and we continue to do so currently. In July 2016, EU and U.S. regulators announced the approval of a new trans-Atlantic Agreement, the

EU-U.S. Privacy Shield, which succeeds the Safe Harbor Program. Companies interested in self-certifying compliance with this new trans-Atlantic data-transfer framework can do so as of August 2016, when the U.S. Department of Commerce began accepting certifications. The self-certification process under the Privacy

Table of Contents

Shield is similar to the Safe Harbor program. However, the compliance requirements under the Privacy Shield are generally more stringent than under the Safe Harbor.

Other methods for transferring personal data across the Atlantic are also facing legal scrutiny. In May 2016, the Irish Data Protection Commissioner announced its intention to seek declaratory relief in the Irish High Court and a referral to the European Court of Justice, or the ECJ, to determine the legal status of data transfers under standard contractual clauses. An adverse decision from the ECJ will impact how either we or our clients transfer personal data out of the European Union. Further uncertainty exists with regard to data transfers in relation to the United Kingdom due to the recent referendum in which voters in the UK decided to withdraw from the European Union. Finally, the EU recently adopted the General Data Protection Regulation, or GDPR, which is the most comprehensive reform of data protection law in the EU's history. The GDPR, which is expected to be effective in May 2018, will significantly update and modify European data protection law, including extending its application to a wider range of non-EU entities, harmonizing data protection rules across EU member states, giving data subjects important new rights, and significantly increasing penalties for non-compliance.

Any of these developments, and the cost of compliance, could harm our operations and financial results. Moreover, any non-compliance, or perceived non-compliance, with these obligations could result in investigations or enforcement actions by applicable regulators, lawsuits by private parties, changes to our business practices, increased cost of operations, or declines in client growth, or may otherwise harm our business. In addition to government activity, privacy advocacy groups and the technology and other industries are considering various new, additional or different self-regulatory standards that may place additional burdens on us. If the processing of information were to be curtailed in this manner, our solution may be less attractive, which may reduce demand for our solution and harm our business.

Risks Related to Ownership of Our Common Stock

Our stock price has been volatile, may continue to be volatile and may decline, including due to factors beyond our control.

The market price of our common stock has been volatile in the past and may fluctuate significantly in the future in response to numerous factors, many of which are beyond our control. During the nine months ended September 30, 2016, the sale price per share of our common stock ranged from a low of $6.14 to a high of $16.23. Factors that may contribute to continuing volatility in the price of our common stock include:

- actual or anticipated fluctuations in our operating results;
- the financial projections we provide to the public, any changes in these projections or our failure to meet these projections;
- failure of securities analysts to initiate or maintain coverage of our company, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;
- ratings changes by any securities analysts who follow our company;
- sales or distributions of our common stock by us or our significant stockholders, or the public announcement of same;
- the assessment of our business or position in our market published in research and other reports;
- announcements by us or our competitors of significant technical innovations, acquisitions, strategic partnerships, joint ventures or capital commitments;
- changes in operating performance and stock market valuations of other technology companies generally, or those in the SaaS industry in particular;
- price and volume fluctuations in the overall stock market, including as a result of trends in the U.S. or global economy;
- any major change in our board of directors or management;
- lawsuits threatened or filed against us;
- legislation or regulation of our business, the internet and/or contact centers;
- loss of key personnel;
- new entrants into the contact center market, including the transition by providers of legacy on-premise contact center systems to cloud solutions, as well as cable and incumbent telephone companies and other well-capitalized competitors;

52

Table of Contents

- new products or new sales by us or our competitors;
- the perceived or real impact of events that harm our direct competitors;
- developments with respect to patents or proprietary rights;
- general market conditions;
- distributions to limited partners, or block sales, by original venture capital investors; and
- other events or factors, including those resulting from war, incidents of terrorism or responses to these events, which could be unrelated to, or outside of, our control.

In addition, stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many technology companies. Stock prices of many technology companies have fluctuated in a manner unrelated or disproportionate to the operating performance of those companies. These and other factors may disproportionately impact the trading price of our common stock. In the past, stockholders have instituted securities class action litigation following periods of market volatility. If we were to become involved in securities litigation, it could subject us to substantial costs, divert resources and the attention of management from our business and harm our business, results of operations, financial condition, reputation and cash flows.

If securities or industry analysts discontinue publishing research or reports about our business, or publish negative reports about our business, our share price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business, our market and our competitors. We do not have any control over these analysts. If one or more of the analysts who cover us downgrade our shares or change their opinion of our shares, our share price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

Substantial future sales of shares of our common stock could cause the market price of our common stock to decline.

The market price of shares of our common stock could decline as a result of substantial sales of our common stock, particularly sales by our directors, executive officers and significant stockholders and persons to whom our shares are distributed by our significant stockholders or the perception in the market that holders of a large number of shares intend to sell their shares.

As of September 30, 2016, the holders of up to approximately 6,249,479 shares of our outstanding common stock (including shares of common stock issuable upon exercise of our warrants) have rights, subject to certain conditions, to require us to file registration statements covering their shares or to include their shares in registration statements that we may file for ourselves or our stockholders. The filing of a registration statement for these shares may cause our stock price to decline, even before such shares are actually sold in the market. We have also registered shares of common stock that we may issue under our employee equity incentive plans. These shares can be sold freely in the public market upon issuance.

We are an emerging growth company and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an “emerging growth company” as defined in the JOBS Act. Under the JOBS Act, emerging growth companies can delay adopting new or revised financial accounting standards until such time as those standards apply to private companies. We irrevocably elected not to avail ourselves of this extended transition period and, therefore, we are subject to the same new or revised accounting standards as other public companies that are not “emerging growth companies.”

For as long as we continue to be an emerging growth company, we may take advantage of certain other exemptions from reporting requirements that are applicable to other public companies including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. Investors may find our common stock less attractive because we rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading

market for our common stock and our stock price may be more volatile or decline.

Table of Contents

We will remain an emerging growth company until the earliest of (i) the end of the fiscal year in which the market value of our common stock that is held by non-affiliates is at least $700 million as of the last business day of our most recently completed second fiscal quarter, (ii) the end of the fiscal year in which we have total annual gross revenues of $1 billion or more during such fiscal year, (iii) the date on which we issue more than $1 billion in non-convertible debt in a three-year period or (iv) the end of fiscal 2019.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of our company more difficult, limit attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws may have the effect of delaying or preventing a change in control or changes in our management. Our amended and restated certificate of incorporation and amended and restated bylaws:

- provide that our board of directors is classified into three classes of directors;
- provide that stockholders may remove directors only for cause and only with the approval of holders of at least 66 $^{2}/_{3}$% of our then outstanding capital stock;
- provide that the authorized number of directors may be changed only by resolution of the board of directors;
- provide that all vacancies, including newly created directorships, may, except as otherwise required by law, be filled by the affirmative vote of a majority of directors then in office, even if less than a quorum;
- provide that our stockholders may not take action by written consent, and may only take action at annual or special meetings of our stockholders;
- provide that stockholders seeking to present proposals before a meeting of stockholders or to nominate candidates for election as directors at a meeting of stockholders must provide notice in writing in a timely manner, and also specify requirements as to the form and content of a stockholder's notice;
- restrict the forum for certain litigation against us to Delaware;
- do not provide for cumulative voting rights (therefore allowing the holders of a majority of the shares of common stock entitled to vote in any election of directors to elect all of the directors standing for election);
- provide that special meetings of our stockholders may be called only by the chairman of the board, our chief executive officer or the board of directors pursuant to a resolution adopted by a majority of the total number of authorized directors; and
- provide that stockholders will be permitted to amend our amended and restated bylaws only upon receiving at least 66 $^{2}/_{3}$% of the votes entitled to be cast by holders of all outstanding shares then entitled to vote generally in the election of directors, voting together as a single class.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which generally prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any "interested" stockholder for a period of three years following the date on which the stockholder became an "interested" stockholder.

Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware is the sole and exclusive forum for substantially all disputes between us and our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers or employees.

Our amended and restated certificate of incorporation provides that, unless we consent to the selection of an alternative forum, the Court of Chancery of the State of Delaware is the sole and exclusive forum for (1) any derivative action or proceeding brought on our behalf, (2) any action asserting a claim of breach of fiduciary duty owed by any of our directors, officers or other employees to us or to our stockholders, (3) any action asserting a claim arising pursuant to the Delaware General Corporation Law or (4) any action asserting a claim governed by the internal affairs doctrine. The choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits against us and our directors, officers and other employees. Alternatively, if a court were to find the choice of forum provision contained in our amended and restated certificate of incorporation to be

54

Table of Contents

inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could harm our business, operating results and financial condition.

We have never paid cash dividends and do not intend to pay dividends for the foreseeable future.

We have never declared or paid any cash dividends on our common stock. We currently intend to retain any future earnings and do not expect to pay any dividends in the foreseeable future. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to applicable laws, and will depend on a number of factors, including our financial condition, results of operations, capital requirements, contractual restrictions, general business conditions and other factors that our board of directors may deem relevant. In addition, our New Revolving Credit Facility prohibits us and our subsidiaries from, among other things, paying any dividends or making any other distribution or payment on account of our common stock. Accordingly, holders of our common stock must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments.

Our directors, executive officers and significant stockholders, who hold approximately 24% of the voting power of our outstanding common stock, have substantial control over us and could delay or prevent a change in corporate control.

As of September 30, 2016, our directors, executive officers and holders of more than 5% of our common stock, together with their affiliates, beneficially owned, in the aggregate, approximately 24% of our outstanding common stock. As a result, these stockholders, acting together, have the ability to substantially influence the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, consolidation or sale of all or substantially all of our assets. In addition, these stockholders, acting together, have the ability to substantially influence the management and affairs of our company. Accordingly, this concentration of ownership might decrease the market price of our common stock by:

- delaying, deferring or preventing a change in control of Five9;
- impeding a merger, consolidation, takeover or other business combination involving us; or
- discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of Five9.

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

Not applicable.

ITEM 3. Defaults Upon Senior Securities

None.

Table of Contents

ITEM 4. Mine Safety Disclosures
Not applicable.

ITEM 5. Other Information
None.

Table of Contents

ITEM 6. Exhibits

Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation of Five9, Inc. (filed as Exhibit 3.2 to the Company's Current Report on Form 8-K filed with the SEC on April 10, 2014 (File No. 001-36383) and incorporated by reference herein).
3.2	Amended and Restated Bylaws of Five9, Inc. (filed as Exhibit 3.1 to the Company's Current Report on Form 8-K filed with the SEC on April 10, 2014 (File No. 001-36383) and incorporated by reference herein).
10.1	Loan and Security Agreement, dated August 1, 2016, by and among Five9, Inc., the lenders party thereto and City National Bank, as agent for such lenders (filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on August 3, 2016 (File No. 001-36383) and incorporated by reference herein).
31.1*	Certification of Chief Executive Officer of Five9, Inc. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer of Five9, Inc. Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Chief Executive Officer and Chief Financial Officer of Five9, Inc. Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Schema Linkbase Document
101.CAL*	XBRL Taxonomy Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Definition Linkbase Document
101.LAB*	XBRL Taxonomy Labels Linkbase Document
101.PRE*	XBRL Taxonomy Presentation Linkbase Document

* Filed herewith.
** Furnished herewith.

Table of Contents

SIGNATURES

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

Five9, Inc.

Date: November 1, 2016 By: /s/ Michael Burkland
Michael Burkland
Chief Executive Officer and President
(Duly Authorized Officer)

Date: November 1, 2016 By: /s/ Barry Zwarenstein
Barry Zwarenstein
Chief Financial Officer
(Principal Financial Officer)