EGAIN Corp
Form 10-K
September 13, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended June 30, 2018

or

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

For the transition period from to

Commission File Number: 001-35314

eGain Corporation

(Exact name of registrant as specified in its charter)

Delaware	77-0466366
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1252 Borregas Avenue

Sunnyvale, California 94089

(Address of principal executive offices, including zip code)

(408) 636-4500

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.001 per share	Nasdaq Capital Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates (based on the closing price on the Nasdaq Capital Market) on December 31, 2017, was approximately $91.3 million. For purposes of the foregoing calculation only, the registrant has included in the shares owned by affiliates the beneficial ownership of voting and non-voting common equity of officers and directors, and affiliated entities, of the registrant and members of their families. Such inclusion shall not be construed as an admission that any such person is an affiliate for any other purpose.

There were 27,706,077 shares of the Registrant’s Common Stock $0.001 par value, outstanding on September 11, 2018.

DOCUMENTS INCORPORATED BY REFERENCE

Items 10 (as to directors), 11, 12, 13 and 14 of Part III incorporate by reference information from the registrant’s proxy statement to be filed with the Securities and Exchange Commission in connection with the solicitation of proxies for the registrant’s 2018 Annual Meeting of Stockholders.

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eGAIN CORPORATION

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PART I

ITEM 1.BUSINESS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of the words such as “anticipates,” “believes,” “continue,” “could,” “would,” “estimates,” “expects,” “intends,” “may,” “might,” “plans,” “potential,” “should,” or expressions or the negative of those terms. The forward-looking statements include, but are not limited to, statements regarding: the effect of changes in macroeconomic factors beyond our control; our hybrid revenue model and its potential impact on our total revenue; our ability to predict subscription renewals or upgrade rates; our lengthy sales cycles and the difficulty in predicting timing of sales or delays; competition in the markets in which we do business and our competitive advantages; our expectations regarding the composition of our customers and the result of a loss of a significant customer; our beliefs regarding our prospects for our business; the adequacy of our capital resources and our ability to raise additional financing; the effect of our failure to comply with our obligations under our Credit Agreement; the development and expansion of our strategic and third party distribution partnerships and relationships with systems integrators; legal liability or the effect of negative publicity for the services provided to consumers through our technology platforms; our ability to compete; the operational integrity and maintenance of our systems; the effect of unauthorized access to a customer’s data or our data or our IT systems and cybersecurity attacks; the uncertainty of demand for our products; our beliefs regarding the attributes and anticipated customer benefits of our products; the actual mix in new business between subscription and license transactions; our ability to increase the profitability of our recurring products and services; our ability to increase revenue as a result of the increased investment in sales and marketing; our ability to hire additional personnel and retain key personnel; our ability to expand and improve our sales performance and marketing activities; our ability to manage our expenditures and estimate future expenses, revenue, and operational requirements; the effect of changes to management judgments and estimates; the impact of any modification to our pricing practices in the future; our beliefs regarding our international operations; our ability to timely adapt and comply with changing European regulatory and political environments; uncertainty relating to the implementation and effect of Brexit; the effect of recent changes in U.S. tax legislation; our inability to successfully detect weaknesses or errors in our internal controls; our ability to take adequate precautions against claims or lawsuits made by third parties, including alleged infringement of proprietary rights; the potential impact of foreign currency fluctuations; the impact of accounting pronouncements and our critical accounting policies, judgments, estimates, models and assumptions on our financial results; and our expectations with respect to revenue, cost of revenue, expenses and other financial metrics.

Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expected. These risks and uncertainties include, but are not limited to, those risks discussed in Item 1A “Risk Factors” in this report, as well as our ability to manage our business plans, strategies and outlooks and any business-related forecasts or projections; our ability to effectively implement and improve our current products; our ability to innovate and respond to rapid technological change and competitive challenges; customer acceptance of our existing and future products; the impact of new legislation or regulations, or of judicial decisions, on our business; legal and regulatory uncertainties and other risks related to protection of our intellectual property assets; our ability to compete against third parties; the success of our partnerships; our ability to obtain capital when needed; the economic environment; our history of operating losses; our ability to manage future growth; the market price of our common stock; and foreign currency fluctuations. These forward looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to update any forward looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

All references to “eGain”, the “Company”, “our”, “we” or “us” mean eGain Corporation and its subsidiaries, except where it is clear from the context that such terms mean only this parent company and excludes subsidiaries.

eGain and the eGain® are trademarks of eGain Corporation. We also refer to trademarks of other corporations and organizations in this report.

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Overview

eGain is an innovative software-as-a service (SaaS) provider of customer engagement solutions in a digital world, with operations in the US, UK and India. Business-to-Consumer (B2C) brands quickly operationalize customer engagement strategy on our feature rich, comprehensive, and open platform to optimize experience for Agents, Businesses, and Customers. Connected artificial intelligence (AI), knowledge and analytics capabilities automate self-service across touch points and augment a digital-first, omnichannel agent desktop to reduce service cost, increase upsell, and improve business agility. Hundreds of customers around the world, primarily in financial services, telco, retail, government, healthcare and utilities, rely on eGain to provide a unified customer engagement hub.

In fiscal year 2017, we completed our transition from a hybrid model where we sold both SaaS and perpetual license solutions to a SaaS only business model (SaaS Transition). Today we only sell SaaS to new clients and are actively migrating our remaining perpetual license clients to SaaS. As we continue to migrate our legacy perpetual license clients to SaaS, we expect our non-SaaS recurring revenue, primarily comprising annual maintenance and support fees for legacy perpetual license clients, to continue to decline.

Our go-forward SaaS business model affords us recurring revenue visibility and more predictability. Our SaaS clients adopt our product innovation much faster in the perpetual license model and enjoy better service levels. Finally, we believe SaaS clients enjoy up to 50% faster time to value from their eGain investment.

Industry Background

Introduction

Traditional CRM tools do not serve the needs of the digital world because they were designed primarily as systems of record to capture, view, and report on customer data in a phone-centric environment. They do not offer rich applications to engage customers across digital-first touch points nor escalate with full context across self-service to agent assistance. They view knowledge management as document management (a monolithic content model that struggles in the personalized, media-rich, and content-heavy digital world). In the CRM world, agents are presumed to have a high capacity to retain and update relevant knowhow across complex product portfolios in their head (with extensive training and retraining). Finally, in-band process guidance for self-service and agent assistance are foreign to the traditional CRM world. Agents struggle with no guidance in that world; they just get lost with data on their screens. The reality of contact centers today is that we believe agents ignore 90% of available data on their screens – most of it hidden in multiple tabs – as they merely refer to post-it notes or internal chat sessions to find the right answer for a customer. It is time for change.

Digital Economy Demands Modern Software

In a world selling commoditized products to information-rich customers short on time, smart customer engagement reduces cognitive effort. And easy customer engagements build sticky brand and boost profit. As a result, businesses are actively seeking digital-first, modern software platforms to layer on top of their traditional systems of record like CRM. These platforms must be agile, comprehensive, scalable, and cost-effective to help automate customer self-service, augment agent productivity and orchestrate contact center operation in an omnichannel environment.

AI-powered Customer Engagement Automation

Energized in the digital world by big-data, cloud-computing and open-source technologies, AI and Machine Learning can deliver transformational value when effectively combined with domain expertise and complementary technologies like knowledge, analytics, and digital. In customer engagement, the ultimate goal is automation delivered on a platform that combines these powerful capabilities in a purpose-built way. The pressing challenge for businesses is to separate the wheat from the chaff. In the face of intense marketing from hundreds of providers – from IBM on the high end to countless startups – businesses now demand proof at scale, no-risk trials in a production setting, and outcome-based pricing tied to business-relevant metrics.

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Contact Centers are the Battleground

Contact centers offer a significant opportunity to automate human effort in B2C businesses. Globally, there are more than 10 million contact center agents. Even as digital technologies help improve self-service, time-starved customers faced with sophisticated, connected products generate stubbornly high levels of request for human assistance. The possibility of reducing significant headcount expense through automation is compelling for businesses. Furthermore, contact centers worldwide are undergoing a technology refresh cycle from on-premise voice-centric models to cloud-based omnichannel platforms. This transition affords the opportunity to reimagine the traditional centralized, phone-based contact handling operations and move toward much greater automation of customer engagement, fueled by AI and digital technologies.

Customer Engagement Automation is a Large, Growing Market

Businesses and organizations of all sizes are investing heavily in digital transformation. According to a preeminent strategy firm, customer engagement is the #1 area of investment in digital transformation. Ease of innovation in cloud and a growing API economy present ever more exciting capability dots for enterprise to connect and operate. This is both an opportunity and a challenge. A premier IT analyst firm estimates that by 2022 approximately 72% of all customer interactions will involve emerging technology such as machine-learning applications, chatbots or mobile messaging compared to approximately 11% in 2017. To harness these disruptive and novel capabilities, businesses are looking toward innovative platform providers with proof at scale to deliver a solution.

The eGain Approach and Benefits

What Customers Want

Technology acceleration notwithstanding, human needs for customer engagement and service change very slowly. What customers want is help in three categories: information, transaction, and situational. And any given customer contact can move across these needs as the conversation develops. Therefore, it is critical that an effective solution address these three types of interactions seamlessly and with context - accounting for machine-human hand-offs, channel switching, multimodal interaction, and conversational pause-and-resume. In each of these interactions, customers increasingly want to be guided, even anticipated, because time efficiency is their #1 goal after a correct answer is their biggest hurdle to a good experience, according to analyst surveys and our own research.

The eGain Solution

eGain offers a comprehensive, unified cloud software solution to automate, augment and orchestrate customer engagement in a digital-first omnichannel world. Our feature rich portfolio of applications empowers businesses to holistically, flexibly, and continuously optimize the experience for agents, business and customers. Our solution experts and partners guide clients on a customer engagement transformation journey using an agile, strategy-aligned set of sprints to activate waves of cooperating capabilities in phases. Each sprint is measured with our analytics to surface business value, justifying the next phase of investment.

Digital-first, Omnichannel Desktop

First, our solution offers comprehensive, scalable capabilities for digital-first, omnichannel interaction within a modern, purpose-built desktop. Rich, out of the box applications help agents efficiently interact with customers using messaging, SMS, chat, email, social media, phone, video, fax, and letter to enable connected customer journeys, offering service across all touch points. Our enterprise-grade digital engagement capabilities are proven at scale with clients such as a leading telco that annually serves over 12 million digital customer interactions with over five thousand agents on a 24x7 basis.

AI and Knowledge Applications

Next, our solution offers powerful AI and Knowledge applications for virtual assistance for customers and agents. These applications enable businesses to centralize knowledge, policies, procedures, and best-practices, while delivering guided, personalized solutions to customers and agents. These applications are designed to ensure that all agents in an organization

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can effectively handle all types of contacts, regardless of product or procedure. Consistent and correct responses across all touchpoints (operated by the previous layer of omnichannel applications) significantly improve customer satisfaction even as first contact resolution rates surge and an agent's time to competency drops. Our AI and Knowledge applications deliver compelling value through large-scale self-service automation. For instance, one of our healthcare clients serves over 25 million requests every year with web self-service. Another client improved customer NPS scores by 20 points and boosted First Contact Resolution by 23% using our AI and Knowledge capabilities in a ten thousand agent customer service operation.

Analytics and Machine Learning Applications

Our powerful analytics capability enables clients to measure, manage and orchestrate their omnichannel service operations. In addition, our recently announced machine learning service helps clients generate product improvement and customer preference insights from all of their customer conversation data and also identify opportunities to automate more processes.

Open, secure APIs and pre-built, certified third-party connectors

Our open, secure platform APIs are available to clients and partners to extend and enhance our solutions and to integrate with enterprise assets and to enable a single view of the customer. Our deep, certified connectors into platforms such as those of Avaya, Amazon.com, Cisco and Salesforce.com enable our clients to leverage their existing systems of record and communication, while building their system of engagement on the eGain platform.

Compelling Benefits

We believe our solution delivers transformational value as clients develop their modern customer engagement capabilities on our platform. Specifically, our solutions allow clients to:

- enhance customer experience with digital-first, omnichannel service.
- reduce operating costs through self-service automation, improved first contact resolution, and compressed agent time-to-competence.
- ensure compliance with regulations, policies, procedures, and best practices even as clients expand their product portfolio and serviced customer segments. This benefit is particularly sought after in regulated sectors like financial services and healthcare, as well as government.
- gain rich, primary insights to enhance products and design new offerings. Analyzing and learning from customer conversations provides a unique tool to businesses looking for hyper-targeting their customers with offerings that

defy commoditization by delivering better consumption and service experience.

Competitive Strengths

Comprehensive omnichannel platform with rich apps and purpose-built APIs

The eGain solution is a comprehensive omnichannel solution for the customer engagement market, with AI and Knowledge at its core. We unlock the full power of our cloud platform with extensive APIs through a developer portal to enable digital engagement, knowledge management, and decision support capabilities for clients and partners in a way that is unique in the market.

Enterprise-grade, secure cloud service with differentiated offerings

Our cloud offering is secure, scalable and offers unique capabilities. With respect to security and certification, we offer FEDRAMP, PCI, HIPPA, HiTrust and GDPR certification. Two of the largest federal tax services, one in North America and the other in Europe, use eGain solutions served from the eGain Cloud. Furthermore, we offer an AlwaysOn capability for businesses who cannot afford to be down at any time, day or night, for “scheduled maintenance downtime.” Finally, we offer credits in the event of non-adherence to contracted service levels.

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Transformative value delivered at scale across large, diversified customer base

Our solution delivers transformative value at scale today across a large, diversified customer base. We believe that our understanding of the customer need and our ability to fulfil it at scale and with enterprise-grade sophistication is unmatched. From sixty thousand agents at a healthcare client using our solution on a 24x7 basis to a P&C insurer with fifteen thousand contact center advisors and thirty-thousand field agents, we are the preferred choice for the large brands looking to automate customer engagement.

Innovation at the core drives an easy consumption model

For over twenty years we have anticipated technology and market trends and sought to consistently stay ahead of them. We anticipated the need for AI in customer service in 2000, and we developed an omnichannel customer engagement hub over a decade ago. With a relentless focus on the customer engagement automation market, we continue to add capabilities designed to enhance our client's investment in eGain. Recently, we added new customer messaging capabilities via Apple Business Chat, Facebook Messenger, and SMS. Also, we launched our new VA 3.0, a third-generation virtual assistant powered by AI, Machine Learning, and Knowledge that is seamlessly connected with the omnichannel assistance capabilities of the eGain platform. This ability to connect dots quickly across new and existing technology capabilities, within the eGain platform and outside, distinguishes us when presenting to clients looking for quick value on a platform that can handle their future needs.

Not only do we seek to innovate more quickly than others, we stand behind our claim with a unique Try+Buy™ offer – a 30-day guided production pilot in the eGain Cloud with no strings attached. Along similar lines, we recently launched another exciting offer, "AI Value in 30 days," to help clients make better choices as they invest in AI technologies to automate their customer engagement operation.

Leveraged go-to-market strategy with a growing partner ecosystem

We take our solutions to market through a partner-leveraged enterprise sales model. Our enterprise sales team works closely with our channel managers to help partners qualify and sell. Our key channel partner today is Cisco. Through its partner ecosystem and direct sales network, we resell cloud-based, eGain-branded solutions in our target geographies of North America and Europe. Given the reach of Cisco and its partners in the enterprise, we see growing opportunities in this ecosystem.

In the second half of fiscal 2018, we also announced a partnership with Avaya as part of its AI Connect program. This recent engagement is beginning to result in opportunities. Also, in late fiscal 2018, we announced a deep integration

with Amazon Connect, a disruptive cloud-based contact center proposition. Finally, at our Digital+AI Day in London in May 2018, we announced an eGain developer portal for partners and clients to integrate with and add value to the eGain platform.

Customers

We serve a worldwide customer base across a wide variety of industry sectors, including healthcare, retail, telecommunications, financial services, insurance, outsourced services, technology, utilities, government, manufacturing and consumer electronics. Our product is sold primarily to large B2C enterprises, which we define as enterprises with over $500 million in annual revenue. For fiscal year 2018, domestic and international revenue accounted for 52% and 48% of total revenue, respectively, compared to 49% and 51%, and 50% and 50%, for fiscal years 2017 and 2016, respectively.

Our largest customer, Cisco Systems, Inc., accounted for 16% of total revenue in fiscal year 2018 and 13% of total revenue in fiscal year 2017. Our two largest customers, Cisco Systems, Inc. and State Farm Insurance Company, accounted for 14% and 10%, respectively, of total revenue in fiscal year 2016.

Competition

We compete with other application software vendors including Genesys Telecommunications, LivePerson, Inc., and Moxie Software, Inc. In addition, we face actual or potential competition from larger software companies such as Microsoft Corporation, Oracle Corporation, Salesforce.com, Inc., and Verint KANA that may attempt to sell customer engagement

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software to their installed base. We also compete with internally developed applications within large enterprises. Finally, we face, or expect to face, competition from software vendors who may develop toolsets and products that allow customers to build new applications that run on the customers' infrastructure or as hosted services. The market that we compete in is highly competitive and some of our competitors may have longer operating histories, greater economies of scale, greater financial resources, greater engineering and technical resources, greater sales and marketing resources, stronger strategic partnerships and distribution channels, larger user bases, products and services with different functions and feature sets and greater brand recognition than we have.

We believe the principal competitive factors in our market include the following:

- proven track record of customer success;
- speed and ease of implementation;
- product functionality;
- financial stability and viability of the vendor;
- product adoption;
- ease of use and rates of user adoption;
- low total cost of ownership and demonstrable cost-effective benefits for customers;
- performance, security, scalability, flexibility and reliability of the service;
- whether the software is delivered via the cloud or on-premises;
- ease of integration with existing applications;
- quality of customer support;
- availability and quality of implementation, consulting and training services; and
- vendor reputation and brand awareness.

Growth Strategy

We intend to scale our business by executing the following programs.

Migrate legacy on-premise customers to eGain Cloud

Since we transitioned our business to SaaS, we have continued to actively migrate legacy on-premise customers to the eGain Cloud. We offer an attractive proposition to our on-premise customers to move to the eGain Cloud where we subsidize the services cost in migrating them to the eGain Cloud in exchange for their multi-year commitment to the eGain Cloud. At the end of fiscal 2018, we still had quarterly support revenue from a number of our on-premise customers. We expect to migrate most of these customers, subject to typical attrition, to the eGain Cloud over the next two years.

Land and Expand in the enterprise

With the progress we have made in customer success over recent periods, we see a replicable pattern emerging: land enterprise logos with a potentially limited footprint in one business unit, demonstrate business value, and then actively expand in the enterprise – activating more of our capabilities and rolling out to multiple business units. Further, we see the opportunity to increase stickiness by integrating via our enhanced APIs with enterprise assets like enterprise collaboration platforms, CRM systems, transaction and billing, and content sources.

Develop new partner relationships

As a business today, we have an abundance of product solutions but limited distribution. We are well positioned to enable existing technology platforms with a strong installed customer base to enhance their proposition with AI-powered customer engagement solutions. We intend to continue to develop partnerships to grow our market share.

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Enter the mid-market

We ran a successful experiment in the US market in fiscal 2018 where we acquired new customers and followed up with rapid customer success that yielded add-on sales opportunities. Based on this success, we plan to increase our investment in the mid-market (sub 100 contact center seats) in the US in the 2019 fiscal year.

Maintain platform innovation leadership

Innovation is in our DNA and we plan to continue to build on our strength. We plan to invest in easy-to-consume innovation with more compelling user experiences and more extensive platform APIs, so that in working with partners we can deliver differentiated and sustained value to clients.

Selectively pursue acquisitions

Historically, we have from time to time pursued inorganic strategies to strengthen our product portfolio. Our most recent was in 2014 when we acquired Exony Limited, a provider of advanced contact analytics software. Moving forward, we will continue to look for possible combinations that we believe will deliver compelling value to our clients.

Sales and Marketing

Sales Strategy

Our sales strategy is to pursue targeted accounts, mostly B2C enterprises, through a combination of our direct sales force and partners. We target our sales efforts at enterprise companies. These enterprises have thousands of customer service agents in their contact centers and, in the aggregate, communicate with billions of customers each year. We attempt to utilize thought leadership and other marketing events to demonstrate our leadership position in the cloud-based customer engagement software market and highlight our successes with existing customers. Our North American direct sales organization is based at our corporate headquarters in Sunnyvale, California, with field sales presences throughout the United States. Internationally, we have offices in India and the United Kingdom.

The direct sales force is organized into teams that include field sales representatives and sales consultants. Our direct sales force is complemented by lead generation representatives and sales development representatives.

We also complement our direct sales force with reseller and sales alliances. We believe we are able to leverage additional sales, marketing and deployment capabilities through these alliances.

Marketing and Partner Strategy

Our marketing strategy is to build our brand around innovative and robust products trusted by leading enterprises. Our marketing organization focuses on public relations, analyst relations, marketing communications and demand generation. We employ a wide range of marketing avenues to deliver our message, including print and Internet advertising, targeted electronic and postal mailing, email newsletters, and a variety of trade shows, seminars, webinars, and interest groups.

Our marketing group also produces sales tools, including product collateral, customer case studies, demonstrations, presentations, and competitive analyses. In addition, the group performs market analyses and customer reviews to identify and develop key partnership opportunities and product capabilities.

We believe that our partners help extend the breadth and depth of our product offerings, drive market penetration, and augment our professional service capabilities. We believe these relationships are important to delivering successful, integrated products and services to our customers, and scaling our business. Our partner portal, EcoNet™, enables us to provide comprehensive sales, support and services information for channel partners, while enabling them to collaborate with one another through an online forum. Partner enablement is also a key focus area for our consulting and training teams.

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As of June 30, 2018, we had 69 employees engaged in worldwide sales and marketing activities.

Subscription Services

Our subscription services provide customers with access to our software within a cloud-based information technology (IT)

environment that we manage and offer on a subscription basis. These subscription services allow our customers to benefit from our latest cloud innovations and to reduce infrastructure, installation and ongoing administration requirements. We also offer cloud-based services to existing customers who previously purchased licenses to our software to access that software within a cloud-based IT environment that we manage. This reduces infrastructure and ongoing administration requirements as an alternative to their on- premises deployment of our software. We generally offer these services via 36 month contracts with pricing based on the number of agents and/or customer service sessions.

Consulting and Education

Our worldwide professional services organization provides consulting and education services designed to facilitate customer success and build customer loyalty.

- Consulting Services. Our consulting services group offers rapid implementation services, custom solution development, and systems integration services. Consultants work with customers to understand their specific requirements, analyze their business needs, and implement integrated solutions. We provide these services independently or in partnership with systems integrators who have developed consulting expertise on our platform.
- Education Services. Our education services group provides a comprehensive set of basic and customized training programs to our customers and partners in addition to online tutorial modules for ongoing refresher courses. Training programs are offered either in-person at the customer site, or at one of our worldwide training centers.

As of June 30, 2018, we had 96 professionals providing worldwide services for systems installation, solutions development, application management, and education.

Customer Support

We offer a comprehensive collection of support services designed to rapidly respond to inquiries. Our technical support services are available to customers worldwide under maintenance and support agreements. The customer success team uses eGain's own software suite to provide world-class service to all our customers through support centers located in California, the United Kingdom, and India.

As of June 30, 2018, there were 64 employees engaged in worldwide customer support services and 41 employees engaged in worldwide cloud services and maintenance support.

Research and Development

The market for our products changes rapidly and is characterized by evolving industry standards, swift changes in customer requirements, and frequent new product introductions and enhancements. We believe that strong product development capabilities are essential to our strategy of maintaining technology leadership. This includes enhancing current technology, providing excellent quality, performance, and functionality, as well as developing additional applications, and maintaining the competitiveness of our product and service offerings.

We continuously analyze market and customer requirements and evaluate external technology that we believe will enhance our competitiveness, increase our lifetime customer value or expand our target market. As a result of this process, we acquired Exony Limited, a leader in enterprise contact center analytics software, in August 2014.

As of June 30, 2018, we had 136 employees engaged in worldwide product development activities. We spent approximately $14.7 million, $13.8 million and $16.1 million on research and development in fiscal years 2018, 2017 and 2016, respectively.

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Intellectual Property

We regard our intellectual property as critical to our success. We rely on intellectual property and other laws, in addition to confidentiality procedures and licensing arrangements, to protect the proprietary aspects of our technology and business.

As of June 30, 2018, we had 11 issued patents in the United States. In addition, we have a number of pending patent applications in the United States, including one provisional filing and several non provisional filings. Our issued U.S. patents expire at various times between 2029 and 2035.

We continually assess the propriety of seeking intellectual property protection for those aspects of our technology that we believe constitute innovations providing significant competitive advantages. Future applications may or may not receive the issuance of valid patents or registered trademarks.

We routinely require our employees, customers, and potential business partners to enter into confidentiality and nondisclosure agreements before we will disclose any sensitive aspects of our products, technology, or business plans. In addition, we require employees to agree to surrender to us any proprietary information, inventions or other intellectual property they generate or come to possess while employed by us. Despite our efforts to protect our proprietary rights through confidentiality and license agreements, unauthorized parties may attempt to copy or otherwise obtain and use our products or technology. These precautions may not prevent misappropriation or infringement of our intellectual property. In addition, some of our license agreements with certain customers and partners require us to place the source code for our products into escrow. These agreements typically provide that some party will have a limited, non-exclusive right to access and use this code as authorized by the license agreement if there is a bankruptcy proceeding instituted by or against us, or if we materially breach a contractual commitment to provide support and maintenance to the party.

Employees

As of June 30, 2018, we had 464 full-time employees, of which 136 were in product development, 201 in services and support, 69 in sales and marketing, and 58 in finance and administration.

None of our employees are covered by collective bargaining agreements. While we believe our relations with our employees are good, our future performance depends largely upon the continued service of our key technical, sales and marketing, and senior management personnel, none of whom are bound by employment agreements requiring service for a defined period of time.

Available Information

We were incorporated in Delaware in September 1997, and our website is located at www.egain.com. We make available free of charge on our website our annual reports on Form 10 K, quarterly reports on Form 10 Q, current reports on Form 8 K and amendments to those reports, as soon as reasonably practicable after we electronically file or furnish such materials to the Securities and Exchange Commission. Our website and the information contained therein or connected thereto are not intended to be incorporated into this Annual Report on Form 10 K.

ITEM 1A. RISK FACTORS

The risks and uncertainties described below are not the only ones facing us. Other events that we do not currently anticipate or that we currently deem immaterial also may affect our results of operations, cash flows and financial condition.

Our business is influenced by a range of factors that are beyond our control and that we have no comparative advantage in forecasting. These include:

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- general economic and business conditions;
- currency exchange rate fluctuations;
- the overall demand for enterprise software and services;
- customer acceptance of cloud-based solutions;

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- governmental budgetary constraints or shifts in government spending priorities; and
- general political developments.

The global economic climate continues to influence our business. This includes items such as, a general tightening in the credit markets, lower levels of liquidity, increases in the rates of default and bankruptcy, and extreme volatility in credit, equity and fixed income markets. These macroeconomic developments negatively affected, and could continue to negatively affect, our business, operating results or financial condition which, in turn, could adversely affect our stock price. A general weakening of, and related declining corporate confidence in, the global economy or the curtailment in government or corporate spending could cause current or potential customers to reduce their technology budgets or be unable to fund software or services purchases, which could cause customers to delay, decrease or cancel purchases of our products and services or cause customers not to pay us or to delay paying us for previously purchased products and services.

Our revenue and operating results have fluctuated in the past and are likely to fluctuate in the future, and because we recognize revenue from subscriptions over a period of time, downturns in revenue may not be immediately reflected in our operating results.

Because we recognize recurring revenue and maintenance revenue ratably over the terms of the related subscription agreements and maintenance support agreements, most of our revenue each quarter results from recognition of deferred revenue related to agreements entered into during previous quarters. Consequently, declines in new or renewed subscription agreements and maintenance agreements that occur in one quarter will largely be felt in future quarters, both because we may be unable to generate sufficient new revenue to offset the decline and because we may be unable to adjust our operating costs and capital expenditures to align with the changes in revenue. In addition, our subscription model makes it more difficult for us to increase our revenue rapidly in any period, because revenue from new customers must be recognized over the applicable subscription term. It is difficult to forecast the expediency of the transition of our license customers to our cloud delivery model. Accordingly, we believe that period-to-period comparisons of our results of operations should not be relied upon as definitive indicators of future performance.

Other factors that may cause our revenue and operating results to fluctuate include:

- timing of customer budget cycles;
- the priority our customers place on our products compared to other business investments;
- size, timing and contract terms of new customer contracts, and unpredictable and often lengthy sales cycles;
- reduced renewals;
- competitive factors, including new product introductions, upgrades and discounted pricing or special payment terms offered by our competitors, as well as strategic actions by us or our competitors, such as acquisitions, divestitures, spin-offs, joint ventures, strategic investments or changes in business strategy;
- technical difficulties, errors or service interruptions in our solutions that may cause customer dissatisfaction with our solutions;
- consolidation among our customers, which may alter their buying patterns, or business failures that may reduce demand for our solutions;
- operating expenses associated with expansion of our sales force or business, and our product development efforts;
- cost, timing and management efforts related to the introduction of new features to our solutions;
- our ability to obtain, maintain and protect our intellectual property rights and adequately safeguard the information imported to our solutions or otherwise provided to us by our customers; and
- extraordinary expenses such as impairment charges, litigation or other payments related to settlement of disputes.

Any of these developments may adversely affect our revenue, operating results and financial condition. Furthermore, we maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. In such cases, we may be required to defer revenue recognition on sales to affected customers. In the

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future, we may have to record additional reserves or write-offs, or defer revenue on sales transactions, which could negatively impact our financial results.

If we are unable to increase the profitability of our recurring revenue products and services, if we experience significant customer attrition, or if we are required to defer recognition of revenue, our operating results could be adversely affected.

We have invested, and expect to continue to invest, substantial resources to expand, market, and implement and refine our recurring revenue products and services offerings. Our business model shift to recurring revenue, and our subscription services in particular, has generally generated much lower gross margins than our traditional perpetual license sales. If we are unable to increase the volume of our subscription business to offset the lower margins, we may not be able to achieve sustained profitability.

Factors that could harm our ability to improve our gross margins, which may affect our operating profitability, include:

- increased costs to license and maintain third party software embedded in our software applications or the cost to create or substitute such third party software if it can no longer be licensed on commercially reasonable terms;
- our inability to maintain or increase the prices customers pay for our products and services based on competitive pricing pressures and general economic conditions limiting customer demand;
- increased cost of third party services providers, including data centers for our cloud operations and professional services contractors performing implementation and technical support services to cloud customers;
- customer contractual requirements that delay revenue recognition until customer implementations commence production operations or customer-specific requirements are met;
- significant attrition as customers decide for their own economic or other reasons to not renew their subscription contracts when they are up for renewal negatively impacting the efficiency of our data centers and leading to the costs being spread over fewer customers negatively impacting gross margin; and
- the inability to implement, or delays in implementing, technology-based efficiencies and efforts to streamline and consolidate processes to reduce operating costs.

We cannot accurately predict subscription renewal rates and the impact these rates may have on our future revenue and operating results.

Even though our subscription contracts are typically structured for auto-renewals, we do allow our customers to elect not to renew their subscriptions for our service after the expiration of their initial subscription period, which is typically 12 to 36 months, and some customers have elected not to renew. In addition, our customers may choose to renew for fewer subscriptions (in quantity or products) or renew for shorter contract lengths. We cannot accurately predict renewal rates given our varied customer base of enterprise and small and medium size business customers and the number of multiyear subscription contracts. Our renewal rates may decline or fluctuate as a result of a number of factors, including customer dissatisfaction with our service, decreases in customers' spending levels, decreases in the number of users at our customers, pricing changes and general economic conditions. If our customers do not renew their subscriptions for our service or reduce the number of paying subscriptions at the time of renewal, our revenue will decline and our business will suffer.

Our future success also depends in part on our ability to sell additional features and services, more subscriptions or enhanced editions of our service to our current customers. This may also require increasingly sophisticated and costly sales efforts that are targeted at senior management. Similarly, the rate at which our customers purchase new or enhanced services depends on a number of factors, including general economic conditions and that our customers do not react negatively to any price changes related to these additional features and services. If our efforts to upsell to our customers are not successful and negative reaction occurs, our business may suffer.

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Our credit agreement contains restrictive and financial covenants that may limit our operational flexibility. Furthermore, if we default on our obligations under the credit agreement, our operations may be interrupted and our business and financial results could be adversely affected.

In November 2014, we entered into a credit agreement (Credit Agreement) with Wells Fargo Bank, National Association (Wells Fargo), under which Wells Fargo agreed to provide a term loan in the amount of $10.0 million and revolving loans to us in an amount not to exceed $10.0 million (Revolving Loans). In September 2015, we increased the maximum borrowing amount of the Revolving Loans to $15.0 million. The Credit Agreement contains a number of restrictive covenants, and its terms may restrict our current and future operations, including:

- affecting our flexibility to plan for, or react to, changes in our business and industry conditions;
- affecting our ability to use our cash flows, or obtain additional financing, for future working capital, capital expenditures, acquisitions or other general corporate purposes;
- placing us at a competitive disadvantage compared to our less leveraged competitors; and
- increasing our vulnerability to the impact of adverse economic and industry conditions.

In addition, if we fail to comply with the covenants or payment obligations specified in the Credit Agreement, we may trigger an event of default, in which case Wells Fargo would have the right to: (i) terminate its commitment to provide additional loans under the Credit Agreement, and (ii) declare all borrowings outstanding, together with accrued and unpaid interest and fees, to be immediately due and payable. In addition, Wells Fargo would have the right to proceed against the collateral under the Credit Agreement, which consists of substantially all our assets. If the debt under the Credit Agreement were to be accelerated, we may not have sufficient cash or be able to sell sufficient collateral to repay this debt, which would have an immediate material adverse effect on our business, results of operations and financial condition.

Our lengthy sales cycles and the difficulty in predicting timing of sales or delays may impair our operating results.

The long sales cycle for our products may cause license and subscription revenue and operating results to vary significantly from period to period. The sales cycle for our products can be six months or more and varies substantially from customer to customer. Because we sell complex and deeply integrated solutions, it can take many months of customer education to secure sales. Because our potential customers may evaluate our products before, if ever, executing definitive agreements, we may incur substantial expenses and spend significant management and legal effort in connection with a potential customer.

Our multi-product offering and the increasingly complex needs of our customers contribute to a longer and unpredictable sales cycle. Consequently, we often face difficulty predicting the quarter in which expected sales will actually occur. This contributes to the uncertainty and fluctuations in our future operating results. In particular, the corporate decision-making and approval process of our customers and potential customers has become more complicated. This has caused our average sales cycle to further increase and, in some cases, has prevented the closure of sales that we believed were likely to close.

Our ability to raise additional capital on acceptable terms in the future may limit our ability to grow our business and expand our operations.

Our working capital requirements in the foreseeable future are subject to numerous risks and will depend on a variety of factors. We may seek additional funding to finance our operations or should we make acquisitions. We may also need to secure additional financing due to unforeseen or unanticipated market conditions. We may try to raise additional funds through public or private financings, strategic relationships, or other arrangements. Such financing may be difficult to obtain on terms acceptable to us, if at all. If we raise additional funds through the issuance of equity or convertible securities, then the issuance could result in substantial dilution to existing stockholders. If we

raise additional funds through the issuance of debt securities or preferred stock, these new securities would have rights, preferences, and privileges senior to those of the holders of our common stock. The terms of these securities could impose restrictions on our operations.

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Because we depend on a relatively small number of customers for a substantial portion of our revenue, the loss of any of these customers or our failure to attract new significant customers could adversely impact our revenue and harm our business.

We have in the past and expect in the future to derive a substantial portion of our revenue from sales to a relatively small number of customers. The composition of these customers has varied in the past, and we expect that it will continue to vary over time. The loss of any significant customer or a decline in business with any significant customer would materially and adversely affect our financial condition and results of operations.

If we acquire companies or technologies, we may not realize the expected business benefits, the acquisitions could prove difficult to integrate, disrupt our business, dilute stockholder value and adversely affect our operations.

As part of our business strategy, we periodically make investments in, or acquisitions of, complementary businesses, joint ventures, services and technologies and intellectual property rights, and we expect that we will continue to make such investments and acquisitions in the future. In August 2014, we acquired Exony Ltd. Acquisitions and investments involve numerous risks, including:

- the potential failure to achieve the expected benefits of the combination or acquisition;
- difficulties in and the cost of integrating operations, technologies, services and personnel;
- diversion of financial and managerial resources from existing operations;
- risks of entering new markets in which we have little or no experience or where competitors may have stronger market positions;
- potential write-offs of acquired assets or investments, and potential financial and credit risks associated with acquired customers;
- potential loss of key employees;
- inability to generate sufficient revenue to offset acquisition or investment costs;
- the inability to maintain relationships with customers and partners of the acquired business;
- the difficulty of transitioning the acquired technology onto our existing platforms and maintaining the security standards consistent with our other services for such technology;
- potential unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into existing technology;
- negative impact to our results of operations because of the depreciation and amortization of amounts related to acquired intangible assets, fixed assets and deferred compensation, and the loss of acquired deferred revenue and unbilled deferred revenue;
- delays in customer purchases due to uncertainty related to any acquisition;
- the need to implement controls, procedures and policies at the acquired company;
- challenges caused by distance, language and cultural differences;
- in the case of foreign acquisitions, the challenges associated with integrating operations across different cultures and languages and any currency and regulatory risks associated with specific countries; and
- the tax effects of any such acquisitions.

We must compete successfully in our market segment.

The market for customer engagement software is intensely competitive. Other than product innovation and existing customer relationships, there are no substantial barriers to entry in this market, and established or new entities may enter this market in the future. While software internally developed by enterprises represents indirect competition, we also

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compete directly with packaged application software vendors, including Avaya, Inc., Genesys Telecommunications, LivePerson, Inc., and Moxie Software, Inc. In addition, we face actual or potential competition from larger software companies such as Microsoft Corporation, Oracle Corporation, Salesforce.com, Inc. and similar companies that may attempt to sell customer engagement software to their installed base.

We believe competition will continue to be fierce as current competitors increase the sophistication of their offerings and as new participants enter the market. Many of our current and potential competitors have longer operating histories, larger customer bases, broader brand recognition, and significantly greater financial, marketing and other resources. With more established and better-financed competitors, these companies may be able to undertake more extensive marketing campaigns, adopt more aggressive pricing policies, and make more attractive offers to businesses to induce them to use their products or services. If we are unable to compete successfully, our business will be adversely affected.

If we fail to expand and improve our sales performance and marketing activities, we may be unable to grow our business, negatively impacting our operating results and financial condition.

Expansion and growth of our business is dependent on our ability to expand our sales force and on the ability of our sales force to increase sales. If we are not able to effectively develop and maintain awareness of our products in a cost-effective manner, we may not achieve widespread acceptance of our existing and future products. This may result in a failure to expand and attract new customers and enhance relationships with existing customers. This may impede our efforts to improve operations in our other areas and may result in declines in the market price of our common stock.

Due to the complexity of our customer engagement hub platform and related products and services, we must utilize highly trained sales personnel to educate prospective customers regarding the use and benefits of our products and services as well as provide effective customer support. If we have turnover in our sales and marketing teams, we may not be able to successfully compete with our competitors, and our results of operations and financial condition may be harmed.

Our failure to develop and expand strategic and third party distribution channels would impede our revenue growth.

Our success and future growth depends in part upon the skills, experience, performance and continued service of our distribution partners, including software and hardware vendors and resellers. Our distribution partners engage with us in a number of ways, including assisting us to identify prospective customers, distributing our products in geographies where we do not have a physical presence and distributing our products where they are considered complementary to other third party products distributed by the partner. We believe that our future success depends in part upon our ability to develop and expand strategic, long-term and profitable partnerships and reseller relationships. If we are unable to do so, or if any existing or future distribution partners fail to successfully market, resell, implement or support our products for their customers, or if distribution partners represent multiple providers and devote greater resources to market, resell, implement and support competing products and services, our future revenue growth could be impeded. Our failure to develop and expand relationships with systems integrators could harm our business.

We sometimes rely on systems integrators to recommend our products to their customers and to install and support our products for their customers. We likewise depend on broad market acceptance by these system integrators of our product and service offerings. Our agreements generally do not prohibit competitive offerings and systems integrators may develop market or recommend software applications that compete with our products. Moreover, if these firms fail to implement our products successfully for their customers, we may not have the resources to implement our products on the schedule required by their customers. To the extent we devote resources to these relationships and the partnerships do not proceed as anticipated or provide revenue or other results as anticipated, our business may be

harmed. Once partnerships are forged, there can be no guarantee that such relationships will be renewed in the future or available on acceptable terms. If we lose strategic third party relationships, fail to renew or develop new relationships, or fail to fully exploit revenue opportunities within such relationships, our results of operations and future growth may suffer.

Our international operations involve various risks.

We derived 48% of our revenue from international sales for the fiscal year 2018 compared to 51% for the fiscal year 2017 and 50% for fiscal year 2016. In addition to those discussed elsewhere in this section, our international sales operations are subject to a number of specific risks, such as:

- general economic conditions in each country or region in which we do or plan to do business;
- foreign currency fluctuations and imposition of exchange controls;
- expenses associated with complying with differing technology standards and language translation issues;
- difficulty and costs in staffing and managing our international operations;
- difficulties in collecting accounts receivable and longer collection periods;
- health or similar issues, such as a pandemic or epidemic;
- various trade restrictions and tax consequences;
- hostilities in various parts of the world; and
- reduced intellectual property protections in some countries.

As of June 30, 2018, approximately 49% of our workforce was employed in India. Of our employees in India, 36% are allocated to research and development. Although the movement of certain operations internationally was principally motivated by cost cutting, the continued management of these remote operations requires significant management attention and financial resources that could adversely affect our operating performance. In addition, with the significant increase in the numbers of foreign businesses that have established operations in India, the competition to attract and retain employees there has increased significantly. As a result of the increased competition for skilled workers, we experienced increased compensation costs and expect these costs to increase in the future. Our reliance on our workforce in India makes us particularly susceptible to disruptions in the business environment in that region. In particular, sophisticated telecommunications links, high-speed data communications with other eGain offices and customers, and overall consistency and stability of our business infrastructure are vital to our day-to-day operations, and any impairment of such infrastructure will cause our financial condition and results to suffer. The maintenance of stable political relations between the United States, the European Union and India are also of great importance to our operations.

Any of these risks could have a significant impact on our product development, customer support, or professional services. To the extent the benefit of maintaining these operations abroad does not exceed the expense of establishing and maintaining such activities, our operating results and financial condition will suffer.

Difficulties in implementing our products could harm our revenue and margins.

We generally recognize license or subscription revenue from a customer sale when persuasive evidence of an arrangement exists, the product or access to the product has been delivered, the arrangement does not involve significant customization of the software, the license or subscription fee is fixed or determinable and collection of the fee is probable. If an arrangement requires significant customization or implementation services from us, recognition of the associated license or subscription and service revenue could be delayed. The timing of the commencement and completion of these services is subject to factors that may be beyond our control, as this process may require access to the customer’s facilities and coordination with the customer’s personnel after delivery of the software. In addition, customers could cancel or delay product implementations. Implementation typically involves working with sophisticated software, computing and communications systems. If we experience difficulties with implementation or do not meet project milestones in a timely manner, we could be obligated to devote more customer support, engineering and other resources to a particular project. Some customers may also require us to develop customized features or capabilities. If new or existing customers cancel or have difficulty deploying our products or require significant amounts of our professional services, support, or customized features, revenue recognition could be cancelled or further delayed and our costs could increase, causing increased variability in our operating results.

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Our reserves may be insufficient to cover receivables we are unable to collect.

We assume a certain level of credit risk with our customers in order to do business. Conditions affecting any of our customers could cause them to become unable or unwilling to pay us in a timely manner, or at all, for products or services we have already provided them. In the past, we have experienced collection delays from certain customers, and we cannot predict whether we will continue to experience similar or more severe delays in the future. Although we have established reserves to cover losses due to delays or inability to pay, there can be no assurance that such reserves will be sufficient to cover our losses. If losses due to delays or inability to pay are greater than our reserves, it could harm our business, operating results and financial condition.

We may be subject to legal liability and/or negative publicity for the services provided to consumers through our technology platforms.

Our technology platforms enable representatives of our customers as well as individual service providers to communicate with consumers and other persons seeking information or advice on the Internet. The law relating to the liability of online platform providers such as us for the activities of users of their online platforms is often challenged in the U.S. and internationally. We may be unable to prevent users of our technology platforms from providing negligent, unlawful or inappropriate advice, information or content through our technology platforms, or from behaving in an unlawful manner, and we may be subject to allegations of civil or criminal liability for negligent, fraudulent, unlawful or inappropriate activities carried out by users of our technology platforms.

Claims could be made against online services companies under both U.S. and foreign law such as fraud, defamation, libel, invasion of privacy, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated by users of our technology platforms. In addition, domestic and foreign legislation has been proposed that could prohibit or impose liability for the transmission over the Internet of certain types of information. Our defense of any of these actions could be costly and involve significant time and attention of our management and other resources.

The Digital Millennium Copyright Act, or DMCA, is intended, among other things, to reduce the liability of online service providers for listing or linking to third party web properties that include materials that infringe copyrights or rights of others. Additionally, portions of The Communications Decency Act, or CDA, are intended to provide statutory protections to online service providers who distribute third party content. A safe harbor for copyright infringement is also available under the DMCA to certain online service providers that provide specific services, if the providers take certain affirmative steps as set forth in the DMCA. Important questions regarding the safe harbor under the DMCA and the CDA have yet to be litigated, and we cannot guarantee that we will meet the safe harbor requirements of the DMCA or of the CDA. If we are not covered by a safe harbor, for any reason, we could be exposed to claims, which could be costly and time-consuming to defend.

Unplanned system interruptions and capacity constraints and failure to effect efficient transmission of customer communications and data over the Internet could harm our business and reputation.

Our customers have in the past experienced some interruptions with eGain cloud operations. We believe that these interruptions will continue to occur from time to time. These interruptions could be due to hardware and operating system failures. As a result, our business will suffer if we experience frequent or long system interruptions that result in the unavailability or reduced performance of our hosted operations or reduce our ability to provide remote management services. We expect to experience occasional temporary capacity constraints due to sharply increased traffic or other Internet-wide disruptions, which may cause unanticipated system disruptions, slower response times, impaired quality, and degradation in levels of customer service. If this were to continue to happen, our business and reputation could be seriously harmed.

The growth in the use of the Internet has caused interruptions and delays in accessing the Internet and transmitting data over the Internet. Interruptions also occur due to systems burdens brought on by unsolicited bulk email or “Spam,” malicious service attacks, denial of service attacks and hacking into operating systems, viruses, worms and a “Trojan” horse, the proliferation of which is beyond our control and may seriously impact our and our customers’ businesses.

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Because we provide cloud-based software, interruptions or delays in Internet transmissions will harm our customers' ability to receive and respond to online interactions. Therefore, our market depends on ongoing improvements being made to the entire Internet infrastructure to alleviate overloading and congestion.

Our success largely depends on the efficient and uninterrupted operation of our computer and communications hardware and network systems. A significant amount of our computer and communications systems are located in Sunnyvale, California. Due to our location, our systems and operations are vulnerable to damage or interruption from fire, earthquake, power loss, telecommunications failure and similar events. Customer data that we store in third party data centers may also be vulnerable to damage or interruption from floods, fires, power loss, telecommunications failures and similar events. Any damage to, or failure of, our systems generally could result in interruptions in our service. Interruptions in our service may reduce our revenue, cause us to issue credits or pay penalties, cause customers to terminate their subscriptions and adversely affect our renewal rate and our ability to attract new customers.

We maintain a business continuity plan for our customers in the event of an outage. We maintain other co-locations for the purposes of disaster recovery as well as maintaining backups of our customer's information. We provide premium disaster recovery and standard disaster recovery to our customers. If a customer opts not to pay for premium disaster recovery, we will only assure that their data is available within 72 hours. This delay could cause severe disruptions to our customers' customers and may result in customer termination of our solutions. Our premium disaster recovery service provides for an alternative data center and a return to operations within one business day.

We have entered into service agreements with some of our customers that require minimum performance standards, including standards regarding the availability and response time of our remote management services. If we fail to meet these standards, our customers could terminate their relationships with us, and we could be subject to contractual refunds and service credits to, and exposure to claims for losses by, customers. Any unplanned interruption of services may harm our ability to attract and retain customers.

If our cybersecurity systems or the systems of our vendors, partners and suppliers are breached and unauthorized access is obtained to a customer's data or our data or our IT systems, our service may be perceived as not being secure, customers may curtail or stop using our service and we may incur significant legal and financial exposure and liabilities.

Our service involves the storage and transmission of customers' proprietary information, and security breaches could expose us to a risk of loss of this information, loss of access, litigation and possible liability. These security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers (which may involve nation states and individuals sponsored by them), employee error, malfeasance or otherwise and result in someone obtaining unauthorized access to our customers' data or our data, including our intellectual property and other confidential business information, or our IT systems. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our customers' data or our data or IT systems.

Employees or contractors have introduced vulnerabilities in, and enabled the exploitation of, our IT environments in the past and may do so in the future. These cybersecurity attacks threaten to misappropriate our proprietary information, cause interruptions of our IT services and commit fraud. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. Further, if unauthorized access or sabotage remains undetected for an extended period of time, the effects of such breach could be exacerbated.

In addition, our customers may authorize third party access to their customer data located in our cloud environment. Because we do not control the transmissions between customer authorized third parties, or the processing of such data by customer authorized third parties, we cannot ensure the integrity or security of such transmissions or processing.

Cybersecurity attacks could require significant expenditures of our capital and diversion of our resources. If these attacks are successful, they could result in the theft of proprietary, personally identifiable, confidential and sensitive information of ours, our employees, our customers and our business partners, and could materially disrupt business for us, our customers and our business partners. A successful cybersecurity attack involving our data center, network or software

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products could also negatively impact the market perception of the effectiveness of our products or lead to contractual disputes, litigation or government regulatory action against us, any of which could materially adversely affect our business, reputation and resulting operations.

The terms we agree to in our Service Level Agreements or other contracts may result in increased costs or liabilities, which would in turn affect our results of operations.

Our Service Level Agreements provide for service credits for system unavailability, and in some cases, indemnities for loss, damage or costs resulting from use of our system. If we were required to provide any of these in a material way, our results of operations would suffer.

We have been and may in the future be sued by third parties for various claims including alleged infringement of proprietary rights.

We are involved in various legal matters arising from the normal course of business activities. These may include claims, suits, and other proceedings involving alleged infringement of third-party patents and other intellectual property rights, and commercial, labor and employment, and other matters.

The software and Internet industries are characterized by the existence of a large number of patents, trademarks and copyrights and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. We have received and may receive in the future communications from third parties claiming that we or our customers have infringed the intellectual property rights of others. In addition we have been, and may in the future be, sued by third parties for alleged infringement of their claimed proprietary rights. Our technologies and those of our customers may be subject to injunction if they are found to infringe the rights of a third party or we may be required to pay damages, or both. Many of our agreements require us to indemnify our customers for third-party intellectual property infringement claims, which would increase the cost to us of an adverse ruling on such a claim.

The outcome of any litigation, regardless of its merits, is inherently uncertain. Any claims and lawsuits, and the disposition of such claims and lawsuits, could be time-consuming and expensive to resolve, divert management attention from executing our business plan, lead to attempts on the part of other parties to pursue similar claims and, in the case of intellectual property claims, require us to change our technology, change our business practices or pay monetary damages, or enter into short- or long-term royalty or licensing agreements.

Any adverse determination related to intellectual property claims or other litigation could prevent us from offering our service to customers, could be material to our financial condition or cash flows, or both, or could otherwise adversely affect our operating results. In addition, depending on the nature and timing of any such dispute, a resolution of a legal matter could materially affect our future results of operation or cash flows or both.

We rely on trademark, copyright, trade secret laws, contractual restrictions and patent rights to protect our intellectual property and proprietary rights and if these rights are impaired, then our ability to generate revenue will be harmed.

If we fail to protect our intellectual property rights adequately, our competitors might gain access to our technology, and our business might be harmed. In addition, defending our intellectual property rights might entail significant expense. Any of our trademarks or other intellectual property rights may be challenged by others or invalidated through administrative process or litigation. While we have some U.S. patents and pending U.S. patent applications, we may be unable to obtain patent protection for the technology covered in our patent applications. In addition, our existing patents and any patents issued in the future may not provide us with competitive advantages, or may be successfully challenged by third parties. Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights are uncertain. Effective patent, trademark, copyright and trade secret

protection may not be available to us in every country in which our service is available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the U.S., and mechanisms for enforcement of intellectual property rights may be inadequate. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

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

Our failure or inability to develop non-infringing technology or license proprietary rights on a timely basis would harm our business.

We may be subject to legal proceedings and claims from time to time in the ordinary course of our business, including claims of alleged infringement of the patents and other intellectual property rights of third parties. Our products may infringe issued patents that may relate to our products because patent applications in the United States are not publicly disclosed until the patent is issued, and hence applications may have been filed which relate to our software products. Intellectual property litigation is expensive, time consuming, and could divert management's attention away from running our business. Litigation could also require us to develop non-infringing technology or enter into royalty or license agreements. These royalty or license agreements, if required, may not be available on acceptable terms, if at all, in the event of a successful claim of infringement.

Software errors could be costly and time-consuming for us to correct, and could harm our reputation and impair our ability to sell our solutions.

Our solutions are based on complex software that may contain errors, or "bugs," that could be costly to correct, harm our reputation and impair our ability to sell our solutions to new customers. Moreover, customers relying on our solutions may be more sensitive to such errors, and potential security vulnerabilities and business interruptions for these applications. If we incur substantial costs to correct any errors of this nature, our operating margins could be adversely affected. Because our customers depend on our solutions for critical business functions, any service interruptions could result in lost or delayed market acceptance and lost sales, higher service-level credits and warranty costs, diversion of development resources and product liability suits.

Our stock price has demonstrated volatility and continued market conditions may cause declines or fluctuations.

The price at which our common stock trades has been and will likely continue to be highly volatile and show wide fluctuations due to factors such as the following:

- transition to a recurring revenue model;
- concerns related to liquidity of our stock;
- actual or anticipated fluctuations in our operating results, our ability to meet announced or anticipated profitability goals and changes in or failure to meet securities analysts' expectations;
- announcements of technological innovations and/or the introduction of new services by us or our competitors;
- developments with respect to intellectual property rights and litigation, regulatory scrutiny and new legislation;
- conditions and trends in the Internet and other technology industries; and
- general market and economic conditions.

Furthermore, the stock market has experienced significant price and volume fluctuations that have affected the market prices for the common stock of technology companies, regardless of the specific operating performance of the affected company. These broad market fluctuations may cause the market price of our common stock to decline.

Our insiders who are significant stockholders may control the election of our board of directors and may have interests that conflict with those of other stockholders.

Our directors and executive officers, together with their affiliates and members of their immediate families, beneficially owned, in the aggregate, approximately 35% of our outstanding capital stock as of August 31, 2018, of which our Chief Executive Officer, Ashutosh Roy, beneficially owned approximately 30% as of such date. As a result of these concentrated

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holdings, Mr. Roy individually or together with this group has the ability to exercise significant control over most matters requiring our stockholders' approval, including the election and removal of directors and the approval of significant corporate transactions, such as a merger or sale of our company or its assets.

Our offshore product development, support and professional services may prove difficult to manage or may not allow us to realize our cost reduction goals, produce effective new solutions and provide professional services to drive growth.

We use offshore resources to perform new product and services development and provide support and professional consulting efforts, which requires detailed technical and logistical coordination. We must ensure that our international resources and personnel are aware of and understand development specifications and customer support, as well as implementation and configuration requirements and that they can meet applicable timelines. If we are unable to maintain acceptable standards of quality in support, product development and professional services, our attempts to reduce costs and drive growth through new products and margin improvements in technical support and professional services may be negatively impacted, which would adversely affect our results of operations. Outsourcing services to offshore providers may expose us to misappropriation of our intellectual property or that of our customers, or make it more difficult to defend intellectual property rights in our technology.

If we are unable to hire and retain key personnel, our business and results of operations would be negatively affected.

Our success will depend in large part on the skills, experience and performance of our senior management, engineering, sales, marketing and other key personnel. The loss of the services of any of our senior management or other key personnel, including our Chief Executive Officer and co-founder, Ashutosh Roy, could harm our business. Additionally, attrition in the Indian workforce on which we rely for research and development could have significant negative effects on us and our results of operations. If we cannot hire and retain qualified personnel, our ability to expand our business would be impaired and our results of operations would suffer.

Changes in the European regulatory environment regarding privacy and data protection regulations, such as the European Union's General Data Protection Regulation (GDPR), could expose us to risks of noncompliance and costs associated with compliance.

We have in the past relied on adherence to the U.S. Department of Commerce's Safe Harbor Privacy Principles and compliance with the U.S.-European Union (EU) and U.S. - Swiss Safe Harbor Frameworks as agreed to and set forth by the U.S. Department of Commerce, and the EU and Switzerland, which established a means for legitimating the transfer of personally identifiable information (PII) by U.S. companies doing business in Europe from the European Economic Area (EEA) to the U.S. As a result of the October 6, 2015 EU Court of Justice (ECJ), opinion in Case C-362/14 (Schrems v. Data Protection Commissioner) regarding the adequacy of the U.S.-EU Safe Harbor Framework, the U.S. – EU Safe Harbor Framework is no longer deemed to be a valid method of compliance with restrictions set forth in European law regarding the transfer of data outside of the EEA requiring us to rely on alternative mechanisms permitted under European law, such as consent and EU-specified standard contractual clauses. The U.S. - EU Safe Harbor was replaced with the EU - U.S. Privacy Shield (Privacy Shield) in July 2016 and, starting on August 1, 2016, the Privacy Shield was made available to companies for self-certification. We have self-certified with the Privacy Shield. Nevertheless, some of the mechanisms permitting transfer of data from the EU to the U.S. have been subject to challenges, whose outcomes remain uncertain.

Furthermore, on May 25, 2018, the EU's GDPR became enforceable, imposing new obligations directly on us as both a data controller and a data processor, as well as on many of our customers. It is possible that these new laws may be interpreted or applied in a manner that is adverse to us, unforeseen, or otherwise inconsistent with our practices or that we may not adequately adapt our internal policies and/or procedures to evolving regulations, any of which could result

in litigation, regulatory investigations and potential legal liability (including potential liability exposure through higher potential penalties for non-compliance), require us to make changes to our services to enable us and/or our customers to meet the new legal requirements, require us to change our practices in a manner adverse to our business or limit access to our products and services in certain countries.

We may be unsuccessful in establishing legitimate means of transferring data from the EEA, we may experience hesitancy, reluctance, or refusal by European or multi-national customers to continue to use our services due to the potential risk

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exposure to such customers as a result of the ECJ ruling or the implementation of GDPR, and we and our customers are at risk of enforcement actions taken by an EU data protection authority until such point in time that we ensure that all data transfers to us from the EEA are legitimized. We may find it necessary to establish systems to maintain EU-origin data in the EEA, which may involve substantial expense and distraction from other aspects of our business. We publicly post our privacy policies and practices concerning our processing, use and disclosure of PII. Our publication of our privacy policy and other statements we publish that provide promises and assurances about privacy and security can subject us to potential governmental action if they are found to be deceptive or misrepresentative of our practices. Further, the costs of compliance with, and other burdens imposed by, such laws, regulations and policies that are applicable to us may limit the use and adoption of our products and solutions and could have a material adverse impact on our results of operations.

Privacy concerns and laws, evolving regulation of cloud computing, cross-border data transfer restrictions and other domestic or foreign regulations may limit the use and adoption of our solutions and adversely affect our business.

Regulation related to the provision of services on the Internet is increasing, as federal, state and foreign governments continue to adopt new laws and regulations addressing data privacy and the collection, processing, storage and use of personal information. Further, laws are increasingly aimed at the use of personal information for marketing purposes, such as the EU's e-Privacy Directive (which is set to be replaced in the coming months by a new EU e-Privacy Regulation which will have a "direct effect" in each EU Member State), and the country-specific regulations that implement that directive. Such laws and regulations are subject to differing interpretations and may be inconsistent among jurisdictions. These and other requirements could reduce demand for our solutions or restrict our ability to store and process data or, in some cases, impact our ability to offer our services and solutions in certain locations.

In addition to government activity, privacy advocacy and other industry groups have established or may establish new self-regulatory standards that may place additional burdens on us. Our customers expect us to meet voluntary certification or other standards established by third parties, such as TRUSTe. If we are unable to maintain these certifications or meet these standards, it could adversely affect our ability to provide our solutions to certain customers and could harm our business.

The costs of compliance with and other burdens imposed by laws, regulations and standards may limit the use and adoption of our service and reduce overall demand for it, or lead to significant fines, penalties or liabilities for any noncompliance.

Furthermore, concerns regarding data privacy may cause our customers' customers to resist providing the data necessary to allow our customers to use our service effectively. Even the perception that the privacy of personal information is not satisfactorily protected or does not meet regulatory requirements could inhibit sales of our products or services, and could limit adoption of our subscription solution.

Industry-specific regulation is evolving and unfavorable industry-specific laws, regulations or interpretive positions could harm our business.

Our customers and potential customers conduct business in a variety of industries, including financial services, the public sector, healthcare and telecommunications. Regulators in certain industries have adopted and may in the future adopt regulations or interpretive positions regarding the use of cloud computing and other outsourced services. The costs of compliance with, and other burdens imposed by, industry-specific laws, regulations and interpretive positions may limit customers' use and adoption of our services and reduce overall demand for our services. For example, some financial services regulators have imposed guidelines for use of cloud computing services that mandate specific controls or require financial services enterprises to obtain regulatory approval prior to outsourcing certain functions. If we are unable to comply with these guidelines or controls, or if our customers are unable to obtain regulatory approval

to use our service where required, our business may be harmed. In addition, an inability to satisfy the standards of certain voluntary third-party certification bodies that our customers may expect, such as an attestation of compliance with the Payment Card Industry (PCI) Data Security Standards, may have an adverse impact on our business. If we are unable to achieve or maintain these industry-specific certifications or other requirements or standards relevant to our customers, it may harm our business.

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In some cases, industry-specific laws, regulations or interpretive positions may also apply directly to us as a service provider. Any failure or perceived failure by us to comply with such requirements could have an adverse impact on our business.

We may need to license third-party technologies and may be unable to do so on commercially reasonable terms.

To the extent we need to license third-party technologies, we may be unable to do so on commercially reasonable terms or at all. In addition, we may fail to successfully integrate any licensed technology into our products or services. Third-party licenses may expose us to increased risks, including risks associated with the integration of new technology, the diversion of resources from the development of our own proprietary technology, and our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs. Our inability to obtain and successfully integrate any of these licenses could delay product and service development until equivalent technology can be identified, licensed and integrated. This in turn would harm our business and operating results.

Changes to current accounting policies could have a significant effect on our reported financial results or the way in which we conduct our business.

Generally accepted accounting principles and the related accounting pronouncements, implementation guidelines and interpretations for some of our significant accounting policies are highly complex and require subjective judgments and assumptions. Some of our more significant accounting policies that could be affected by changes in the accounting rules and the related implementation guidelines and interpretations include:

· recognition of revenue;
· contingencies and litigation; and
· accounting for income taxes.

Changes in these or other rules, or scrutiny of our current accounting practices, or a determination that our judgments or assumptions in the application of these accounting principles were incorrect, could have a significant adverse effect on our reported operating results or the way in which we conduct our business.

We depend on broad market acceptance of our applications and of our business model.

We depend on the widespread acceptance and use of our applications as an effective solution for businesses seeking to manage high volumes of customer interactions across multiple channels, including Web, phone, email, print and in-person. While we believe the potential to be very large, we cannot accurately estimate the size or growth rate of the potential market for such product and service offerings generally, and we do not know whether our products and services in particular will achieve broad market acceptance. The market for customer engagement software is rapidly evolving, and concerns over the security and reliability of online transactions, the privacy of users and quality of service or other issues may inhibit the growth of the Internet and commercial online services. If the market for our applications fails to grow or grows more slowly than we currently anticipate, our business will be seriously harmed.

Furthermore, our business model is premised on business assumptions that are still evolving. Our business model assumes that both customers and companies will increasingly elect to communicate through multiple channels, as well as demand integration of the online channels into the traditional telephone-based call center. If any of these assumptions is incorrect or if customers and companies do not adopt digital technology in a timely manner, our business will be seriously harmed and our stock price will decline.

We may be unable to respond to the rapid technological change and changing customer preferences in the online sales, marketing, customer service, and/or online consumer services industries and this may harm our business.

If we are unable, for technological, legal, financial or other reasons, to adapt in a timely manner to changing market conditions in the online sales, marketing, customer service and/or e-commerce industry or our customers' or Internet users' requirements or preferences, our business, results of operations and financial condition would be materially and adversely affected. Business on the Internet is characterized by rapid technological change. In addition, the market for online sales, marketing, customer service and expert advice solutions is relatively new. Changes in customer and Internet user

requirements and preferences, frequent new product and service introductions embodying new technologies and the emergence of new industry standards and practices such as but not limited to security standards could render our services and our proprietary technology and systems obsolete. The rapid evolution of these products and services will require that we continually improve the performance, features and reliability of our services. Our success will depend, in part, on our ability to:

- enhance the features and performance of our services;
- develop and offer new services that are valuable to companies doing business online as well as Internet users; and
- respond to technological advances and emerging industry standards and practices in a cost-effective and timely manner.

If any of our new services, including upgrades to our current services, do not meet our customers' or Internet users' expectations, our business may be harmed. Updating our technology may require significant additional capital expenditures and could materially and adversely affect our business, results of operations and financial condition.

If new services require us to grow rapidly, this could place a significant strain on our managerial, operational, technical and financial resources. In order to manage our growth, we could be required to implement new or upgraded operating and financial systems, procedures and controls. Our failure to expand our operations in an efficient manner could cause our expenses to grow, our revenue to decline or grow more slowly than expected and could otherwise have a material adverse effect on our business, results of operations and financial condition.

We may engage in future acquisitions or investments that could dilute our existing stockholders, cause us to incur significant expenses or harm our business.

We may review acquisition or investment prospects that we believe may complement our current business or enhance our technological capabilities. Integrating any newly acquired businesses or their technologies or products may be expensive and time-consuming, and may not result in benefits to our business. To finance any acquisitions, we may raise funds through public or private financings. Additional funds may not be available on terms that are favorable to us, if at all, and, in the case of equity financings, may result in dilution to our existing stockholders. We may not be able to operate acquired businesses profitably. If we are unable to integrate newly acquired entities or technologies effectively, our operating results could suffer. Future acquisitions by us could also result in large and immediate write-offs, incurrence of debt and contingent liabilities, or amortization of expenses related to goodwill and other intangible assets, any of which could harm our operating results.

We may not be able to realize the benefits of offering the limited "Try & Buy" free version of our service.

We offer a limited version of our subscription service to customers or potential customers free of charge (known as "Try & Buy") in order to promote usage, brand and product awareness, and adoption, and we invest time and resources for such initial engagements without compensation from the customers. Some customers never enter into a definitive contract for our paid subscription service despite the time and effort we may have expended on such Try & Buy initiatives. To the extent that these customers do not become paying customers, we will not realize the intended benefits of this marketing effort, and our ability to grow our business and revenue may be harmed.

The uncertainty surrounding the implementation and effect of Brexit may cause increased economic volatility, affecting our operations and business.

On June 23, 2016, voters in the United Kingdom (UK) approved an advisory referendum to withdraw membership from the EU, which proposed exit (referred to as Brexit) could cause disruptions to, and create uncertainty surrounding, our business in the UK and EU, including affecting our relationships with our existing and future customers, suppliers and employees. As a result, Brexit could have an adverse effect on our future business, financial

results and operations. The formal process for UK leaving the EU began in March 2017, when the UK served notice to the European Council under Article 50 of the Treaty of Lisbon. The long-term nature of the UK's relationship with the EU is unclear and there is considerable uncertainty when any relationship will be agreed and implemented. The political and economic instability created by Brexit has caused and may continue to cause significant volatility in global financial markets and uncertainty regarding the regulation of data protection in the UK. Brexit could also have the effect of disrupting the free movement of goods, services, and people between the UK, the EU, and elsewhere. The effects of Brexit will depend on any agreements

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the UK makes to retain access to EU markets either during a transitional period or more permanently. Brexit could lead to legal uncertainty and potentially divergent national laws and regulations as the UK determines which EU laws to replace or replicate. Further, uncertainty around these and related issues could lead to adverse effects on the economy of the UK and the other economies in which we operate. There can be no assurance that any or all of these events will not have a material adverse effect on our business operations, results of operations and financial condition.

ITEM 1B.UNRESOLVED STAFF COMMENTS

None.

ITEM 2.PROPERTIES

We lease all facilities used in our business as of June 30, 2018. The following table summarizes our principal properties:

Location	Principal Use	Approximate Square Footage	Lease Expiration Date
Sunnyvale, California	Corporate Headquarters	42,541	2022
Newbury, England	Corporate Office – EMEA	14,090	2024
Pune, India	Corporate Office – APAC	33,262	2021

ITEM 3.LEGAL PROCEEDINGS

In the ordinary course of business, we are involved in various legal proceedings and claims related to alleged infringement of third-party patents and other intellectual property rights, commercial, corporate and securities, labor and employment, wage and hour, and other claims. We have been, and may in the future be, put on notice and/or sued by third parties for alleged infringement of their proprietary rights, including patent infringement.

We evaluate all claims and lawsuits with respect to their potential merits, our potential defenses and counterclaims, settlement or litigation potential and the expected effect on us. Our technologies may be subject to injunction if they are found to infringe the rights of a third party. In addition, our agreements require us to indemnify our customers for third-party intellectual property infringement claims, which could increase the cost to us of an adverse ruling on such a claim.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

Executive Officers of the Registrant.

The following table sets forth information regarding eGain’s executive officers as of September 13, 2018:

Name	Age	Position
Ashutosh Roy	52	Chief Executive Officer and Chairman
Eric Smit	56	Chief Financial Officer
Promod Narang	60	Senior Vice President of Products and Engineering
Todd Woodstra	56	Senior Vice President of Global Sales

Ashutosh Roy co-founded eGain and has served as Chief Executive Officer and a director of eGain since September 1997 and President since October 2003. From May 1995 through April 1997, Mr. Roy served as Chairman of WhoWhere? Inc., an Internet-service company co-founded by Mr. Roy. From June 1994 to April 1995, Mr. Roy co-founded Parsec Technologies, a call center company based in New Delhi, India. From August 1988, to August 1992, Mr. Roy worked as a Software Engineer at Digital Equipment Corp. Mr. Roy holds a B.S. in Computer Science from the Indian Institute of Technology, New Delhi, a Master's degree in Computer Science from Johns Hopkins University and an M.B.A. from Stanford University.

Eric Smit has served as Chief Financial Officer since August 2002. Prior to that, Mr. Smit served in a variety of roles at eGain, including Vice President, Operations from April 2001 to July 2002, Vice President, Finance and Administration

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from June 1999 to April 2001, and Director of Finance from June 1998 to June 1999. From December 1996 to May 1998, Mr. Smit served as Director of Finance for WhoWhere? Inc., an Internet services company. From April 1993 to November 1996, Mr. Smit served as Vice President of Operations and Chief Financial Officer of Velocity Incorporated, a software game developer and publishing company. Mr. Smit holds a Bachelor of Commerce in Accounting from Rhodes University, South Africa.

Promod Narang has served as Senior Vice President of Engineering since March 2000. Mr. Narang joined eGain in October 1998, and served as Director of Engineering prior to assuming his current position. Prior to joining eGain, Mr. Narang served as President of VMpro, a system software consulting company, from September 1987 to October 1998. Mr. Narang holds a Bachelor of Science in Computer Science from Wayne State University.

Todd Woodstra has served as Senior Vice President of Global Sales since August 2017. Prior to joining eGain, Mr. Woodstra was the Senior Vice President of Enterprise/Channels at Sparks Compass and the Senior Vice President of Enterprise Sales for Interactions LLC from January 2015 to February 2017 where he led enterprise customer sales focused on virtual assistant solutions. From November 2009 to July 2014, Mr. Woodstra was Vice President of Global Channel and Partner Alliances for Nuance Communications, where he managed and executed business in channels and commercial enterprise, self-service, mobile, collaboration, unified communications, natural language speech recognition, voice biometrics, gesture technologies, inbound/outbound notification and voice-to-text transcription. Mr. Woodstra holds a Bachelor of Arts in Business Administration, Management Information Systems from California State University, San Bernardino.

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PART II

ITEM 5.MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

The following table sets forth, for the periods indicated, high and low bid prices for eGain's common stock as reported by the Nasdaq Stock Market LLC.

Year Ended June 30, 2018	High	Low
First Quarter	$ 2.90	$ 1.55
Second Quarter	$ 5.45	$ 2.55
Third Quarter	$ 8.50	$ 4.60
Fourth Quarter	$ 15.50	$ 7.35
Year Ended June 30, 2017		
First Quarter	$ 3.51	$ 2.12
Second Quarter	$ 3.40	$ 1.93
Third Quarter	$ 2.40	$ 1.35
Fourth Quarter	$ 1.90	$ 1.30

Holders

As of August 31, 2018, there were approximately 176 stockholders of record. As of August 31, 2018, we estimate that there were approximately 11,320 beneficial stockholders of our common stock.

Dividends

We have never declared or paid any cash dividends on our common stock. We currently anticipate that we will retain all available funds for use in the operation of our business and do not intend to pay any cash dividends in the foreseeable future. In addition, the terms of our Credit Agreement restrict the payment of dividends.

Stock Performance Graph

The following shall not be deemed incorporated by reference into any of our other filings under the Securities Exchange Act of 1934, as amended, or the Securities Act of 1933, as amended.

The graph below compares the cumulative total stockholder return on our common stock with the cumulative total return on the Standard & Poor's 500 Index and the Nasdaq Composite Total Return Index for each of the last five fiscal years ended June 30, 2018, assuming an initial investment of $100. Data for the Standard & Poor's 500 Index and the Nasdaq Composite Total Return Index assume no dividends.

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The comparisons in the graph below are based upon historical data and are not indicative of, nor intended to forecast, future performance of our common stock.

	06-30-13	06-30-14	06-30-15	06-30-16	06-30-17	06-30-18
eGain Corporation	$ 100.00	$ 70.37	$ 52.08	$ 29.31	$ 17.15	$ 156.96
Nasdaq Composite	$ 100.00	$ 131.17	$ 150.10	$ 147.58	$ 189.34	$ 234.02
S&P Software & Services Select Industry Index	$ 100.00	$ 124.67	$ 144.92	$ 144.55	$ 180.53	$ 235.13

Equity Compensation Plan Information

The following table summarizes our equity compensation plans as of June 30, 2018:

Plan Category	Number of securities to be issued upon exercise of outstanding options and rights (a)	Weighted-average exercise price of outstanding options and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders			
1998 Stock Plan	—	$ —	—
2005 Stock Incentive Plan	1,680,734	$ 2.90	588,654
Equity compensation plans not approved by security holders			
2000 Non-Management Stock Option Plan	—	$ —	—
2005 Management Stock Option Plan	1,492,125	$ 3.51	68,649
Total	3,172,859	$ 3.19	657,303

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Equity Compensation Plans Not Approved By Security Holders

2000 Non-Management Stock Option Plan

In July 2000, our board of directors adopted the 2000 Non-Management Stock Option Plan, which provides for the grant of non-statutory stock options and stock purchase rights to employees of eGain. A total of 200,000 shares of common stock were reserved for issuance under the 2000 Non-Management Stock Option Plan. This plan expired in July 2010, and there are no further options available to grant under the 2000 Non-Management Stock Option Plan.

2005 Management Stock Option Plan

In May 2005, our board of directors adopted the 2005 Management Stock Option Plan (2005 Management Plan), pursuant to which the Compensation Committee may grant non-qualified stock options to purchase up to 962,400 shares of eGain common stock, at an exercise price of not less than 100% of the fair market value of such common stock, to directors, officers and key employees of the Company and its subsidiaries. Options granted under the 2005 Management Plan are subject to vesting as determined by the Compensation Committee. The options are exercisable for up to ten years from the date of grant.

Our board of directors approved an increase of 500,000 shares of common stock authorized for issuance under the 2005 Management Plan in November 2007 and another increase of 500,000 shares of common stock authorized for issuance under the 2005 Management Plan in September 2011.

In September 2014, our board of directors approved an amendment to the 2005 Management Plan that increased the number of shares of common stock reserved for issuance by 1,000,000 shares from 1,962,400 shares to 2,962,400 shares and extended the expiration date of the of the 2005 Management Plan to September 30, 2024.

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ITEM 6.SELECTED FINANCIAL DATA

The selected consolidated financial data should be read in conjunction with the information under “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” our consolidated financial statements and the related notes which are included in “Item 8. Financial Statements and Supplementary Data.”

	Year ended June 30,				
	2018	2017	2016	2015	2014
	(in thousands, except per share information)				
Revenue					
Recurring	$ 50,767	$ 43,585	$ 42,783	$ 42,311	$ 40,477
Legacy license	585	4,557	14,466	18,325	14,800
Professional services	9,955	10,073	12,126	15,277	14,985
Total revenue	61,307	58,215	69,375	75,913	70,262
Cost of revenue:					
Cost of recurring	13,075	11,956	12,401	12,082	8,518
Cost of legacy license	77	50	29	61	104
Cost of professional services	9,184	9,193	11,259	16,998	14,840
Total cost of revenue	22,336	21,199	23,689	29,141	23,462
Gross profit	38,971	37,016	45,686	46,772	46,800
Operating expenses					
Research and development	14,711	13,753	16,063	16,042	9,963
Sales and marketing	17,681	20,436	27,722	32,703	33,367
General and administrative	7,567	6,552	7,774	9,313	7,529
Total operating expenses	39,959	40,741	51,559	58,058	50,859
Loss from operations	(988)	(3,725)	(5,873)	(11,286)	(4,059)
Interest expense, net	(983)	(1,730)	(1,958)	(834)	(181)
Other income (expense), net	(206)	(32)	728	11	(415)
Loss before income tax benefit (provision)	(2,177)	(5,487)	(7,103)	(12,109)	(4,655)
Income tax benefit (provision)	186	(533)	863	(320)	(591)
Net loss	$ (1,991)	$ (6,020)	$ (6,240)	$ (12,429)	$ (5,246)
Per share information					
Basic and diluted net loss per common share	$ (0.07)	$ (0.22)	$ (0.23)	$ (0.47)	$ (0.21)
Weighted average shares used to compute basic and diluted net loss per common share	27,333	27,108	27,056	26,609	25,353
Below is a summary of stock-based compensation included in the costs and expenses above:					
Cost of revenue	$ 323	$ 131	$ 249	$ 476	$ 280
Research and development	$ 493	$ 281	$ 472	$ 736	$ 386
Sales and marketing	$ 341	$ 80	$ 169	$ 574	$ 464
General and administrative	$ 538	$ 175	$ 298	$ 531	$ 397

June 30,

	2018	2017	2016	2015	2014
Consolidated Balance Sheet Data:					
Cash, cash equivalents and short-term investments (including restricted cash)	$ 11,504	$ 10,633	$ 11,785	$ 9,309	$ 8,815
Working capital	$ (8,023)	$ (7,680)	$ (886)	$ (2,039)	$ (1,885)
Total assets	$ 39,622	$ 39,751	$ 48,063	$ 49,731	$ 32,647
Deferred revenue	$ 26,197	$ 23,219	$ 15,717	$ 15,812	$ 13,713
Long-term debt (bank borrowings and capital lease obligations)	$ 8,941	$ 14,844	$ 20,376	$ 18,554	$ 4,208

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ITEM 7.MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of eGain's financial condition and results of operations should be read together with the consolidated financial statements and related notes in this Annual Report on Form 10-K. This discussion may contain forward-looking statements based upon current expectations that involve risks and uncertainties. These risks and uncertainties may cause actual results to differ materially from those discussed in the forward-looking statements.

Overview

eGain Corporation is a leading provider of cloud-based customer engagement software. We help B2C brands operationalize digital customer engagement strategy. Our suite includes rich applications for digital interaction, knowledge management, and AI-based process guidance. We also provide advanced, integrated analytics for contact centers and digital properties to holistically measure, manage, and optimize resources. We believe the benefits of our products include reduced customer effort, customer satisfaction, connected service processes, converted upsell opportunities, and improved compliance—across mobile, social, web, and phone. Hundreds of global enterprises rely on eGain to transform fragmented customer service systems into unified Customer Engagement Hubs.

We have operations in the United States, United Kingdom and India.

In fiscal year 2018, we recorded annual revenue of $61.3 million and loss from operations of $988,000, compared to annual revenue of $58.2 million and loss from operations of $3.7 million in fiscal year 2017. The year-over-year increase in total revenue was primarily driven by a 16% increase in recurring revenue, partially offset by a 87% decrease in legacy license revenue and a 1% decrease in professional services revenue. Recurring revenue was $50.8 million in fiscal year 2018, compared to $43.6 million in fiscal year 2017. Legacy license revenue was $585,000 in fiscal year 2018, compared to $4.6 million in fiscal year 2017. Professional services revenue was $10.0 million in fiscal year 2018, compared to $10.1 million in fiscal year 2017. Cash provided by operations was $6.6 million for fiscal year 2018, compared to cash provided by operations of $5.4 million for fiscal year 2017.

Unbilled Deferred Revenue

Unbilled deferred revenue represents business that is contracted but not yet invoiced or collected and off–balance-sheet and, accordingly, is not recorded in deferred revenue. As such, the deferred revenue balance on our consolidated balance sheet does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements. As of June 30, 2018, unbilled deferred revenue increased to $51.4 million, up from $37.0 million as of June 30, 2017.

Key Financial Measures

We monitor the key financial performance measures set forth below as well as cash and cash equivalents and available debt capacity, which are discussed in Liquidity and Capital Resources, to help us evaluate trends, establish budgets, measure the effectiveness of our sales and marketing efforts and assess operational effectiveness and efficiencies. These key financial performance measures include certain non-GAAP metrics, including non-GAAP operating income (loss) as defined below. The presentation of the non-GAAP financial measures is not intended to be considered in isolation or as a substitute for, or superior to, the financial information prepared and presented in accordance with generally accepted accounting principles (GAAP).

Non-GAAP operating income (loss) is defined as operating loss, adjusted for the impact of stock-based compensation expense and amortization of acquired intangible assets.

Management believes that it is useful to exclude certain non-cash charges and non-core operational charges from non-GAAP operating income (loss) because (i) the amount of such expenses in any specific period may not directly correlate to the underlying performance of our business operations; and (ii) such expenses can vary significantly between periods as a result of the timing of new stock-based awards and acquisitions.

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The following table presents our key financial measures, including a reconciliation of GAAP loss from operations to non-GAAP income (loss) from operations for each of the following periods:

	Fiscal Year Ended June 30		
	2018	2017	2016
Loss from operations	$ (988)	$ (3,725)	$ (5,873)
Add:			
Stock-based compensation	1,695	667	1,188
Amortization of intangible assets	2,015	2,091	2,781
Non-GAAP income (loss) from operations	$ 2,722	$ (967)	$ (1,904)

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. On an on-going basis, management evaluates its estimates and judgments, including those related to revenue recognition, allowance for doubtful accounts, goodwill, intangible assets, deferred tax valuation allowance, accrued liabilities, long-lived assets and stock-based compensation. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Business Combinations

Business combinations are accounted for at fair value under the purchase method of accounting. Acquisition costs are expensed as incurred and recorded in general and administrative expenses and changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date affect income tax expense. The accounting for business combinations requires estimates and judgment as to expectations for future cash flows of the acquired business, and the allocation of those cash flows to identifiable intangible assets, in determining the estimated fair value for assets acquired and liabilities assumed. The fair values assigned to tangible and intangible assets acquired and liabilities assumed are based on management's estimates and assumptions, as well as other information compiled by management, including valuations that utilize customary valuation procedures and techniques. If the actual results differ from the estimates and judgments used in these estimates, the amounts recorded in the consolidated financial statements could result in a possible impairment of the intangible assets and goodwill, or require acceleration of the amortization expense of finite-lived intangible assets.

Revenue Recognition

We enter into arrangements to deliver multiple products or services (multiple-elements). We apply software revenue recognition rules and multiple-elements arrangement revenue guidance. Significant management judgments and estimates are made and used to determine the revenue recognized in any accounting period. Material differences may result in changes to the amount and timing of our revenue for any period if different conditions were to prevail. We present revenue net of taxes collected from customers and remitted to governmental authorities.

We derive revenue from three sources:

i. Recurring fees (previously referred to as subscription and support) primarily consist of cloud revenue from customers accessing our enterprise cloud computing services, term and ratable license revenue, and maintenance and support revenue;
ii. Legacy license fees primarily consist of revenue from perpetual software licenses which we no longer sell to new customers;
iii. Professional services primarily consist of consulting, implementation services and training.

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Revenues are recognized when all of the following criteria are met:

· Persuasive evidence of an arrangement exists: Evidence of an arrangement consists of a written contract signed by both the customer and management prior to the end of the period. We use signed software license, services agreements and order forms as evidence of an arrangement for sales of software, cloud, maintenance and support. We use a signed statement of work as evidence of arrangement for professional services.
· Delivery or performance has occurred: Software is delivered to customers electronically, and license files are delivered electronically. Delivery is considered to have occurred when we provide the customer access to the software along with a license file and/or login credentials.
· Fees are fixed or determinable: We assess whether the fee is fixed or determinable based on the payment terms associated with the transaction. Arrangements where a significant portion of the fee is due beyond 90 days from delivery are generally not considered to be fixed or determinable.
· Collectibility is probable: We assess collectibility based on a number of factors, including the customer's past payment history and its current creditworthiness. Payment terms generally range from 30 to 90 days from invoice date. If we determine that collection of a fee is not reasonably assured, we defer the revenue and recognize it at the time collection becomes reasonably assured, which is generally upon receipt of cash payment.

Revenue from sales to resellers is generally recognized upon delivery to the reseller dependent on the facts and circumstances of the transaction, such as our understanding of the reseller's plans to sell the software, existence of return provisions, price protection or other allowances, the reseller's financial status and our past experience with the reseller. Historically sales to resellers have not included any return provisions, price protection or other allowances.

We apply the provisions of Accounting Standards Codification (ASC) 985-605, Software Revenue Recognition, to all transactions involving the licensing of software products. In the event of a multiple element arrangement for a license transaction, we evaluate the transaction as if each element represents a separate unit of accounting taking into account all factors following the accounting standards. We apply ASC 605, Revenue Recognition, for cloud transactions to determine the accounting treatment for multiple elements. We also apply ASC 605-35 for fixed fee arrangements in which we use the percentage of completion method to recognize revenue when reliable estimates are available for the costs and efforts necessary to complete the implementation services. When such estimates are not available, the completed contract method is utilized. Under the completed contract method, revenue is recognized only when a contract is completed or substantially complete.

When legacy perpetual licenses were sold together with system implementation and consulting services, legacy license fees were recognized upon shipment, provided that (i) payment of the license fees were not dependent upon the performance of the consulting and implementation services, (ii) the services were available from other vendors, (iii) the services qualified for separate accounting as we have sufficient experience in providing such services, had the ability to estimate cost of providing such services, and we had vendor specific objective evidence, or VSOE, of fair value, and (iv) the services were not essential to the functionality of the software.

We enter into arrangements with multiple-deliverables that generally include subscription, maintenance and support, and professional services. We evaluate whether each of the elements in these arrangements represents a separate unit of accounting, as defined by ASC 605, using all applicable facts and circumstances, including whether (i) we sell or could readily sell the element unaccompanied by the other elements, (ii) the element has stand-alone value to the customer, and (iii) there is a general right of return. For revenue recognition with multiple-deliverable elements, we apply the selling price hierarchy, which includes VSOE, third-party evidence of selling price, or TPE, and best estimate of selling price, or BESP. We determine the relative selling price for a deliverable based on VSOE, if available, or BESP, if VSOE is not available. We determined that TPE is not a practical alternative due to differences in our service offerings compared to other parties and the availability of relevant third-party pricing information.

We determine BESP by considering our overall pricing objectives and market conditions. Significant pricing practices taken into consideration include our discounting practices, the size and volume of our transactions, the customer demographic, the geographic area where services are sold, price lists, our go-to-market strategy, historical standalone sales and contract prices. The determination of BESP is made through consultation with and approval by our management,

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taking into consideration our go-to-market strategy. As our go-to-market strategies evolve, we may modify our pricing practices in the future, which could result in changes in relative selling prices, including both VSOE and BESP.

During fiscal year 2018, we continued our transition from a perpetual license to a cloud delivery model. As a result, we did not maintain VSOE related to maintenance and support revenue for which maintenance and support had been sold in connection with legacy perpetual licenses. Additionally, we did not maintain VSOE related to professional services revenue due to variable pricing in our services provided and other factors. Accordingly, we have used BESP to determine the relative selling price.

Recurring Revenue

Cloud Revenue

Cloud revenue consists of subscription fees along with bundled maintenance and support revenue from customers accessing our cloud-based service offerings. We recognize cloud revenue ratably over the period of the applicable agreement as services are provided. Cloud agreements typically have an initial term of 12 to 36 months and automatically renew unless either party cancels the agreement. The majority of the cloud services customers purchase a combination of our cloud service and professional services.

We consider the applicability of ASC 985-605, Software Revenue Recognition, on a contract-by-contract basis. In cloud-based agreements, where the customer does not have the contractual right to take possession of the software, the revenue is recognized on a ratable basis over the term of the contract. Invoiced amounts are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met. We consider a software element to exist when we determine that the customer has the contractual right to take possession of our software at any time during the cloud period without significant penalty and can feasibly run the software on its own hardware or enter into another arrangement with a third party to host the software. Additionally, we had previously established VSOE for the cloud and maintenance and support elements of perpetual license sales, based on the prices charged when sold separately and substantive renewal terms. Accordingly, when a software element exists in a cloud services arrangement, license revenue for the perpetual software license element is determined using the residual method and is recognized upon delivery. Revenue for the cloud and maintenance and support elements is recognized ratably over the contractual time period. Professional services are recognized as described below under Professional Services Revenue. If VSOE of fair value cannot be established for the undelivered elements of an arrangement, the entire amount of revenue from the arrangement is recognized ratably over the period that these elements are delivered.

Term and Ratable License Revenue

Term and ratable license revenue includes arrangements where our customers receive license rights to use our software along with bundled maintenance and support services for the term of the contract or where we have not established VSOE for the bundled multi-year maintenance and support services. The majority of our contracts provide customers with the right to use one or more products up to a specific license capacity. Certain terms of our license agreements stipulate that customers can exceed pre-determined base capacity levels, in which case additional fees are specified in the license agreement. Term license revenue is recognized ratably over the term of the license contract, and ratable license revenue is recognized over the term of the associated bundled maintenance and support contract.

Version 15.5 and future releases of the perpetual license is a cloud and perpetual license hybrid software which represents a service contract under ASC 605-25. The cloud components are essential to the functionality of version 15.5 and future releases, and we have a contractual obligation to deliver these cloud components. Per ASC 605-25, a delivered item is considered a separate unit of accounting only if (i) the delivered item has standalone value; and (ii) if

the service contract has a general right of return, then delivery and performance of the undelivered item is probable and substantially within the vendor's control. We cannot separate the cloud components because there is no standalone value of the cloud components. The perpetual license revenue is recognized over the economic life of the software which was determined to be three years.

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Maintenance and Support Revenue

Maintenance and support revenue consists of customers purchasing maintenance and support for our on-premise software. Maintenance and support revenue is recognized ratably over the term of the maintenance contract, which is typically one year. Maintenance and support is renewable by the customer on an annual basis. Maintenance and support rates, including subsequent renewal rates, are typically established based upon a specified percentage of net license fees as set forth in the arrangement.

Legacy License Revenue

Legacy license revenue consists of perpetual license rights sold to customers to use our software in conjunction with related maintenance and support services. If an acceptance period is required, revenue is recognized upon the earlier of customer acceptance or the expiration of the acceptance period. In software arrangements that include rights to multiple software products and/or services, we use the residual method for perpetual licenses released as version 15 or prior under which revenue is allocated to the undelivered elements based on VSOE of the fair value of such undelivered elements. The residual amount of revenue is allocated to the delivered elements and recognized as revenue, assuming all other criteria for revenue recognition have been met. Such undelivered elements in these arrangements typically consist of software maintenance and support, implementation and consulting services and, in some cases, cloud services.

Professional Services Revenue

Professional services revenue includes system implementation, consulting and training. For license transactions, the majority of our consulting and implementation services qualify for separate accounting. We use BESP to determine the relative selling price. Our consulting and implementation service contracts are bid either on a fixed-fee basis or on a time-and-materials basis. Substantially all of our contracts are on a time-and-materials basis. For time-and-materials contracts, where the services are not essential to the functionality, we recognize revenue as services are performed. If the services are essential to functionality, then both the product license revenue and the service revenue are recognized under the percentage of completion method. For a fixed-fee contract, we recognize revenue based upon the costs and efforts to complete the services in accordance with the percentage of completion method, provided we are able to estimate such cost and efforts.

Under ASC 605-25, in order to account for deliverables in a multiple-deliverable arrangement as separate units of accounting, the deliverables must have standalone value upon delivery. For cloud services, in determining whether professional services have standalone value, we consider the following factors for each professional services agreement: availability of the services from other vendors, the nature of the professional services, the timing of when the professional services contract was signed in comparison to the subscription service start date and the contractual dependence of the subscription service on the customer’s satisfaction with the professional services work.

We have standalone value for consulting and implementation services. For those contracts that have standalone value, we recognize the services revenue when rendered for time and material contracts, when the milestones are achieved and accepted by the customer for fixed price contracts or by percentage of completion basis if there is no acceptance criteria.

Training revenue that meets the criteria to be accounted for separately is recognized when training is provided.

Deferred Revenue

Deferred revenue primarily consists of payments received in advance of revenue recognition from cloud, term and ratable licenses, and maintenance and support services and is recognized as the revenue recognition criteria are met. We generally invoice customers in annual or quarterly installments. The deferred revenue balance does not represent the total contract value of annual or multi-year, non-cancelable cloud or maintenance and support agreements. Deferred revenue is influenced by several factors, including seasonality, the compounding effects of renewals, invoice duration, invoice timing and new business linearity within the quarter.

Deferred revenue that will be recognized during the succeeding twelve-month period is recorded as current deferred revenue and the remaining portion is recorded as noncurrent. As of June 30, 2018, deferred revenue increased to $26.2 million compared to $23.2 million as of June 30, 2017.

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Deferred Commissions

Deferred commissions are the direct and incremental costs directly associated with cloud and term license contracts with customers and consist of sales commissions to our direct sales force.

The commissions are deferred and amortized over the terms of the related customer contracts which are typically 12 to 36 months. The commission payments are paid based on contract terms in the month following the quarter in which the commissions are earned. The deferred commission amounts are recognized as sales and marketing expense in the consolidated statements of operations over the terms of the related customer contracts, in proportion to the recognition of the associated revenue.

Stock-Based Compensation

We account for stock-based compensation in accordance with ASC 718, Compensation — Stock Compensation. Under the fair value recognition provisions of ASC 718, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense over the vesting period. Determining the fair value of the stock-based awards at the grant date requires significant judgment and the use of estimates, particularly surrounding Black-Scholes valuation assumptions such as stock price volatility and expected option lives. We determine the appropriate measure of expected volatility by reviewing historic volatility in the share price of our common stock, as adjusted for certain events that management deems to be non-recurring and non-indicative of future events. We base our estimate of expected life on the historical exercise behavior, cancellations of all past option grants made by us during the time period in which our common stock has been publicly traded, the contractual term, the vesting period and the expected remaining term of the option. Based on our historical experience of option pre-vesting cancellations, we have assumed an annualized 12.45% forfeiture rate for our options. We record additional expense if the actual forfeiture rate is lower than we estimated, and record a recovery of prior expense if the actual forfeiture rate is higher than what we estimated.

Goodwill and Other Intangible Assets

In accordance with ASC 350, Goodwill and Other Intangible Assets, we review goodwill annually for impairment or sooner whenever events or changes in circumstances indicate that they may be impaired. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit. In addition, we evaluate purchased intangible assets to determine that all such assets have determinable lives. We operate under a single reporting unit and accordingly, all of our goodwill is associated with the entire company. We had no impairment due to a negative carrying amount of our reporting unit. We performed an annual impairment review and found no impairment for fiscal years ended June 30, 2018 and 2017.

Accounts Receivable and Allowance for Doubtful Accounts

We extend unsecured credit to customers on a regular basis. Our accounts receivable are derived from revenue earned from customers and are not interest bearing. We also maintain an allowance for doubtful accounts to reserve for potential uncollectible trade receivables. We review our trade receivables by aging category to identify specific customers with known disputes or collectability issues. We exercise judgment when determining the adequacy of these reserves as we evaluate historical bad debt trends, general economic conditions in the U.S. and internationally, and changes in customer financial conditions. If we make different judgments or utilize different estimates, then material differences may result in additional reserves for trade receivables, which would be reflected by charges in general and administrative expenses for any period presented. We write-off a receivable after all collection efforts have been exhausted and the amount is deemed uncollectible.

Leases

Lease agreements are evaluated to determine whether they are capital or operating leases in accordance with ASC 840, Leases. When any one of the four test criteria in ASC 840 is met, the lease then qualifies as a capital lease.

Capital leases are capitalized at the lower of the net present value of the total amount payable under the leasing agreement (excluding finance charges) or the fair market value of the leased asset. Capital lease assets are depreciated on a straight-line basis, over a period consistent with our normal depreciation policy for tangible fixed assets, but not exceeding the

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lease term. Interest charges are expensed over the period of the lease in relation to the carrying value of the capital lease obligation.

Rent expense for operating leases, which may include free rent or fixed escalation amounts in addition to minimum lease payments, is recognized on a straight-line basis over the duration of each lease term.

Recent Tax Legislation

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (Tax Act). The Tax Act revised the taxation of U.S. and multinational corporations which significantly reduced the statutory corporate U.S. federal income tax rate from 35% to 21%, imposed limitations on the ability of corporations to deduct interest expense and made taxation changes on U.S. multinational corporation's foreign operations. The provisions of the Tax Act are complex and likely will be subject to regulatory and administrative guidance. As we have a fiscal year end of June 30, the lower corporate tax rate will be phased in, resulting in a U.S. statutory federal rate of approximately 28% for our fiscal year 2018 and 21% for subsequent fiscal years. As part of the transition to the new territorial tax system, the Tax Act imposed a one-time repatriation tax on the mandatory deemed repatriation of cumulative earnings of foreign subsidiaries. In addition, the reduction of the U.S. corporate tax rate will cause us to adjust our U.S. deferred tax assets and liabilities to the lower federal base rate of 21%. Because ASC 740-10-25-47 requires the effect of a change in tax laws or rates to be recognized as of the date of enactment, we remeasured our deferred tax assets and liabilities as well as our offsetting valuation allowance in the current period. There was no impact to tax expense as the remeasurement of net deferred tax assets was completely offset by a corresponding change in valuation allowance. The reduction to U.S. deferred tax assets and the offsetting valuation allowance was $26.6 million. We did not incur a tax liability from the deemed repatriation of accumulated foreign earnings due to a net overall accumulated deficit in foreign earnings and profits. The Tax Act includes a provision to tax global intangible low-taxed income (GILTI) of foreign subsidiaries and a base erosion anti-abuse tax (BEAT) measure that taxes certain payments between a U.S. corporation and its foreign subsidiaries. The GILTI and BEAT provisions of the Act will be effective for us as of July 1, 2018 (our fiscal year 2019).

Fiscal Year 2018 Compared with Fiscal Year 2017

Our effective tax rate for fiscal years 2018 and 2017 was a tax benefit rate of 8.6% and a tax provision rate of 9.7%, respectively. The change in our effective tax rate for fiscal year 2018 as compared to fiscal year 2017 was primarily due to the rate change related to the enactment of the Tax Act in fiscal year 2018, change in valuation allowance, foreign rate differential, stock based compensation and the research and development tax credit.

The loss before income tax benefit (provision) between the U.S. and foreign countries impacted our effective tax rate as a result of the geographic distribution and customer demand related to our products and services. In fiscal year 2018, our U.S. loss and foreign loss before our net income tax benefit was $587,000 and $1.6 million, respectively. In fiscal year 2017, our U.S. loss and foreign loss before our net income tax provision was $5.1 million and $339,000, respectively.

Fiscal Year 2017 Compared with Fiscal Year 2016

Our effective tax rate for fiscal years 2017 and 2016 was a tax provision rate of 9.7% and a tax benefit rate of 12.1%, respectively. The change in our effective tax rate for fiscal year 2017 as compared to fiscal year 2016 was primarily due to a foreign rate differential, stock based compensation and change in valuation allowance.

The loss before income tax benefit (provision) between the U.S. and foreign countries impacted our effective tax rate as a result of the geographic distribution and customer demand related to our products and services. In fiscal year

2017, our U.S. loss and foreign loss before our net income tax provision was $5.1 million and $339,000, respectively. In fiscal year 2016, our U.S. loss and foreign income before our net income tax benefit was $11.8 million and $4.7 million, respectively.

Deferred Tax Valuation Allowance

When we prepare our consolidated financial statements, we estimate our income tax liability for each of the various jurisdictions where we conduct business. This requires us to estimate our actual current tax exposure and to assess temporary differences that result from differing treatment of certain items for tax and accounting purposes. The net deferred

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tax assets are reduced by a valuation allowance if, based upon weighted available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. We make significant judgments to determine our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance to be recorded against our net deferred tax assets. As of June 30, 2018, we had a valuation allowance of approximately $57.1 million of which approximately $54.2 million was attributable to U.S. and state net operating losses and domestic research and development credit carryforwards.

We apply ASC 740, Income Taxes, in determining any uncertain tax positions. The guidance seeks to reduce the diversity in practice associated with certain aspects of measurement and recognition in accounting for income taxes and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position that an entity takes or expects to take in a tax return. Additionally, ASC 740 provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Under ASC 740, an entity may only recognize or continue to recognize tax positions that meet a “more likely than not” threshold. In accordance with our accounting policy, we recognize accrued interest and penalties related to unrecognized tax benefits as a component of other income (expense), net in the consolidated statements of operations.

Fair Value of Financial Instruments

Our financial instruments consist of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities. We do not have any derivative financial instruments. We believe the reported carrying amounts of these financial instruments approximate fair value, based upon their short-term nature and comparable market information available at the respective balance sheet dates. The carrying value of our bank borrowings and capital lease obligations approximates fair value based on the borrowing rates currently available to us for loans and capital leases with similar terms.

Results of Operations

The following table sets forth certain items reflected in our consolidated statements of operations expressed as a percent of total revenue for the periods indicated.

	2018		2017		2016	
Revenue:						
Recurring	83	%	75	%	62	%
Legacy license	1	%	8	%	21	%
Professional services	16	%	17	%	17	%
Total revenue	100	%	100	%	100	%
Cost of revenue:						
Cost of recurring	21	%	20	%	18	%
Cost of legacy license	0	%	0	%	0	%
Cost of professional services	15	%	16	%	16	%
Total cost of revenue	36	%	36	%	34	%
Gross profit	64	%	64	%	66	%
Operating Expenses:						
Research and development	24	%	24	%	23	%
Sales and marketing	29	%	35	%	40	%
General and administrative	13	%	11	%	11	%
Total operating expenses	66	%	70	%	74	%

Loss from operations	(2)	%	(6)	%	(8)	%

Revenue

Total revenue, which consists of recurring, legacy license and professional services revenue, was $61.3 million, $58.2 million, and $69.4 million, in fiscal years 2018, 2017, and 2016, respectively.

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In fiscal year 2018, total revenue increased 5% or $3.1 million from the prior year. The increase in recurring revenue in fiscal year 2018 was primarily attributable to the transition from a perpetual license business toward a cloud delivery model. Our international sales accounted for approximately 48% of total revenue in fiscal year 2018, a decrease from 51% of total revenue in fiscal year 2017.

The increase in total revenue in fiscal year 2018 compared to fiscal year 2017 included an increase of $1.7 million related to foreign exchange fluctuation between the U.S. dollar, the Euro and the British pound. The decrease in total revenue in fiscal year 2017 compared to fiscal year 2016 included a decrease of $4.8 million related to foreign exchange fluctuation between the U.S. dollar, the Euro and the British pound.

One customer accounted for 16% of total revenue in fiscal year 2018. One customer accounted for 13% of total revenue in fiscal year 2017. Two customers accounted for 14% and 10% of total revenue in fiscal year 2016.

Recurring Revenue

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Revenue							
Recurring	$ 50,767	$ 43,585	$ 42,783	$ 7,182	16 %	$ 802	2 %
Percentage of total revenue	83 %	75 %	62 %				

Recurring revenue includes cloud, term and ratable licenses, software maintenance and support revenue. Recurring revenue was $50.8 million, $43.6 million, and $42.8 million in fiscal years 2018, 2017, and 2016, respectively. This represented an increase of 16% or $7.2 million in fiscal year 2018 compared to fiscal year 2017 and an increase of 2% or $802,000 in fiscal year 2017 compared to fiscal year 2016. Recurring revenue represented 83%, 75% and 62% of total revenue for the fiscal years 2018, 2017 and 2016, respectively.

Excluding an increase of $1.4 million related to foreign exchange fluctuation, the increase in recurring revenue in fiscal year 2018 was primarily due to our continued progression toward a cloud delivery model from the hybrid model that included legacy perpetual licenses.

Excluding a decrease of $3.4 million related to foreign exchange fluctuation, the increase in recurring revenue in fiscal year 2017 was primarily due to the strategic decision to move to a cloud delivery model from the hybrid model that included legacy perpetual licenses.

Excluding the impact from any future foreign currency fluctuation, we expect recurring revenue to increase in fiscal year 2019 due to the shift from a legacy perpetual license business toward a cloud delivery model.

Legacy license Revenue

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Revenue							
Legacy license	$ 585	$ 4,557	$ 14,466	$ (3,972)	(87) %	$ (9,909)	(68) %

Percentage of total revenue	1 %	8 %	21 %

Legacy license revenue was $585,000, $4.6 million and $14.5 million in fiscal years 2018, 2017 and 2016, respectively. This represented a decrease of 87% or $4.0 million in fiscal year 2018 from fiscal year 2017, compared to a decrease of 68% or $9.9 million in fiscal year 2017 from fiscal year 2016. Legacy license revenue represented 1%, 8%, and 21% of total revenue for the fiscal years 2018, 2017 and 2016, respectively.

Excluding an increase of $59,000 related to foreign exchange fluctuation, the decrease in legacy license revenue in fiscal year 2018 was primarily attributable to the transition from a perpetual license business toward a cloud delivery model.

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Excluding a decrease of $418,000 related to foreign exchange fluctuation, the decrease in legacy license revenue in fiscal year 2017 was primarily attributable to the transition from a perpetual license business toward a cloud delivery model.

We no longer sell legacy licenses to new customers and continue to migrate existing legacy license customers to our cloud delivery model. We anticipate legacy license revenue to decrease in fiscal year 2019.

Professional Services Revenue

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Revenue							
Professional services	$ 9,955	$ 10,073	$ 12,126	$ (118)	(1) %	$ (2,053)	(17) %
Percentage of total revenue	16 %	17 %	17 %				

Professional services revenue was $10.0 million, $10.1 million, and $12.1 million in fiscal years 2018, 2017 and 2016, respectively. This represented a decrease of 1% or $118,000 in fiscal year 2018 compared to fiscal year 2017 and a decrease of 17% or $2.1 million in fiscal year 2017 compared to fiscal year 2016.

Excluding an increase of $259,000 related to foreign exchange fluctuation, the decrease in professional services revenue in fiscal year 2018 was primarily attributable to a continued reduction in time required for an average implementation project as a result of the improvements to our product deployment process. In addition, our cloud deployment requires less professional services as compared to our on-premise deployment.

Excluding a decrease of $987,000 related to foreign exchange fluctuation, the decrease in professional services revenue in fiscal year 2017 was primarily attributable to a continued reduction in time required for an average implementation project as a result of the improvements to our product deployment process. In addition, our cloud deployment requires less professional services as compared to our on-premise deployment.

Excluding the impact from any future foreign currency fluctuation, we expect professional services revenue to decrease in fiscal year 2019.

Cost of Revenue

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Cost of revenue	$ 22,336	$ 21,199	$ 23,689	$ 1,137	5 %	$ (2,490)	(11) %
Percentage of total revenue	36 %	36 %	34 %				
Gross margin	64 %	64 %	66 %				

Total cost of revenue was $22.3 million, $21.2 million, and $23.7 million in fiscal years 2018, 2017 and 2016, respectively. This represented an increase of 5% or $1.1 million in fiscal year 2018 compared to fiscal year 2017 and a decrease of 11% or $2.5 million in fiscal year 2017 compared to fiscal year 2016.

Total cost of revenue as a percentage of total revenue was 36%, 36% and 34% for fiscal years 2018, 2017 and 2016, respectively.

Excluding an increase of $395,000 related to foreign exchange fluctuation of the U.S. dollar against the Euro, British pound and Indian rupee, the increase in cost of revenue in fiscal year 2018 was primarily due to increases of (i) $822,000 in cloud related expenses due to incremental costs incurred while migrating from the use of traditional data centers to web-based services; (ii) $61,000 in outside consulting services; and (iii) $27,000 in license related expenses; partially offset by a decrease of $168,000 in personnel and personnel-related expenses primarily in professional services related to the improved efficiency in customer system implementations.

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Excluding a decrease of $1.4 million related to foreign exchange fluctuation of the U.S. dollar against the Euro, British pound and Indian rupee, the decrease in fiscal year 2017 was primarily due to decreases of (i) $1.4 million in personnel and personnel-related expenses primarily in professional services related to the improved efficiency in customer system implementations; and (ii) $438,000 in outside consulting services; partially offset by increases of (a) $676,000 in cloud related expenses due to increased costs incurred to migrate from the use of traditional data centers to web-based services; and (b) $22,000 in license related expenses.

Gross margin was 64%, 64% and 66% for fiscal years 2018, 2017 and 2016, respectively.

In order to better understand the changes within our cost of revenue and resulting gross margins, we have provided the following discussion of the individual components of our cost of revenue.

Cost of Recurring

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Cost of recurring	$ 13,075	$ 11,956	$ 12,401	$ 1,119	9 %	$ (445)	(4) %
Percentage of recurring revenue	26 %	27 %	29 %				
Gross margin	74 %	73 %	71 %				

Cost of recurring revenue includes personnel costs for our cloud services and maintenance and support, and to a lesser extent occupancy costs and related overhead. Cost of recurring revenue also includes depreciation of capital equipment used in our hosted network, cost of support for third-party software, and lease costs for remote co-location centers.

Total cost of recurring revenue was $13.1 million, $12.0 million, and $12.4 million in fiscal years 2018, 2017 and 2016, respectively. This represented an increase of 9% or $1.1 million in fiscal year 2018 compared to fiscal year 2017 and a decrease of 4%, or $445,000 in fiscal year 2017 compared to fiscal year 2016. Total cost of recurring revenue as a percentage of total recurring revenue was 26%, 27% and 29% in fiscal years 2018, 2017 and 2016, respectively. Gross margin was 74%, 73% and 71% in fiscal years 2018, 2017 and 2016, respectively.

Excluding an increase of $199,000 related to foreign exchange fluctuation, the increase in cost of recurring revenue in fiscal year 2018 was primarily due to increases of (i) $822,000 in cloud related expenses due to increased costs incurred to migrate from the use of traditional data centers to web-based services; and (ii) $164,000 in personnel and personnel-related expenses; partially offset by a decrease of $65,000 in outside consulting services.

Excluding a decrease of $689,000 related to foreign exchange fluctuation, the decrease in cost of recurring revenue in fiscal year 2017 was primarily due to decreases of (i) $252,000 in personnel and personnel-related expenses; and (ii) $180,000 in outside consulting services; partially offset by an increase of $676,000 in cloud related expenses due to increased costs incurred to migrate from the use of traditional data centers to web-based services.

Excluding the impact from any future foreign currency fluctuations, we anticipate cost of recurring revenue to increase in fiscal year 2019.

Cost of Legacy License

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Cost of legacy license	$ 77	$ 50	$ 29	$ 27	54 %	$ 21	72 %
Percentage of legacy license revenue	13 %	1 %	0 %				
Gross margin	87 %	99 %	100 %				

Cost of legacy license primarily includes third-party software royalties and delivery costs for shipments to customers. Total cost of legacy license was $77,000, $50,000 and $29,000 in fiscal years 2018, 2017 and 2016, respectively. This represented an increase of 54% or $27,000 in fiscal year 2018 compared to 2017 and an increase of 72% or $21,000 in

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fiscal year 2017 compared to 2016. Total cost of legacy license as a percentage of total legacy license revenue was 13%, 1% and 0% in fiscal years 2018, 2017 and 2016, respectively. Gross margin was 87%, 99% and 100% in fiscal years 2018, 2017 and 2016, respectively.

We anticipate cost of legacy license to remain relatively constant in future periods but to increase as a percentage of legacy license revenue as we expect legacy license revenue to decline.

Cost of Professional Services

	Fiscal Year Ended June 30			Year-Over-Year Change			
	2018	2017	2016	2017 to 2018		2016 to 2017	
	(in thousands)						
Cost of professional services	$ 9,184	$ 9,193	$ 11,259	$ (9)	(0) %	$ (2,066)	(18) %
Percentage of professional services	92 %	91 %	93 %				
Gross margin	8 %						