

Synacor, Inc.  
Form 10-K  
March 22, 2017

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 December 31, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-33843

Synacor, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	16-1542712 (I.R.S. Employer Identification No.)
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40 La Riviere Drive, Suite 300 Buffalo, New York (Address of principal executive offices)	14202 (Zip Code)
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(716) 853-1362

(Registrant's telephone number, including area code)

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

(Title of each class)	(Name of each exchange on which registered)
Common Stock, \$0.01 par value	The Nasdaq Global Market

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

None.

(Title of Class)

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 the 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) 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, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

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

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

The aggregate market value of shares of common stock held by non-affiliates as of June 30, 2016, the last business day of the registrant's most recently completed second fiscal quarter, computed by reference to the closing sale price of \$3.08 per share on The Nasdaq Global Market on June 30, 2016, was approximately \$73,566,083. For purposes of this disclosure, shares of common stock held by persons who held more than 10% of the outstanding shares of common stock at such time and shares held by executive officers and directors of the registrant have been excluded because such persons may be deemed to be affiliates. This determination of executive officer or affiliate status is not

necessarily a conclusive determination for other purposes.

As of March 16, 2017, there were 31,484,756 shares of the registrant's common stock issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of the definitive Proxy Statement to be used in connection with the registrant's 2017 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K to the extent stated. That Proxy Statement will be filed within 120 days of registrant's fiscal year ended December 31, 2016.

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## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K includes forward-looking statements that reflect our current views with respect to future events or our future financial performance, are based on information currently available to us, and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. All statements, other than statements of historical fact, are statements that could be deemed forward-looking statements, including statements containing the words “believes,” “can,” “expects,” “anticipates,” “estimates,” “intends,” “objective,” “plans,” “possibly,” “potential,” “predicts,” “likely,” “may,” “might,” “would,” “should,” “could,” and similar expressions or phrases (including the negatives of such expressions or phrases). We intend all such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, statements in the sections of this Annual Report on Form 10-K titled “Trends Affecting Our Business” and “Key Initiatives” as well as statements about:

- our expected future financial performance;
- our expectations regarding our operating expenses;
- our strategies and business plan;
- our ability to maintain or broaden relationships with existing customers and develop relationships with new customers;
- our success in anticipating market needs or developing new or enhanced services and products to meet those needs;
- our expectations regarding market acceptance of our services and products;
- our ability to recruit and retain qualified technical and other key personnel;
- our competitive position in our industry, as well as innovations by our competitors;
- our success in managing growth;
- our expansion in international markets;
- our ability to successfully integrate assets and personnel from our acquisitions;
- our success in identifying and managing potential acquisitions;
- our capacity to protect our confidential information and intellectual property rights;
- our need to obtain additional funding and our ability to obtain funding in the future on acceptable terms; and
- anticipated trends and challenges in our business and the markets in which we operate.

Any forward-looking statements contained in this Annual Report on Form 10-K are based upon our historical performance and our current plans, estimates and expectations. The inclusion of this forward-looking information should not be regarded as a representation by us or any other person that the future plans, estimates or expectations contemplated by us will be achieved. All forward-looking statements involve risks, assumptions and uncertainties. Given these risks, assumptions and uncertainties, you should not place undue reliance on any forward-looking statements. The occurrence of the events described, and the achievement of the expected results, depend on many factors, some or all of which are not predictable or within our control.

Actual results may differ materially from expected results. See “Risk Factors” and elsewhere in this Annual Report on Form 10-K for a more complete discussion of these risks, assumptions and uncertainties and for other risks, assumptions and uncertainties. These risks, assumptions and uncertainties are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward-looking statements.

Other unknown or unpredictable factors also could harm our results. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this Annual Report on Form 10-K might not occur, and we therefore qualify all of our forward-looking statements by these cautionary statements. Any forward-looking statement

made by us in this Annual Report on Form 10-K speaks only as of the date on which it is made. Except as required by law, we undertake no obligation to update publicly or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Unless expressly indicated or the context requires otherwise, the terms “Synacor,” “Company,” “we,” “us,” and “our” in this document refer to Synacor, Inc., a Delaware corporation, and, where appropriate, our wholly-owned subsidiaries.

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## PART I

### ITEM 1. BUSINESS

#### Our Business

We enable our customers to better engage with their consumers. Our customers include video, internet and communications providers, device manufacturers, governments and enterprises. We are their trusted technology development, multiplatform services and revenue partner. Our customers use our technology platforms and services to scale their businesses and extend their subscriber relationships. We deliver managed portals, advertising solutions, email and collaboration platforms, end-to-end video solutions and cloud-based identity management.

We enable our customers to provide their consumers engaging, multiscreen experiences with products that require scale, actionable data and sophisticated implementation. Through our Managed Portals and Advertising solutions, we enable our customers to earn incremental revenue by monetizing media among their consumers. At the same time, because consumers have high expectations for their online experience as a result of advances in video, mobile and social, we provide, through our Recurring and Fee-Based Revenue solutions, a suite of products and services that helps our customers successfully meet those high expectations by enabling them to deliver to their consumers access to the same digital content across all devices, including PCs, tablets, smartphones and connected TVs.

#### Products and Services

Our Managed Portals and Advertising solutions provide our customers with substantial revenue opportunities generated by their consumers' engagement across devices. Managed Portals and Advertising solutions generated 59% of our revenue for 2016.

Our Managed Portals are intended to be daily destinations for consumers and are delivered across devices and under our customers' own brand names. To help our customers increase their consumers' engagement, we deliver relevant content, such as top news, entertainment, and long- and short-form video and apps, on our Managed Portals. We have licensing and distribution agreements with a wide range of programmers and content and service providers. In addition, consumers have the ability through our portals to manage their email and messaging, pay bills, receive special promotions and perform other account management needs.

We monetize the online traffic generated by consumers through search advertising, digital advertising (including video), and syndicated content on our Managed Portals. As we monetize our customers' online traffic on our Managed Portals, we share a portion of this revenue with our customers, resulting in a mutually beneficial partnership.

Our Recurring and Fee-Based Revenue solutions generated 41% of our revenue for 2016 and are comprised of our End-to-End Advanced Video Services, Email/Collaboration Services, and paid content and premium services:

End-to-End Advanced Video Services include our Cloud ID Authentication Platform and Search & Discovery Metadata Platform. Our End-to-End Advanced Video Services offering is a highly-reliable, economically efficient, managed service that enables our customers to provide their consumers with TV Everywhere and multiscreen Over The Top (OTT) services.

#### Cloud ID Authentication

Consumers can watch TV on a myriad of devices, but many find the login process frustrating. Synacor Cloud ID addresses this issue by offering home-based auto-authentication and social login, which improve the consumer experience by reducing login failures.

## Search & Discovery Metadata Platform

Once a consumer is authenticated, our Search & Discovery Metadata Platform helps them find their desired content successfully and easily. We curate videos every day and have compiled more than 2.2 million long- and short-form videos from hundreds of sources. We believe that we fill an important role for our customers as use of streaming video increases and consumers' video content consumption preferences shift away from traditional viewing habits.

Our Email/Collaboration Services include white-label hosting, security and migration. With the acquisition of certain assets related to the Zimbra Email/Collaboration products and services business (the "Zimbra assets" or "Zimbra") in 2015, our software and managed service offering now supports a network of over 1,000 value-added resellers, or VARs, over 500 Business Service Providers, or BSPs, and over 3,500 enterprise, government and nonprofit customers, and it powers approximately 530 million mailboxes.

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## Recent Developments

In March 2017 we announced that Windstream, a top-10 U.S.-based service provider, has selected Synacor and our Zimbra platform, to be Windstream's hosted email provider. Windstream's residential high-speed internet customers will use Synacor's email offering. We also announced in March 2017 that another regional service provider has selected Synacor's end-to-end video platform to deliver their TV Everywhere experience.

## Our Strategy

Our strategy is, with operational and financial discipline, to:

- increase value for existing customers by optimizing consumer experience and monetization;
- innovate on Synacor-as-a-platform for advanced services;
- win new customers in current and related verticals; and
- extend our product portfolio into emerging growth areas.

Increasing value for existing customers by optimizing user experience and monetization

With respect to our Managed Portals and Advertising solutions, 92% of our customers' consumers have upgraded to our latest-generation portal, driving a 15% increase in year-over-year engagement. Our portal, with its engaging user experience and responsive design for desktop and mobile web, and our mobile apps, have video threaded throughout and is designed to optimize consumer engagement and monetization. We are also decreasing the implementation time for customers to launch our latest-generation portal.

## Innovating on Synacor-as-a-platform for advanced services

Our Cloud ID Authentication platform is reported as having some of the highest consumer login success rates in the industry.

In 2016, we extended our Cloud ID relationships to content providers, OTT players, and device manufacturers. We delivered Authentication services for HBO GO, providing, for example, authentication in connection with the Game of Thrones' record-breaking sixth season and finale. Additionally, Apple uses Synacor's Authentication services to support Apple Single Sign-On. The current wave of MVPDs launched by Apple are almost all running on Synacor's Cloud ID Advanced Authentication platform. Our Authentication services also support Sling TV, PlayStation Vue and others to simplify the consumer log-in experience.

We believe we fill an important role as the number of streaming video consumers increases because we believe that our customers are looking for a single vendor with whom to work, not a balkanized group of vendors. We created a professional services team to work with partners to support the delivery of our End-to-End Advanced Video Services. Our acquisition of the assets of NimbleTV in 2015 also resulted in innovation in our End-to-End Advanced Video Services. Our acquisitions of the Zimbra assets in 2015 and certain assets from Technorati in 2016 resulted in innovations in our email/collaboration and digital advertising capabilities, respectively.

## Winning new customers in current and related verticals

We have an established presence among broadband and pay-TV providers in the U.S. and Canada. Some of these providers use our complete suite of solutions, and others use only certain components. We view this as a growth opportunity within our existing customer base.

On May 4, 2016, we announced that AT&T selected Synacor to develop AT&T's new multiplatform digital experience to enhance user engagement and experience. The new multiplatform experiences integrate multiple avenues for monetization including a combination of targeted banner advertising, pre-roll video ads and popular promoted content. We expect that our partnership with AT&T will create a virtuous cycle that benefits all our current customers, and makes Synacor platforms more attractive for new customers.

In 2016, we released our iOS and Android video apps for GVTC and Consolidated Communications, which are powered by our end-to-end video platform. These apps enable consumers to watch TV everywhere, video-on-demand and OTT content in and out of the home. Further, we believe our apps are helping our customers drive new subscriptions through improved search and discovery because we enable our customers to transform massive amounts of data into easy-to-access content, and created new ways for consumers to access new services.

## Extending our product portfolio into emerging growth areas

We plan to capitalize on opportunities such as international expansion and delivery of business services. Through our acquisition of the Zimbra assets we have expanded our international customer base, and we believe this represents an opportunity to find new customers for our Managed Portals and Advertising solutions.

## Technology and Operations

### Technology Architecture

To route traffic through our network in the most efficient manner, we use load-balancing products. These products spread work among multiple servers and link controllers that monitor the availability and performance of multiple connections. Our technology is reliable, fault tolerant and scalable through the addition of more servers as usage grows. In 2016 and 2015, we spent \$25.6 million and \$20.0 million, respectively (exclusive of depreciation and amortization) on technology and development activities. The cost of these activities is generally not borne directly by our customers.

### Data Center Facilities

We currently operate and maintain six data centers in regionally diverse locations and have a network operations center that is staffed 24 hours a day, seven days a week. Our primary data centers are located in shared facilities in Atlanta, Georgia; Dallas, Texas; Lewis Center, Ohio; Denver, Colorado; Toronto, Canada and Amsterdam, The Netherlands. All systems are fully monitored for reporting continuity and fault isolation. The data centers are each in a physically secure facility using monitoring, environmental alarms, closed circuit television and redundant power sources. Our network operations center also is located in a secure facility.

## Customers

Our Managed Portals and Advertising customers principally consist of high-speed internet service providers, such as AT&T, Windstream, Mediacom and CenturyLink, as well as consumer electronics manufacturers, such as Toshiba America Information Systems, Inc. (Toshiba). Contracts with these customers typically have an initial term of two to three years from the deployment of our Managed Portals and frequently provide for one or more automatic renewal terms of one to two years each. Our Managed Portals and Advertising customer contracts typically contain service level agreements that call for specific system “up times” and 24 hours per day, seven days per week support. As of December 31, 2016, we had agreements with over 50 Managed Portals and Advertising customers.

Our Recurring and Fee-Based customers consist of high-speed internet service providers along with enterprises, government and nonprofit organizations, either directly or through resellers. Contracts with these customers typically have an initial term of one to three years and frequently provide for one or more automatic renewal terms of one to two years each. Our Recurring and Fee-Based customer contracts also typically contain service level agreements that call for specific system “up times” and 24 hours per day, seven days per week support. As of December 31, 2016, we had agreements, both directly and indirectly through resellers, with over 120 high-speed internet service providers and over 3,500 enterprise, government and nonprofit customers.

Revenue attributable to one customer accounted for 16% of our revenue, or \$20.8 million, in the year ended December 31, 2016.

## Content and Service Providers

We license the content available in our Managed Portals, including free and paid content offerings and premium services, from numerous third-party content and service partners. These partners provide a variety of content, including news and information, entertainment, sports, music, video, games, shopping, travel, autos, careers and finance. Our relationships with content providers give consumers access to over one hundred thousand short-form video and articles each month. To obtain this content, we enter into a variety of licensing arrangements with the content providers. These arrangements are typically one to three years in duration with payment terms that may be based on traffic, advertising revenue share, number of subscribers, flat fee payments over time, or some combination thereof. In addition to using licensed content to populate our Managed Portals, we also provide premium services and paid content that subscribers may purchase for additional fees. As of December 31, 2016, we had arrangements with over 65 content providers, such as The Associated Press, CNN, Tribune Content Agency, Gracenote, and Bankrate.

## Sales and Marketing

### Managed Portals and Advertising Solutions

Our sales and marketing efforts focus on five primary areas: customer acquisitions, client services, account management, marketing and advertising sales. Our customer acquisition team consists of direct sales personnel who call upon prospective customers, typically large and mid-sized high-speed internet service providers and consumer electronics manufacturers. A significant amount of time and effort is devoted to researching and analyzing the requirements and objectives of each prospective customer. Each bid is specifically customized for the prospective customer, and often requires many months of interaction and negotiation before an agreement is reached.

Once an agreement is reached, our client services team, working closely with the customer acquisition team, assumes responsibility for managing the customer relationship during the time of the initial deployment and integration period, which is usually three to six months. During this period, the customer's technology is assessed and, if required, modifications are proposed to make it compatible with our technology. The client services team is responsible for the quality of the client deployment, customer relationship management during the time of deployment, and integration and project management associated with upgrades and enhancements.

After deployment, our account management team takes over management of the customer relationship, analyzing the ways in which a customer could further benefit from increased use of our products and services. The account management team is responsible for ongoing customer relationship management, upgrades and enhancements to the available products and services, as well as tracking the financial elements and performance of the customer relationship.

Our marketing team works closely with our account management team to deliver marketing programs that support our customers' sales efforts as well as their consumers' interaction with these products and services. We assist our customers in developing marketing materials and advertising that can be accessed by consumers through different media outlets, including the internet, print, television and radio. We also assist our customers in training their customer service representatives to introduce and sell premium services and our paid content offerings to new and existing customers.

Our advertising sales team sells advertising inventory directly to advertisers, frequently through the advertising agencies representing those advertisers. These advertisers may be small companies with the advertising locally or regionally focused on the Managed Portals of one customer, or large companies with nationwide advertising on the Managed Portals of many customers. We have a team of direct advertising sales employees and independent advertising sales representatives focused on this effort and will continue to develop this team and attempt to grow the amount of advertising revenue generated with our customers. As of December 31, 2016, we had arrangements with over 100 advertising partners such as AppNexus, Comcast Spotlight, Criteo, DoubleClick, NCC Media, Mediavest, and Tremor Video.

### Email/Collaboration

We market our Email/Collaboration product through both direct and indirect sales channels. Our regional sales and marketing teams host several events each year with partners and run various campaigns to generate sales leads. Once a lead has been identified, our internal sales representatives work closely with our regional partners on better identifying the opportunity and gathering customer requirements.

We sell to internet service providers primarily through a direct sales force consisting of regional account executives. Sales cycles can be six months or longer. We sell to prospective government, nonprofit and enterprise

customers through a two-tier indirect model via over 1,000 VARs and 500 BSPs. Our VARs sell on-premise licenses to end customers while our BSPs sell a cloud service to the end customer. Sales cycles can range from thirty days to six months, depending on size and scope.

#### Government Regulation

We generally are not regulated other than under international, federal, state and local laws applicable to the internet or e-commerce or to businesses in general. Some regulatory authorities have enacted or proposed specific laws and regulations governing the internet and online entertainment. These laws and regulations cover issues such as taxation, pricing, content, distribution, quality and delivery of services and products, electronic contracts, intellectual property rights, user privacy and information security.

Federal laws regarding the internet that could have an impact on our business include the following: the Digital Millennium Copyright Act of 1998, which is intended to reduce the liability of online service providers of third-party content, including content that may infringe copyrights or rights of others; the Children's Online Privacy Protection Act, which imposes additional restrictions on the ability of online services to collect user information from minors; and the Protection of Children from Sexual Predators Act, which requires online service providers to report evidence of violations of federal child pornography laws under certain circumstances.

Laws and regulations regarding user privacy and information security impact our business because we collect and use personal information through our technology. We use this information to deliver more relevant content and services and provide consumers with a personalized online experience. We share this information on an aggregate basis with our customers and content providers and, subject to confidentiality agreements, to prospective customers and content providers. Laws such as the CAN-SPAM Act of 2003 or other user privacy or security laws could restrict our and our customers' ability to market products to their consumers, create uncertainty in internet usage and reduce the demand for our services and products or require us to redesign our Managed Portals.

### Intellectual Property

We believe that the protection of our intellectual property is critical to our success. We rely on copyright, service mark and patent enforcement, contractual restrictions and trade secret laws to protect our proprietary rights. We have entered into confidentiality and invention assignment agreements with our employees and contractors, and nondisclosure agreements with certain parties with whom we conduct business in order to limit access to, and disclosure of, our proprietary information. We have applied for patents to protect certain of our intellectual property. In addition, we have acquired intellectual property, including patents and trademarks, through our acquisitions including Zimbra, Technorati, NimbleTV and Teknision. Our registered service mark in the United States is Synacor ®.

We endeavor to protect our internally-developed systems and maintain our trademarks and service marks. We generally control access to and use of our proprietary software and other confidential information through the use of internal and external controls, including contractual protections with employees, contractors, customers and partners, and our software is protected by United States and international copyright laws.

In addition to legal protections, we believe that factors such as the technological and creative skills of our personnel, new product developments, frequent product enhancements and reliable product support and services are essential to establishing and maintaining a technology leadership position.

### Competition

The market for internet-based services and products in which we operate is highly competitive and involves rapidly-changing technologies and customer and consumer requirements, as well as evolving industry standards and frequent product introductions. While we believe that our technology offers considerable value and flexibility to our customers by helping them to extend their consumer relationships to a wide variety of internet-based services, we face competition at four levels:

- When one of our prospective or existing customers considers another supplier, including one of our partners, for elements of the services or products which we provide.
- When consumers choose to rely on other vendors for similar products and services.
- When content and service providers prefer to establish direct relationships with one or more of our customers.
- When one of our customers decides to make the significant headcount and technology investment to develop products and services in-house similar to those that we provide.

Our technology competes primarily with high-speed internet service providers that have internal information technology staff capable of developing similar solutions in-house.

### Managed Portals and Advertising Solutions

In addition, with respect to our Managed Portals and Advertising solutions, we compete with companies such as Facebook, Inc.; Yahoo! Inc. or Yahoo!; Google; AOL, a division of Verizon, or AOL; Hulu; Netflix; Amazon; and

MSN, a division of Microsoft Corporation, or Microsoft, which have destination websites of their own or are capable of delivering content, service offerings and search or advertising models similar to ours.

We also compete with providers of paid content and services over the internet, especially companies with the capability of bundling paid content and premium services in much the same manner that we do. These companies include WatchESPN, F-Secure Corporation, Exent Technologies Ltd., Zynga Inc., MLB Advanced Media, Symantec Corporation, McAfee, Inc., Activision Blizzard, Inc. and Electronic Arts Inc. In some cases we have performed software integrations with these companies on behalf of our customers or, as in the case of F-Secure Corporation, we have partnered with them in order to offer their services more broadly to all our customers.



We believe the principal competitive factors in our markets include a company's ability to:

- reinforce the brands of our cable, satellite, telecom and consumer electronics customers;
- produce products that are flexible and easy to use;
- offer competitive fees for Managed Portal development and operation;
- generate additional revenue for our customers;
- enable our customers to be involved in designing the "look and feel" of their online presence;
- offer services and products that meet the changing needs of our customers and their consumers, including emerging technologies and standards;
- provide high-quality product support to assist the customer's service representatives; and
- aggregate content to deliver more compelling bundled packages of paid content.

We believe that we distinguish ourselves from potential competitors in three principal ways. First, we provide a white-label solution that, unlike the co-branded approach of most of our competitors, creates a consumer experience that reinforces our customers' and partners' brands. Second, we give customers control over the sign-on process and billing function for a wide range of internet services and content by integrating with their internal systems (where applicable) thereby allowing our customers to "own the consumer." Finally, our solutions are flexible and neutral, meaning that we allow deliverables that are customized to our customers' specific needs, as well as advanced video solutions that are either end-to-end or a la carte.

#### Email/Collaboration

With respect to our Email/Collaboration solutions, we compete primarily with Google and Microsoft in the enterprise and government markets, and with Open-Xchange and OpenWave in the internet service provider markets.

We believe the principal competitive factors in the email/collaboration market include a company's ability to:

- provide customers the ability to perform security and compliance audits of our source code;
- deliver anti-spam, anti-virus and encryption technologies;
- provide products and services at lowest possible total cost of ownership (TCO);
- provide local partners the ability to store data within the legal jurisdiction of the country where their consumers do business;
- provide an enterprise-ready solution suitable for large-scale deployments including such enterprise features such as delegated administration, detailed logging, and performance and availability transparency;
- offer access to real-time performance and availability statistics;
- afford customers and partners the ability to rebrand their cloud collaboration experience; and
- make available to partners both integrations and extensions to the collaboration cloud environment specific to consumers' needs.

We believe that we distinguish ourselves from potential competitors in several ways. First, we offer our Email/Collaboration products and services a la carte, enabling consumers to buy only the services they need, providing for a much lower TCO. Second, our Zimbra Email/Collaboration solution is a complete feature-rich, enterprise-ready solution scalable up to 40 million mailboxes. Finally, our products are customizable and extendable and designed to meet very high standards of security.

#### Employees

As of December 31, 2016, we had 322 employees in the United States and 130 based internationally. Of these employees, 449 were full-time employees. None of our employees are represented by a labor union, and we consider current employee relations to be good.



## Corporate Information

Synacor's predecessor company was originally formed as a New York corporation, and in November 2002, Synacor re-incorporated under the laws of the State of Delaware. Our headquarters are located at 40 La Riviere Drive, Buffalo, New York 14202, and our telephone number is (716) 853-1362.

We have determined that we have a single reporting segment. A summary of our financial information by geographic location is found in Note 7, Information About Segment and Geographic Areas, in the Notes to Consolidated Financial Statements. Our international operations and sales subject us to a variety of risks; see Item 1A, "Risk Factors," for further discussion.

## Available Information

Our internet website address is <http://www.synacor.com>. We provide free access to various reports that we file with or furnish to the Securities and Exchange Commission, or SEC, through our website, as soon as reasonably practicable after they have been filed or furnished. These reports include, but are not limited to, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports. Our SEC reports can be accessed through the investor relations section of our website, or through <http://www.sec.gov>. Information on our website does not constitute part of this Annual Report on Form 10-K or any other report we file or furnish with the SEC. Stockholders may request copies of these documents from:

Synacor, Inc.

Investor Relations Department

40 La Riviere Drive

Suite 300

Buffalo, New York 14202

## ITEM 1A. RISK FACTORS

Our business and financial results are subject to numerous risks and uncertainties, including those described below, which could adversely and materially affect our business, financial condition or results of operations. You should carefully consider these risks and uncertainties, including the following risk factors and all other information contained in this Annual Report on Form 10-K, together with any other documents we file with the SEC.

### Risks Related to Our Business

A loss of any significant Managed Portals and Advertising customer could negatively affect our financial performance.

Although we continue to diversify our product portfolio and our customer base, we continue to derive a substantial portion of our revenue from a small number of Managed Portal customers. Revenue attributable to these customers includes the Recurring and Fee-Based revenue earned directly from them, as well as the search and digital advertising revenue earned through our relationships with our advertising partners, such as Google, based on traffic generated from our Managed Portals. Revenue attributable to CenturyLink, Toshiba, and Verizon Corporate Services Group, Inc., or Verizon together accounted for approximately 49% of our revenue, or \$53.5 million for the year ended December 31, 2015. For 2015, revenue attributable to one of these customers accounted for 20% or more of our revenue, and revenue attributable to each of the other two customers accounted for more than 10% of our revenue. For 2016, revenue attributable to one customer accounted for approximately 16% of our revenue, or \$20.8 million, and no other customer accounted for 10% or more of our revenue for that period.

Our contracts with our Managed Portals and Advertising customers generally have an initial term of approximately two to three years from the launch of their Managed Portals and frequently provide for one or more automatic renewal terms of one to two years each. If a key contract is not renewed or is otherwise terminated, or if revenue from a significant customer declines because of competitive or other reasons, our revenue would decline and our ability to achieve or sustain profitability would be impaired. In addition to the loss of Recurring and Fee-Based revenue, we would also lose significant revenue from the related search and digital advertising services that we provide. In addition to the decline of revenue, we may have to impair our long-lived assets, to the extent that such assets are used exclusively to support these customers, which would adversely impact our results of operations and financial position.

If our delivery of our products and services under our contract with AT&T is executed according to our plan, we expect that, following such delivery, we will derive a substantial portion of our revenue from AT&T, with revenue attributable to AT&T exceeding the revenue attributable to any of our other customers. If our contract with AT&T is not renewed or is otherwise terminated, or if revenue from the AT&T relationship were to decline due to competitive or other reasons, our results of operations and financial position would be adversely affected.

Our search advertising partner, Google, accounts for a significant portion of our revenue, and any loss of, or diminution in, our business relationship with Google would materially and adversely affect our financial performance.

We rely on traffic on our Managed Portals to generate search and digital advertising revenue, a substantial portion of which is derived from text-based links to advertisers' websites as a result of internet searches. We have a revenue-sharing relationship with Google under which we include a Google-branded search tool on our Managed Portals. When a consumer makes a search request using this tool, we deliver it to Google, and Google returns search results to us that include advertiser-sponsored links. If the consumer clicks on a sponsored link, Google receives payment from the sponsor of that link and shares a portion of that payment with us. We then typically share a portion of that payment with the applicable customer. Our Google-related search advertising revenue attributable to our customers, which consists of the portion of the payment from the sponsor that Google shares with us, accounted for approximately 12%, 28%, and 42% of our revenue in 2016, 2015, and 2014 or \$15.9 million, \$31.2 million, and \$45.4

million respectively. Our agreement with Google was extended in December 2016 for an additional twelve-month period and expires in February 2018 unless we and Google mutually elect to renew it. Additionally, Google may terminate our agreement if we experience a change in control, if we enter into an agreement providing for a change in control, if we do not maintain certain search and digital advertising revenue levels or if we fail to conform to Google's search policies and advertising policies. Google may from time to time change its existing, or establish new, methodologies and metrics for valuing the quality of internet traffic. Any changes in these methodologies, metrics and advertising technology platforms could decrease the advertising rates that we receive and/or the amount of revenue that we generate from digital advertisements. If advertisers were to discontinue their advertising via internet searches, if Google's revenue from search-based advertising were to decrease, if Google's share of the search revenue were to be increased or if our agreement with Google were to be terminated for any reason or renewed on less favorable terms, our business, financial condition and results of operations would be materially and adversely affected. Moreover, consumers' increased use of search tools other than the Google-branded search tool we provide would have similar effects.

We have a history of significant pre-tax net losses and may not be profitable in future periods, which would limit our ability to use our net operating loss carryforwards.

We have reported pre-tax net income in only three years, 2009, 2011 and 2012, in amounts of \$0.3 million, \$3.9 million, and \$5.6 million, respectively. In all other years, we have incurred losses, and at December 31, 2016 our cumulative net operating loss carryforward totals approximately \$14 million. We have taken cost saving measures, including a reduction in workforce carried out in September 2014. However, our expenses may increase in future periods as we implement initiatives designed to grow our business including, among other things, the start-up and product development expenses we will incur in connection with providing Managed Portal and Advertising solutions to AT&T, acquisitions of complementary businesses (such as our acquisition of the Zimbra assets and our acquisition of assets from Technorati), the development and marketing of new services and products, licensing of content, expansion of our infrastructure and international expansion. If our revenue does not sufficiently increase to offset these expected increases in operating expenses, we may incur significant losses and may not be profitable. For example, although our revenue in 2016 increased as compared to 2015 and our revenue in 2015 increased as compared to 2014, we have not yet returned to profitability. We may not be able to return to or maintain profitability in the future. Any failure to achieve or maintain profitability may materially and adversely affect our business, financial condition, results of operations and impact our ability to utilize our net operating loss carryforwards. As a result of our pre-tax cumulative losses, we have established a full valuation allowance against our deferred income tax asset, which includes our net operating loss carryforwards.

Many individuals are using devices other than personal computers and software applications other than internet browsers to access the internet. If users of these devices and software applications do not widely adopt the applications and other solutions we develop for them, our business could be adversely affected.

The number of people who access the internet through devices other than PCs, including tablets, smartphones and connected TVs, has increased dramatically in the past few years and is projected to continue to increase. Similarly, individuals are increasingly accessing the internet through apps other than internet browsers, such as those available for download through Apple Inc.'s App Store and the Android Market. Our Managed Portals include our responsive desktop and mobile web products and also our mobile native iOS and Android apps. If consumers do not use our mobile products at all or use these products less frequently than previously, our financial results could be negatively affected. Additionally, as new devices and new apps are continually being released, it is difficult to predict the problems we may encounter in developing new versions of our apps and other solutions for use on these alternative devices and apps, and we may need to devote significant resources to the creation, support and maintenance of such apps and solutions. If users of these devices and apps do not widely adopt the apps and other solutions we develop, our business, financial condition and results of operations could be adversely affected.

Consumer tastes continually change and are unpredictable, and sales of our Managed Portals and Advertising solutions may decline if we fail to enhance our service and content offerings to achieve continued consumer acceptance.

Our business depends on aggregating and providing services and content that our customers will place on our Managed Portals, including television programming, news, entertainment, sports and other content that their consumers find engaging, and premium services and paid content that their consumers will buy. Accordingly, we must continue to invest significant resources in licensing efforts, research and development and marketing to enhance our service and content offerings, and we must make decisions about these matters well in advance of product releases to implement them in a timely manner. Our success depends, in part, on unpredictable and volatile factors beyond our control, including consumer preferences, competing content providers and websites and the availability of other news, entertainment, sports and other services and content. While we work with our customers to have their consumers' homepages set to our Managed Portals, a consumer may easily change that setting, which would likely decrease the

use of our Managed Portals. Similarly, consumers who change their device's operating system or internet browser may no longer have our Managed Portals set as their default homepage, and unless they change it back to our Managed Portals, their usage of our Managed Portals would likely decline and our results of operations could be negatively impacted. Consumers who acquire new consumer electronics devices will no longer have our Managed Portals initially set as their default homepage, and unless they change the default to our Managed Portals, their usage of our Managed Portals would likely decline and our results of operations could be negatively impacted.

If our services are not responsive to the requirements of our customers or the preferences of their consumers, or the services are not brought to market in a timely and effective manner, our business, financial condition and results of operations would be harmed. Even if our services and content are successfully introduced and initially adopted, a subsequent shift in the preferences of our customers or their consumers could cause a decline in the popularity of our services and content that could materially reduce our revenue and harm our business, financial condition and results of operations.

Our revenue growth will be adversely affected if we are unable to expand the breadth of our services and products or to introduce new services and products on a timely basis.

To retain our existing customers, attract new customers and increase revenue, we must continue to develop and introduce new services and products on a timely basis and continue to develop additional features to our existing product base. For example, under our relationship with AT&T, we have agreed to deliver a number of additional products and services to AT&T's consumers. If our existing and prospective customers do not perceive that we will deliver our services and products on schedule, or if they do not perceive our services and products to be of sufficient value and quality, we may lose the confidence of our existing customers and fail to increase sales to these existing customers, existing customers may be able to terminate their agreements with us, and we may not be able to attract new customers, each of which would adversely affect our operating results.

Our sales cycles and the contracting process with new customers are long and unpredictable and may require us to incur expenses before executing a customer agreement, which makes it difficult to project when, if at all, we will obtain new customers and when we will generate additional revenue and cash flows from those customers.

We market our services and products directly to high-speed internet service and communications providers, consumer electronics manufacturers, and directly and indirectly to enterprises, and governmental and nonprofit organizations. New customer relationships typically take time to obtain and finalize because of the burdensome cost of migrating from an existing solution to our platform. Due to operating procedures in many organizations, a significant time period may pass between selection of our services and products by key decision-makers and the signing of a contract. The length of time between the initial customer sales call and the realization of significant sales is difficult to predict and can range from several months to several years. As a result, it is difficult to predict when we will obtain new customers and when we will begin to generate revenue and cash flows from these potential new customers.

As part of our sales cycle for our Managed Portals and Advertising customers, we may incur significant expenses in the form of compensation and related expenses and equipment acquisition before executing a definitive agreement with a prospective customer so that we may be ready to launch shortly following execution of a definitive agreement. If conditions in the marketplace generally or with a specific prospective customer change negatively, it is possible that no definitive agreement will be executed, and we will be unable to recover any expenses incurred before a definitive agreement is executed, which would in turn have an adverse effect on our business, financial condition and results of operations.

Many of our customers are high-speed internet service providers, and consolidation within the cable and telecommunications industries could adversely affect our business, financial condition and results of operations.

Our revenue from high-speed internet service and communications providers, including our search and digital advertising revenue generated by online consumer traffic on our Managed Portals and our revenue from our Email/Collaboration offerings, accounted for approximately 63% in 2016, approximately 82% in 2015 and approximately 85% in 2014. The cable and telecommunications industries have experienced consolidation over the past several years, and we expect that this trend will continue. As a result of consolidation, some of our customers may be acquired by companies with which we do not have existing relationships and which may have relationships with one of our competitors or may have the in-house capacity to perform the services we provide. As a result, such acquisitions could cause us to lose customers and the associated revenue. Under our agreements with some of our customers, including CenturyLink, they have the right to terminate the agreement if we are acquired by one of their competitors.

Consolidation may also require us to renegotiate our agreements with our customers as a result of enhanced customer leverage. We may not be able to offset the effects of any such renegotiations, and we may not be able to attract new



customers to counter any revenue declines resulting from the loss of customers or their subscribers.

We rely, to a significant degree, on indirect sales channels for the distribution of our Email/Collaboration products, and disruption within these channels could adversely affect our business, financial condition, operating results and cash flows.

We use a variety of indirect distribution methods for our offerings, including channel partners, such as cloud service providers, distributors, and value added resellers. A number of these partners in turn distribute our offerings via their own networks of channel partners with whom we have no direct relationship. These relationships allow us to offer our technologies to a much larger customer base than we would otherwise be able through our direct sales and marketing efforts.

We rely, to a significant degree, on each of our channel partners to select, screen and maintain relationships with its distribution network and to distribute our offerings in a manner that is consistent with applicable law and regulatory requirements and our quality standards. If our channel partners or a partner in its distribution network violate applicable law or regulatory requirements or misrepresent the functionality of our offerings, our reputation could be damaged and we could be subject to potential liability. Furthermore, our channel partners may offer their own products and services that are competitive with our offerings or may not distribute and market our offerings effectively. Our existing channel partner relationships do not, and any future channel partner relationships may not, afford us any exclusive marketing or distribution rights. In addition, if a channel partner is acquired by a competitor or its business units are reorganized or divested, our revenue derived from that partner may be adversely impacted.

Recruiting and retaining qualified channel partners and training them in the use of our technologies require significant time and resources. If we fail to devote sufficient resources to support and expand our network of channel partners, our business may be adversely affected. In addition, because we rely on channel partners for the indirect distribution of our technologies, we may have little or no contact with the ultimate end-users of our technologies, thereby making it more difficult for us to establish brand awareness, ensure proper delivery and installation of our software, support ongoing customer requirements, estimate end-user demand, respond to evolving customer needs and obtain renewals from end-users.

Most of our sales to government entities have been made indirectly through our channel partners. Government entities may have statutory, contractual, or other legal rights to terminate contracts with our channel partners for convenience or due to a default, and any such termination may adversely impact our future operating results. Governments routinely investigate and audit government contractors' administrative processes, and any unfavorable audit could result in the government refusing to continue buying our offerings, a reduction of revenue or fines or civil or criminal liability if the audit uncovers improper or illegal activities.

If our indirect distribution channel is disrupted, we may be required to devote more resources to distribute our offerings directly and support our customers, which may not be as effective and could lead to higher costs, reduced revenue and growth that is slower than expected.

As technology continues to evolve, the use of our products by our current and prospective consumer electronics manufacturer customers may decrease and our business could be adversely affected.

The consumer electronics industry is subject to rapid change, and our contracts for Managed Portals and Advertising solutions with our consumer electronics manufacturer customers are not exclusive. As consumer electronics manufacturers continue to develop new technologies and introduce new models and devices, there can be no assurance that we will be able to develop solutions that will persuade consumer electronics manufacturers that are our customers at such time to utilize our technology for those new devices. If our current and prospective consumer electronics manufacturer customers elect not to integrate our solutions into their new products, our business, financial condition and results of operations could be adversely affected.

Moreover, updates to internet browser technology may adversely affect our business. For example, for our consumer electronics manufacturer customers that have the Windows 8 operating system pre-installed on some of their devices, the Windows 8 operating system places our Managed Portal on a second tab when the internet browser is launched, leading to decreased search and digital advertising revenue. Further, upgrades to the Windows 10 operating system default to Microsoft's latest Edge browser and displace users' previous browser settings including default homepages, which can also lead to decreased search and digital advertising revenue. Unless consumers change their browser settings back to our Managed Portals, their usage of our Managed Portals would likely decline and our results of operations could be negatively impacted.

We invest in features and functionality designed to increase consumer engagement with our Managed Portals; however, these investments may not lead to increased revenue.

Our future growth and profitability will depend in large part on the effectiveness and efficiency of our efforts to provide a compelling consumer experience that increases consumer engagement with our Managed Portals. We have made and will continue to make substantial investments in features and functionality for our technology that are designed to drive consumer engagement. We expect we will have invested a total of approximately \$10 million through March 31, 2017 in start-up expenses, development expenses and capital expenditures relating to our contract with AT&T, including approximately \$8.2 million invested in the year ended December 31, 2016, of which approximately \$6.3 million was operating expense and the remaining \$1.9 million was capital expenditure, and we expect to invest an additional \$2 million in 2017, of which we expect approximately \$0.1 million to be capital expenditure and the remainder to be operating expense.

Not all of these activities directly generate revenue, and we cannot assure you that we will reap sufficient rewards from these investments to make them worthwhile. If the expenses that we incur in connection with these activities do not result in increased

consumer engagement that in turn results in revenue increases that exceed these expenses, our business, financial condition and results of operations will be adversely affected.

Our services and products may become less competitive or even obsolete if we fail to respond to technological developments.

Our future success will depend, in part, on our ability to modify or enhance our services and products to meet customer and consumer needs, to add functionality and to address technological advancements that would improve their performance. For example, if our smartphone and tablet products fail to capture the increased search activity on such devices or if our services and products do not adapt to the increasing video usage on the internet or to take into account evolving developments in social networking, then they could begin to appear obsolete. Similarly, if we fail to develop new ways to deliver content and services through apps other than traditional internet browsers, consumers could seek alternative means of accessing content and services.

To remain competitive, we will need to develop new services and products and adapt our existing ones to address these and other evolving technologies and standards. However, we may be unsuccessful in identifying new opportunities or in developing or marketing new services and products in a timely or cost-effective manner. In addition, our product innovations may not achieve the market penetration or price levels necessary for profitability. If we are unable to develop enhancements to, and new features for, our existing services and products or if we are unable to develop new services and products that keep pace with rapid technological developments or changing industry standards, our services and products may become obsolete, less marketable and less competitive, and our business will be harmed.

We depend on third parties for content that is critical to our business, and our business could suffer if we do not continue to obtain high-quality content at a reasonable cost.

We license the content that we aggregate on our Managed Portals from numerous third-party content providers, and our future success is highly dependent upon our ability to maintain and enter into new relationships with these and other content providers. In some cases, we are required under our contracts, including our contract with AT&T, to provide our customers' consumers access to certain types of content. In the future, some of our content providers may not give us access to high-quality content, may fail to adapt to changes in consumer tastes or may increase the royalties, fees or percentages that they charge us for their content, any of which could have a material negative effect on our operating results. Our rights to the content that we offer to our customers and their consumers are not exclusive, and the content providers could license their content to our competitors. Our content providers could even grant our competitors exclusive licenses. In addition, our customers are not prohibited from entering into content deals directly with our content providers. Any failure to enter into or maintain satisfactory arrangements with content providers would adversely affect our ability to provide a variety of attractive services and products to our customers. Our reputation and operating results could suffer as a result, and it may be more difficult for us to develop new relationships with potential customers.

Our Zimbra Email/Collaboration solution was developed as an open-source software product. As such, it may be relatively easy for competitors, some of which may have greater resources than we have, to compete with us.

One of the characteristics of open source software is that anyone may modify and redistribute the existing open source software and use it to compete with us. Such competition can develop without the degree of overhead and lead time required by traditional proprietary software companies. In addition, some of these competitors may make their open source software available for free download and use on an ad hoc basis or may position their open source software as a loss leader. We cannot guarantee that we will be able to compete successfully against current and future competitors or that competitive pressure and/or the availability of open source software will not result in price reductions, reduced

operating margins and loss of market share, any one of which could adversely affect our business, financial condition, operating results and cash flows.

In 2016, we announced an initiative to promote support for our open source Zimbra Email/Collaboration solution with the expectation that the initiative would lead to increased maintenance, support and professional service revenue. There can be no assurance that this initiative will yield an increase in revenue.

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Our revenue and operating results may fluctuate, which makes our results difficult to predict and could cause our results to fall short of expectations.

As a result of the rapidly changing nature of the markets in which we compete, our quarterly and annual revenue and operating results are likely to fluctuate from period to period. These fluctuations may be caused by a number of factors, many of which are beyond our control, including but not limited to the various factors set forth in this “Risk Factors” section, as well as:

- any failure to maintain strong relationships and favorable revenue-sharing arrangements with our Managed Portals and Advertising partners, in particular Google, including a reduction in the quantity or pricing of sponsored links that consumers click on or a reduction in the pricing of digital advertisements by advertisers;
- the timing of our investment in, or the timing of our monetization of, our products and services, such as our end-to-end video solutions portfolio or our Zimbra Email/Collaboration product;
- any failure of significant customers to renew their agreements with us;
- our ability to attract new customers;
- our ability to increase sales of premium services and paid content to our existing customers’ consumers;
- any development by our significant customers of the in-house capacity to replace the solutions we provide;
  - the release of new product and service offerings by our competitors or our customers;
- variations in the demand for our services and products and the implementation cycles of our services and products by our customers;
- changes to internet browser technology that may render our Managed Portals less competitive;
- changes in our pricing policies or those of our competitors;
- changes in the prices our customers charge their consumers for email, premium services and paid content;
- service outages, other technical difficulties or security breaches;
- limitations relating to the capacity of our networks, systems and processes;
- our failure to accurately estimate or control costs, including costs related to the implementation of our solutions for new customers;
- maintaining appropriate staffing levels and capabilities relative to projected growth;
- the timing of costs related to the development or acquisition of technologies, services or businesses to support our existing customers and potential growth opportunities; and
- general economic, industry and market conditions and those conditions specific to internet usage and online businesses.

For these reasons and because the market for our services and products is relatively new and rapidly changing, it is difficult to predict our future financial results.

Expansion into international markets, which is an important part of our strategy, but where we have limited experience, will subject us to risks associated with international operations.

We plan to continue to expand our product offerings internationally, particularly in Asia, Canada, Latin America and Europe. Although our exposure to and expertise in international markets have increased as a result of our acquisition of the Zimbra assets in September 2015, we still have limited experience in marketing and operating all of our services and products in international markets, and we may not be able to successfully develop or grow our business in these markets. Our success in these markets will be directly linked to the success of our relationships with potential customers, resellers, content partners and other third parties.

As the international markets in which we operate continue to grow, we expect that competition in these markets will intensify. Local companies may have a substantial competitive advantage because of their greater understanding of, and focus on, the local markets. Some of our domestic competitors who have substantially greater resources than we

do may be able to more quickly and comprehensively develop and grow in international markets. International expansion may also require significant financial investment including, among other things, the expense of developing localized products, the costs of acquiring foreign companies and the integration of such companies with our operations, expenditure of resources in developing customer and content relationships and the increased costs of supporting remote operations.

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Other risks of doing business in international markets include the increased risks and burdens of complying with different legal and regulatory standards, difficulties in managing and staffing foreign operations, recruiting and retaining talented direct sales personnel, limitations on the repatriation of funds and fluctuations of foreign exchange rates, varying levels of internet technology adoption and infrastructure and our ability to enforce contracts and our intellectual property rights in foreign jurisdictions. In addition, our success in international expansion could be limited by barriers to international expansion such as tariffs, adverse tax consequences and technology export controls. If we cannot manage these risks effectively, the costs of doing business in some international markets may be prohibitive or our costs may increase disproportionately to our revenue. Some of our business partners also have international operations and are subject to the risks described above. Even if we are able to successfully manage the risks of international operations, our business may be adversely affected if our business partners are not able to successfully manage these risks.

Failure to comply with the United States Foreign Corrupt Practices Act could subject us to penalties and other adverse consequences.

We are subject to the United States Foreign Corrupt Practices Act, which generally prohibits U.S. companies from engaging in bribery or other prohibited payments to foreign officials for the purpose of obtaining or retaining business. Corruption, extortion, bribery, pay-offs, theft and other fraudulent practices may occur with respect to our expansion into international markets. Our employees or other agents may engage in such conduct for which we might be held responsible. If our employees or other agents are found to have engaged in such practices, we could suffer severe penalties and other consequences, including adverse publicity and damage to our reputation that may have a material adverse effect on our business, financial condition and results of operations.

Our agreements with some of our customers and content providers require fixed payments, which could adversely affect our financial performance.

Certain of our agreements with Managed Portals and Advertising customers and content providers require us to make fixed payments to them. The aggregate amount of such fixed payments for the year ending December 31, 2017 is approximately \$1.6 million. We are required to make these fixed payments regardless of the achievement of any revenue objectives or subscriber or usage levels. If we do not achieve our financial objectives, these contractual commitments would constitute a greater percentage of our revenue than originally anticipated and would adversely affect our profitability.

Our agreements with some of our customers and content providers contain penalties for non-performance, which could adversely affect our financial performance.

We have entered into service level agreements with many of our customers. These agreements generally call for specific system “up times” and 24 hours per day, seven days per week support and include penalties for non-performance. We may be unable to fulfill these commitments due to circumstances beyond our control, which could subject us to substantial penalties under those agreements, harm our reputation and result in a reduction of revenue or the loss of customers, which would in turn have an adverse effect on our business, financial condition and results of operations. To date, we have not incurred any material penalties.

In addition, certain of our agreements with customers contain penalties for certain types of non-performance which, if not timely rectified, could result in substantial financial penalties to us.

System failures or capacity constraints could harm our business and financial performance.



The provision of our services and products depends on the continuing operation of our information technology and communications systems. Any damage to or failure of our systems could result in interruptions in our service. Such interruptions could harm our business, financial condition and results of operations, and our reputation could be damaged if people believe our systems are unreliable. Our systems are vulnerable to damage or interruption from snow storms, terrorist attacks, floods, fires, power loss, telecommunications failures, security breaches, computer malware, computer hacking attacks, computer viruses, computer denial of service attacks or other attempts to, or events that, harm our systems. Our data centers are also subject to break-ins, sabotage and intentional acts of vandalism and to potential disruptions if the operators of the facilities have financial difficulties. Although we maintain insurance to cover a variety of risks, the scope and amount of our insurance coverage may not be sufficient to cover our losses resulting from system failures or other disruptions to our online operations. For example, the limit on our business interruption insurance is approximately \$20 million for cyber loss (\$38 million for physical loss). Any system failure or disruption and any resulting losses that are not recoverable under our insurance policies may materially harm our business, financial condition and results of operations. To date, we have never experienced any material losses.

Our data centers are not on full second-site redundancy, however we have the capability to do so; only certain customers require us to. We regularly back-up our systems and store the system back-ups in Atlanta, Georgia; Dallas, Texas; Lewis Center, Ohio; Denver, Colorado; Toronto, Canada; and Amsterdam, the Netherlands. If we were forced to relocate to an alternate site and to rely on

our system back-ups to restore the systems, we would experience significant delays in restoring the functionality of our platform and could experience loss of data, which could materially harm our business and our operating results.

Security breaches, computer viruses and computer hacking attacks could harm our business, financial condition and results of operations.

Security breaches, computer malware and computer hacking attacks are prevalent in the technology industry. Any security breach caused by hacking, which involves efforts to gain unauthorized access to information or systems, or to cause intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment, and the inadvertent transmission of computer viruses could harm our business, financial condition and results of operations. We have previously experienced hacking attacks on our systems, and may in the future experience hacking attacks. Though it is difficult to determine what harm may directly result from any specific interruption or breach, any failure to maintain performance, reliability, security and availability of our technology infrastructure to the satisfaction of our customers and their consumers may harm our reputation and our ability to retain existing customers and attract new customers.

We may not maintain acceptable website performance for our Managed Portals and Advertising customers, which may negatively impact our relationships with our customers and harm our business, financial condition and results of operations.

A key element to our continued growth is the ability of our customers' consumers in all geographies to access our Managed Portals and other offerings within acceptable load times. We refer to this as website performance. We may in the future experience platform disruptions, outages and other performance problems due to a variety of factors, including infrastructure changes, human or software errors, capacity constraints due to an overwhelming number of users accessing our technology simultaneously, and denial of service or fraud or security attacks.

In some instances, we may not be able to identify the cause or causes of these website performance problems within an acceptable period of time. It may become increasingly difficult to maintain and improve website performance, especially during peak usage times, and as our solutions become more complex and our user traffic increases. If our Managed Portals and Advertising solutions are unavailable when consumers attempt to access them or do not load as quickly as they expect, consumers may seek other alternatives to obtain the information for which they are looking, and may not use our products and services as often in the future, or at all. This would negatively impact our relationships with our customers. We expect to continue to make significant investments to maintain and improve website performance. To the extent that we do not effectively address capacity constraints, upgrade our systems as needed and continually develop our technology and network architecture to accommodate actual and anticipated changes in technology, our business and operating results may be harmed.

We rely on our management team and need additional personnel to expand our business, and the loss of key officers or an inability to attract and retain qualified personnel could harm our business, financial condition and results of operations.

We depend on the continued contributions of our senior management and other key personnel, especially Himesh Bhise, our President and Chief Executive Officer, and William J. Stuart, our Chief Financial Officer. The loss of the services of any of our executive officers or other key employees could harm our business and our prospects. All of our executive officers and key employees are at-will employees, which means they may terminate their employment relationship with us at any time.

Our future success also depends on our ability to identify, attract and retain highly skilled technical, managerial, finance, marketing and creative personnel. Further, we will need to hire personnel outside the United States to

continue to pursue an international expansion strategy, and we will need to hire additional advertising salespeople to sell more advertisements directly. We face intense competition for qualified individuals from numerous technology, marketing and media companies, and we may incur significant costs to attract them. We may be unable to attract and retain suitably qualified individuals, or we may be required to pay increased compensation in order to do so. If we were to be unable to attract and retain the qualified personnel we need to succeed, our business could suffer.

Volatility or lack of performance in the trading price of our common stock may also affect our ability to attract and retain qualified personnel. Many of our senior management personnel and other key employees have become, or will become, vested in a substantial amount of stock or stock options. Employees may be more likely to leave us if the shares they own or the shares underlying their options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the options or if the exercise prices of the options that they hold are significantly above the trading price of our common stock. If we are unable to retain our employees, our business, financial condition and results of operations would be harmed.

If we fail to manage our growth effectively, our business, financial condition and results of operations may suffer.

Following the merger of our predecessor companies, Chek, Inc., or Chek, and MyPersonal.com, Inc., or MyPersonal, to form Synacor, much of our business expansion resulted from organic growth. More recently, however, we have sought to, and may continue to seek to, grow through strategic acquisitions. For example, in the first quarter of 2016, we acquired certain assets from Technorati, and in 2015, we acquired the Zimbra assets and certain assets of NimbleTV. Our goal of returning to growth may place significant demands on our management and our operational and financial infrastructure. Our ability to manage our growth effectively and to integrate new technologies and acquisitions (such as the assets acquired from Technorati, Zimbra, and NimbleTV) into our existing business will require us to continue to expand our operational, financial and management information systems and to continue to retain, attract, train, motivate and manage key employees. Growth could strain our ability to:

- develop and improve our operational, financial and management controls;
- enhance our reporting systems and procedures;
- recruit, train and retain highly skilled personnel;
- maintain our quality standards; and
- maintain customer and content owner satisfaction.

Managing our growth will require significant expenditures and allocation of valuable management resources. If we fail to achieve the necessary level of efficiency in our organization as it grows, our business, financial condition and results of operations would be harmed.

We may expand our business through acquisitions of, or investments in, other companies or new technologies, or joint ventures or other strategic alliances with other companies, which may divert our management's attention or prove not to be successful.

In February 2016 we acquired substantially all of the assets of, and hired certain personnel from, Technorati; in 2015 we acquired the Zimbra assets and hired certain related personnel and we purchased assets from, and hired the personnel of, NimbleTV; and in March 2013, we entered into a joint venture in China. We may decide to pursue other acquisitions of, investments in, or joint ventures involving other technologies and businesses in the future. Such transactions could divert our management's time and focus from operating our business.

Our ability as an organization to integrate acquisitions is relatively unproven. Integrating an acquired company, business or technology is risky and may result in unforeseen operating difficulties and expenditures, including, among other things, with respect to:

- incorporating new technologies into our existing business infrastructure;
- consolidating corporate and administrative functions;
- coordinating our sales and marketing functions to incorporate the new business or technology;
- maintaining morale, retaining and integrating key employees to support the new business or technology and managing our expansion in capacity; and
- maintaining standards, controls, procedures and policies (including effective internal control over financial reporting and disclosure controls and procedures).

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

Future acquisitions could result in potentially dilutive issuances of our equity securities, including our common stock, or the incurrence of debt, contingent liabilities, amortization expenses or acquired in-process research and development expenses, any of which could harm our business, financial condition and results of operations. Future acquisitions may also require us to make payments above. A portion of those payments may reduce the deferred grant incentive liability rather than being recorded as expense. See Note 9 for additional information.

#### Construction of New Headquarters

On June 11, 2014, the Company entered into a Redevelopment Agreement, a Design-Build Contract, and a Development Services Agreement as well as various ancillary agreements related to the acquisition of real property located in New Brighton, Minnesota and the development of such property into the Company's new corporate headquarters.

Pursuant to the Contract for Private Redevelopment by and among the City of New Brighton (the "City"), Ryan Companies US, Inc. ("Ryan"), and the Company, dated June 11, 2014 (the "Redevelopment Agreement"), the Company purchased approximately ten acres of real property from the City for a purchase price of \$500. The City also granted the Company the option to purchase an additional 3.6 acres prior to May 31, 2021.

Pursuant to the Design-Build Cost Plus Construction Contract by and between Ryan and the Company, dated June 11, 2014, the Company has contracted with Ryan to furnish all services, labor, materials, equipment, procurement services, project management and other duties and services necessary for construction of the Company's new headquarters on the land purchased from the City. The Company and Ryan expect to have construction substantially completed by March 1, 2015, and, pursuant to the Redevelopment Agreement discussed above, Ryan and the Company have agreed to complete construction by December 31, 2015. The Company will pay Ryan a fee of 3.85% of the cost of the work.

The Company also entered into a Development Services Agreement with Ryan, dated June 11, 2014, pursuant to which Ryan will perform certain development services to facilitate development of the project, including coordination with the City and overall coordination of development strategy. The Company will pay Ryan a fee for the development services, which includes a sum equal to 3.25% of the adjusted total project costs, payable at certain points in the construction process, and a sum equal to 5% of the adjusted total project costs, payable upon substantial completion of the project, as well as reimbursement of certain expenses incurred by Ryan.

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In connection with the agreements above, the Company is required to hold approximately \$9,128 in an escrow account that will be used to fund the final construction payments. The escrow is classified as construction in progress in property and equipment, net, on the consolidated balance sheet.

## 9. Texas Production Facility

Effective on September 9, 2009, the Company entered into an agreement with the Pearland Economic Development Corporation (the "PEDC") for the construction and lease of an approximately 46,000 square foot production facility located in Pearland, Texas. The facility primarily serves as an additional manufacturing location for the Company.

The Company and the PEDC entered into a Corporate Job Creation Agreement dated June 17, 2009, which was subsequently amended July 2, 2012. The Job Creation Agreement, as amended, provided the Company with \$2,975 in net cash incentive funds. The Company believes it will be able to comply with the conditions specified in the amended agreement. The PEDC will provide the Company with an additional \$425 of net cash incentive funds if: (1) the Company hires 125 full-time employees at the facility before June 30, 2015 and (2) maintains 125 employees at the facility through June 30, 2016. The Company had the opportunity to receive an additional \$425 of net cash incentive funds upon hiring the 75<sup>th</sup> employee on or before March 31, 2014; however, the Company did not achieve this incentive.

In order to retain all of the cash incentives, the Company must maintain no fewer than 25 jobs at the Texas facility through June 30, 2015. Failure to meet this requirement will result in an obligation to make reimbursement payments to the PEDC as outlined in the amended agreement. The Company will not have any reimbursement requirements after June 30, 2015. As of September 30, 2014, the Company was in compliance with all minimum requirements under the amended agreement. The Company believes it will be able to comply with the conditions specified in the amended agreement.

The Job Creation Agreement, as amended, also provided the Company with a net \$1,020 award, of which \$510 was received from the PEDC and the remainder is funded through the Texas Enterprise Fund program associated with the State of Texas. As of September 30, 2014, \$340 has been received and the remaining \$170 will be provided upon the hiring of the 75<sup>th</sup> full-time employee at the facility. The grant from the State of Texas is subject to reimbursement if the Company fails to meet certain job creation targets through 2014 and maintain these positions through 2020. The Company reimbursed the State of Texas \$46 during fiscal 2014 as it did not meet the target of hiring 75 employees at the facility by December 31, 2013.

The Company has presented the net cash incentive funds as a current and long-term liability on the balance sheet. The liabilities are reduced through the term of the agreement and recorded as an offset to expenditures incurred using a systematic methodology. As of September 30, 2014, the deferred grant incentive liabilities have been reduced by \$20 in cumulative expenses, resulting in a remaining current liability of \$39.

## 10. Earnings Per Share

The following table presents a reconciliation of the numerators and denominators used in the basic and diluted earnings per common share computations (in thousands except share and per share amounts):

	Three Months Ended September 30,	
	2014	2013
Numerator		
Net loss	\$(8,224	) \$(7,292
Denominator		

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Weighted average common shares – basic	31,311,110	24,751,368
Effect of dilutive stock options, warrants, convertible debt <sup>(a)(b)(c)</sup>	—	—
Weighted average common shares outstanding – diluted	31,311,110	24,751,368
Net loss per common share — basic and diluted	\$(0.26	) \$(0.29 )

At September 30, 2014 and 2013, 0 and 1,667,481 warrants, respectively, were outstanding. The effect of the (a) shares that would be issued upon exercise of these warrants has been excluded from the calculation of diluted loss per share because those shares are anti-dilutive.

At September 30, 2014 and 2013, 847,208 and 1,656,774 stock options, respectively, were outstanding. The effect (b) of the shares that would be issued upon exercise of these options has been excluded from the calculation of diluted loss per share because those shares are anti-dilutive.

At September 30, 2014 and 2013, 0 and 288,420 additional shares of common stock were issuable upon the (c) conversion of outstanding convertible debt agreements. The effect of the shares that would be issued upon conversion of these debt agreements has been excluded from the calculation of diluted loss per share because those shares are anti-dilutive.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes appearing under Item 1 of Part I. Some of the information contained in this discussion and analysis or set forth elsewhere in this quarterly report, including information with respect to our plans and strategy for our business and expected financial results, includes forward-looking statements that involve risks and uncertainties. You should review the "Risk Factors" discussed in our Form 10-K for the year ended June 30, 2014 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

OVERVIEW

We are a medical device company focused on developing and commercializing interventional treatment systems for vascular disease. Our peripheral arterial disease ("PAD") products, the Stealth 360<sup>®</sup> PAD System (the "Stealth 360"), the Diamondback 360<sup>®</sup> PAD System (the "Diamondback 360 Peripheral"), and the Diamondback Predator 360<sup>®</sup> (the "Predator 360") are catheter-based platforms capable of treating a broad range of plaque types in leg arteries both above and below the knee and address many of the limitations associated with other treatment alternatives. In March 2014, we received approval for the Diamondback 360<sup>®</sup> 60cm Peripheral Orbital Atherectomy System ("OAS") access device, which allows physicians to treat PAD patients in the small and tortuous vessels located below the knee through alternative access sites in the ankle or foot. We refer to the Stealth 360, Diamondback 360 Peripheral, Predator 360, and the Diamondback 360 60cm Peripheral OAS collectively in this report as the "PAD Systems." We have also obtained approval to market our Diamondback 360<sup>®</sup> Coronary OAS ("CAD System") as a treatment for severely calcified coronary arteries.

Since 1997, we have devoted substantially all of our resources to the development of the PAD Systems and, since 2007, to the approval of our CAD System. From 2003 to 2005, we conducted numerous bench and animal tests in preparation for application submissions to the Food and Drug Administration ("FDA"). We initially focused our testing on providing a solution for coronary in-stent restenosis, but later changed the focus to PAD. In 2006, we obtained an investigational device exemption from the FDA to conduct our pivotal OASIS clinical trial, which was completed in January 2007. The OASIS clinical trial was a prospective 20-center study that involved 124 patients with 201 lesions.

In August 2007, the FDA granted us 510(k) clearance for the use of the Diamondback 360 Peripheral as a therapy in patients with PAD. We commenced commercial introduction of the Diamondback 360 Peripheral in the United States in September 2007. We were granted 510(k) clearance of the Predator 360 in March 2009 and Stealth 360 in March 2011. We received 510(k) clearance of the Diamondback 360 60cm Peripheral OAS in March 2014. We market the PAD Systems in the United States through a direct sales force and expend significant capital on our sales and marketing efforts to expand our customer base and utilization per customer. At our facilities, we assemble the saline infusion pump and the single-use catheter used in the PAD Systems with components purchased from third-party suppliers, as well as with components manufactured in-house. We purchase supplemental products from third-party suppliers.

We have developed a modified version of the PAD System to treat coronary arteries. A coronary application required us to conduct a clinical trial and file a premarket approval ("PMA") application and obtain approval from the FDA. In March 2013, we completed submission of our PMA application to the FDA for our OAS to treat calcified coronary arteries. In October 2013, we received PMA from the FDA to market the CAD System as a treatment for severely calcified coronary arteries. We commenced a controlled commercial launch of the CAD System following the receipt of PMA approval.



As of September 30, 2014, we had an accumulated deficit of \$246.8 million. We expect our losses to continue as we invest in sales, marketing, medical education, clinical studies and product research and development for our next phase of growth in the peripheral market and broaden the commercial launch of our CAD System. To date, we have financed our operations primarily from the issuance of stock, convertible promissory notes, and debt.

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## CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT JUDGMENTS AND ESTIMATES

Our management's discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of our consolidated financial statements requires us to make estimates, assumptions and judgments that affect amounts reported in those statements. Our estimates, assumptions and judgments, including those related to revenue recognition, allowance for doubtful accounts, excess and obsolete inventory, and stock-based compensation, are updated as appropriate at least quarterly. We use authoritative pronouncements, our technical accounting knowledge, cumulative business experience, judgment and other factors in the selection and application of our accounting policies. While we believe that the estimates, assumptions and judgments that we use in preparing our consolidated financial statements are appropriate, these estimates, assumptions and judgments are subject to factors and uncertainties regarding their outcome. Therefore, actual results may materially differ from these estimates.

Some of our significant accounting policies require us to make subjective or complex judgments or estimates. An accounting estimate is considered to be critical if it meets both of the following criteria: (1) the estimate requires assumptions about matters that are highly uncertain at the time the accounting estimate is made, and (2) different estimates that reasonably could have been used, or changes in the estimate that are reasonably likely to occur from period to period, would have a material impact on the presentation of our financial condition, results of operations, or cash flows.

Our critical accounting policies are identified in our Annual Report on Form 10-K for the fiscal year ended June 30, 2014 in Management's Discussion and Analysis of Financial Condition and Results of Operations under the heading "Critical Accounting Policies and Significant Judgments and Estimates." There were no significant changes to our critical accounting policies during the three months ended September 30, 2014.

## RESULTS OF OPERATIONS

The following table sets forth our results of operations expressed as dollar amounts (in thousands) and the changes between the specified periods expressed as percent increases or decreases:

	Three Months Ended September 30,		Percent Change	%
	2014	2013		
Revenues	\$41,354	\$29,766	38.9	
Cost of goods sold	8,885	6,864	29.4	
Gross profit	32,469	22,902	41.8	
Expenses:				
Selling, general and administrative	33,507	25,371	32.1	
Research and development	7,152	4,378	63.4	
Total expenses	40,659	29,749	36.7	
Loss from operations	(8,190 )	(6,847 )	19.6	
Interest and other, net	(34 )	(445 )	(92.4 )	
Net loss	\$(8,224 )	\$(7,292 )	12.8	

## Comparison of Three Months Ended September 30, 2014 with Three Months Ended September 30, 2013

Revenues. Revenues increased by \$11.6 million, or 38.9%, from \$29.8 million for the three months ended September 30, 2013 to \$41.4 million for the three months ended September 30, 2014. This increase was primarily

attributable to a \$5.6 million, or 21.5%, increase in the number of PAD Systems sold, which reflects a 20.1% increase in number of devices sold. Additionally, sales of the CAD System contributed approximately \$4.7 million in revenues following our PMA approval in October 2013. Other product revenue also increased \$1.3 million, or 36.1%, during the three months ended September 30, 2014 as compared to the three months ended September 30, 2013, primarily driven by increased sales of PAD and CAD Systems, which the other products support.

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Currently, all of our revenues are in the United States; however, we intend to sell internationally in the future and have commenced the process of seeking approval to do so in both Europe and Japan. We expect our revenue to increase as we continue to increase the number of physicians using the devices, increase the usage per physician, introduce new and improved products, generate additional clinical data, continue the controlled commercial launch of our CAD System, and expand into new geographies.

**Cost of Goods Sold.** Cost of goods sold increased by \$2.0 million, or 29.4%, from \$6.9 million for the three months ended September 30, 2013 to \$8.9 million for the three months ended September 30, 2014. Cost of goods sold represents the cost of materials, labor and overhead for single-use catheters, guidewires, saline pumps, and other ancillary products. The increase was due to an increase in the quantities of products sold, partially offset by lower indirect costs per unit from higher production volumes and manufacturing efficiencies. Cost of goods sold for the three months ended September 30, 2014 and 2013 includes \$222,000 and \$142,000, respectively, for stock-based compensation. Gross margin increased from 76.9% during the three months ended September 30, 2013 to 78.5% for the three months ended September 30, 2014, which was primarily due to higher average selling prices primarily for our CAD Systems and lower indirect costs per unit. We expect that gross margin in the remainder of fiscal 2015 will be similar to the three months ended September 30, 2014. Quarterly margin fluctuations could occur based on production volumes, timing of new product introductions, sales mix, pricing changes, or other unanticipated circumstances.

**Selling, General and Administrative Expenses.** Our selling, general and administrative expenses increased by \$8.1 million, or 32.1%, from \$25.4 million for the three months ended September 30, 2013 to \$33.5 million for the three months ended September 30, 2014. The increase was due primarily to higher coronary expenses from commercial launch, clinical studies and product development, the expansion of our sales and marketing organization and increased incentive compensation. Selling, general and administrative expenses for the three months ended September 30, 2014 and 2013 include \$3.0 million and \$1.9 million, respectively, for stock-based compensation. We expect our selling, general and administrative expenses to increase in the future as a result of the costs associated with expanding our sales and marketing organization and medical education and other programs to further commercialize our PAD products and expand the commercial launch of our CAD System.

**Research and Development Expenses.** Research and development expenses increased by \$2.8 million, or 63.4%, from \$4.4 million for the three months ended September 30, 2013 to \$7.2 million for the three months ended September 30, 2014. Research and development expenses relate to specific projects to develop new products or expand into new markets, such as the development of new versions of the PAD and CAD Systems, shaft designs, crown designs, and PAD and CAD clinical trials. The increase related mainly to additional product development projects and clinical studies, and the related increase in headcount. Research and development expenses for the three months ended September 30, 2014 and 2013 include \$320,000 and \$217,000, respectively, for stock-based compensation. As we continue to expand our product portfolio and clinical studies within the PAD and CAD markets, we generally expect to incur quarterly research and development expenses above amounts incurred for the three months ended September 30, 2014. Fluctuations could occur based on the number of projects and studies and the timing of expenditures.

**Interest and Other, Net.** Interest and other expense, net, was \$34,000 for the three months ended September 30, 2014 compared to \$445,000 for the three months ended September 30, 2013. The decrease was primarily driven by lower interest expense related to lower outstanding debt balances, as well as the elimination of charges from debt conversions and changes in fair value of the debt conversion option that were associated with the previously outstanding convertible debt.

## LIQUIDITY AND CAPITAL RESOURCES

We had cash and cash equivalents of \$116.4 million and \$126.6 million at September 30, 2014 and June 30, 2014, respectively. During the three months ended September 30, 2014, net cash used in operations amounted to \$4.5 million. As of September 30, 2014, we had an accumulated deficit of \$246.8 million. We have historically funded our operating losses primarily from the issuance of stock, convertible promissory notes, and debt.

#### Loan and Security Agreement with Silicon Valley Bank

On March 29, 2010, we entered into an amended and restated loan and security agreement with Silicon Valley Bank. The agreement was amended on December 27, 2011 to increase outstanding borrowings, amended on June 29, 2012 to modify financial covenants and reduce the interest rate and other fees, amended on May 10, 2013 to modify financial covenants, amended on June 26, 2014 to extend the line of credit's maturity date to September 30, 2014 and reduce the interest rate, and amended on September 29, 2014 to extend the line of credit's maturity date to December 31, 2014. The agreement, as amended, includes a \$15.0 million line of credit.

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The \$15.0 million line of credit has a floating interest rate equal to the Wall Street Journal's prime rate. Interest on borrowings is due monthly and the principal balance is due at maturity. Borrowings on the line of credit are based on 85% of eligible accounts. Accounts receivable receipts are deposited into a lockbox account in the name of Silicon Valley Bank. The line of credit is subject to non-use fees, annual fees, and cancellation fees. The balance outstanding on the line of credit at September 30, 2014 and June 30, 2014 was \$1.2 million and \$2.4 million, respectively.

Borrowings from Silicon Valley Bank are secured by all of our assets. The borrowings are subject to prepayment penalties and financial covenants, including maintaining certain liquidity and fixed charge coverage ratios. Any non-compliance by us under the terms of debt arrangements could result in an event of default under the Silicon Valley Bank loan, which, if not cured, could result in the acceleration of this debt. We were in compliance with all financial covenants as of September 30, 2014.

### Loan and Security Agreement with Partners for Growth

On April 14, 2010, we entered into a loan and security agreement with Partners for Growth III, L.P. ("PFG"), as amended on August 23, 2011, December 27, 2011, June 30, 2012, and May 10, 2013. The amended agreement provides that PFG will make loans to us up to \$5.0 million. The agreement has a maturity date of April 14, 2015. The loans bear interest at a floating per annum rate equal to 2.75% above Silicon Valley Bank's prime rate, and such interest is payable monthly. The principal balance of and any accrued and unpaid interest on any notes are due on the maturity date and may not be prepaid by us at any time in whole or in part. As of September 30, 2014 and June 30, 2014, there were no loans outstanding.

At any time prior to the maturity date, PFG may, at its option, convert any outstanding loan into shares of our common stock at the applicable conversion price, which in each case equals the ten-day volume weighted average price per share of our common stock prior to the issuance date of each note. We may also effect at any time a mandatory conversion of amounts, subject to certain terms, conditions and limitations provided in the agreement, including a requirement that the ten-day volume weighted average price of our common stock prior to the date of conversion is at least 15% greater than the conversion price. We may reduce the conversion price to a price that represents a 15% discount to the ten-day volume weighted average price of our common stock to satisfy this condition and effect a mandatory conversion. We recorded an expense of \$0 and \$61,000 for the three months ended September 30, 2014 and 2013, respectively, related to the change in fair value of the conversion options on all outstanding loans. This amount is a component of interest and other, net on the accompanying statement of operations.

Any loans are secured by certain of our assets, and the agreement contains customary covenants limiting our ability to, among other things, incur debt or liens, make certain investments and loans, effect certain redemptions of and declare and pay certain dividends on our stock, permit or suffer certain change of control transactions, dispose of collateral, or change the nature of our business. In addition, the PFG loan and security agreement contains financial covenants requiring us to maintain certain liquidity and fixed charge coverage ratios. We were in compliance with all financial covenants at September 30, 2014. If we do not comply with the various covenants, PFG may, subject to various customary cure rights, decline to provide additional loans, require amortization of any future loan over its remaining term, or require the immediate payment of all amounts outstanding under any future loan and foreclose on any or all collateral, depending on which financial covenants are not maintained.

### Changes in Liquidity

Cash and Cash Equivalents. Cash and cash equivalents were \$116.4 million at September 30, 2014 and \$126.6 million at June 30, 2014. The decrease is primarily attributable to net cash used in operations and investing activities during the three months ended September 30, 2014.

Operating Activities. Net cash used in operations was \$4.5 million and \$5.6 million for the three months ended September 30, 2014 and 2013, respectively. For the three months ended September 30, 2014 and 2013, we had a net loss of \$8.2 million and \$7.3 million, respectively. Significant changes in working capital during these periods included:

Cash used in accounts receivable of \$1.7 million and \$631,000 during the three months ended September 30, 2014 and 2013, respectively, was primarily due to the amount and timing of revenue during the three months ended September 30, 2014 and 2013.

Cash used in inventories of \$1.8 million and \$2.0 million during the three months ended September 30, 2014 and 2013, respectively. For the three months ended September 30, 2014, the amount of cash used in inventories was primarily due to higher levels of raw materials for manufacture of products, including the CAD System commercial launch. For the three months ended September 30, 2013, cash used in inventories was primarily due to higher levels of finished goods for future sales and timing of inventory purchases and sales.

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Cash provided by prepaid expenses and other current assets was \$717,000 and \$11,000 during the three months ended September 30, 2014 and 2013, respectively, primarily due to payment timing of vendor deposits and other expenditures.

Cash provided by accounts payable of \$2.1 million and \$1.3 million during the three months ended September 30, 2014 and 2013, respectively, due to the amount and timing of purchases and vendor payments and overall increased levels of spending.

Cash (used in) provided by accrued expenses and other liabilities of \$(271,000) and \$143,000 during the three months ended September 30, 2014 and 2013, respectively, primarily due to the amount and timing of compensation payments.

**Investing Activities.** Net cash used in investing activities was \$5.2 million and \$411,000 for the three months ended September 30, 2014 and 2013, respectively, related to the purchase of property and equipment and patents, as well as the purchases of available-for-sale marketable securities during the three months ended September 30, 2014. During the three months ended September 30, 2014, we paid \$2.6 million towards the construction of our new corporate headquarters, which is discussed further below.

**Financing Activities.** Net cash (used in) provided by financing activities was \$(517,000) and \$1.4 million for the three months ended September 30, 2014 and 2013, respectively. For the three months ended September 30, 2014, cash used in financing activities was due to payments on debt of \$1.2 million, partially offset by proceeds from the exercise of stock options of \$683,000. For the three months ended September 30, 2013, cash provided by financing activities consisted of proceeds from exercise of stock options and warrants of \$2.6 million, partially offset by payments on debt of \$1.2 million.

Our future liquidity and capital requirements will be influenced by numerous factors, including the extent and duration of future operating losses, the level and timing of future sales and expenditures, the results and scope of ongoing research and product development programs, working capital required to support our sales growth, the receipt of and time required to obtain regulatory clearances and approvals, our sales and marketing programs, the continuing acceptance of our products in the marketplace, competing technologies, market and regulatory developments and ongoing facility requirements. As of September 30, 2014, we believe our current cash and cash equivalents will be sufficient to fund working capital requirements, capital expenditures (including the new corporate headquarters discussed below) and operations for the foreseeable future, including at least the next twelve months. We intend to retain any future earnings to support operations and to finance the growth and development of our business, and we do not anticipate paying any dividends in the foreseeable future. We may raise additional capital in the future, to fund acceleration of our current growth initiatives or additional growth opportunities, if we believe it will significantly enhance our value.

**New Corporate Headquarters.** On June 11, 2014, we entered into a Redevelopment Agreement, a Design-Build Contract, and a Development Services Agreement, as well as various ancillary agreements, related to the acquisition of real property located in New Brighton, Minnesota and the development of such property into our new corporate headquarters. Pursuant to the Contract for Private Redevelopment by and among the City of New Brighton (the "City"), Ryan Companies US, Inc. ("Ryan"), and us, dated June 11, 2014 (the "Redevelopment Agreement"), we purchased approximately ten acres of real property from the City for a purchase price of \$500,000. The City also granted us the option to purchase an additional 3.6 acres prior to May 31, 2021.

Pursuant to the Design-Build Cost Plus Construction Contract by and between Ryan and us, dated June 11, 2014, we have contracted with Ryan to furnish all services, labor, materials, equipment, procurement services, project management and other duties and services necessary for construction of our new headquarters on the land purchased from the City. We expect to have construction substantially completed by March 1, 2015, and, pursuant to the Redevelopment Agreement discussed above, we and Ryan have agreed to complete construction by December 31, 2015.



We anticipate that the total cost for the construction of the headquarters will be approximately \$23 million, subject to certain increases or decreases if work is completed prior to or after March 1, 2015 or if changes are made to the project plans during construction. We will pay Ryan a fee of 3.85% of the cost of the work. We also anticipate that the additional cost to furnish, equip and open the headquarters will be approximately \$8 million.

We also entered into a Development Services Agreement with Ryan, dated June 11, 2014, pursuant to which Ryan will perform certain development services to facilitate development of the project, including coordination with the City and overall coordinate of development strategy. We will pay Ryan a fee for the development services, which includes a sum equal to 3.25% of the adjusted total project costs, payable at certain points in the construction process and a sum equal to 5% of the adjusted total project costs, payable upon substantial completion of the project, as well as reimbursement of certain expenses incurred by Ryan.

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In connection with the agreements above, we are required to hold approximately \$9.1 million in an escrow account that will be used to fund the final construction payments. The escrow is classified as construction in progress in property and equipment, net, on the consolidated balance sheet.

## NON-GAAP FINANCIAL INFORMATION

To supplement our consolidated financial statements prepared in accordance with GAAP, our management uses a non-GAAP financial measure referred to as “Adjusted EBITDA.” The following table sets forth, for the periods indicated, a reconciliation of Adjusted EBITDA to the most comparable U.S. GAAP measure expressed as dollar amounts (in thousands):

	Three Months Ended September 30,	
	2014	2013
Loss from operations	\$(8,190	) \$(6,847
Add: Stock-based compensation	3,573	2,300
Add: Depreciation and amortization	408	316
Adjusted EBITDA	\$(4,209	) \$(4,231

Adjusted EBITDA was consistent with the prior year quarter due to increased stock-based compensation, which offset the increase in loss from operations. The loss from operations was impacted by increases in operating expenses as discussed above, partially offset by an increase in revenues and gross profit. Stock-based compensation increased \$1.3 million, or 55.3%, as a result of increased employee stock awards granted due to our expanded hiring and higher grant date fair values.

## Use and Economic Substance of Non-GAAP Financial Measures Used and Usefulness of Such Non-GAAP Financial Measures to Investors

We use Adjusted EBITDA as a supplemental measure of performance and believe this measure facilitates operating performance comparisons from period to period and company to company by factoring out potential differences caused by depreciation and amortization expense and non-cash charges such as stock-based compensation. Our management uses Adjusted EBITDA to analyze the underlying trends in our business, assess the performance of our core operations, establish operational goals and forecasts that are used to allocate resources and evaluate our performance period over period and in relation to our competitors’ operating results. Additionally, our management is partially evaluated on the basis of Adjusted EBITDA when determining achievement of their incentive compensation performance targets.

We believe that presenting Adjusted EBITDA provides investors greater transparency to the information used by our management for its financial and operational decision-making and allows investors to see our results “through the eyes” of management. We also believe that providing this information better enables our investors to understand our operating performance and evaluate the methodology used by our management to evaluate and measure such performance.

The following is an explanation of each of the items that management excluded from Adjusted EBITDA and the reasons for excluding each of these individual items:

**Stock-based compensation.** We exclude stock-based compensation expense from our non-GAAP financial measures primarily because such expense, while constituting an ongoing and recurring expense, is not an expense that requires cash settlement. Our management also believes that excluding this item from our non-GAAP results is useful to investors to understand the application of stock-based compensation guidance and its impact on our operational performance, liquidity and ability to make additional investments in the Company, and it allows for greater

transparency to certain line items in our financial statements.

Depreciation and amortization expense. We exclude depreciation and amortization expense from our non-GAAP financial measures primarily because such expenses, while constituting ongoing and recurring expenses, are not expenses that require cash settlement and are not used by our management to assess the core profitability of our business operations. Our management also believes that excluding these items from our non-GAAP results is useful to investors to understand our operational performance, liquidity and ability to make additional investments in the company.

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### Material Limitations Associated with the Use of Non-GAAP Financial Measures and Manner in Which We Compensate for these Limitations

Non-GAAP financial measures have limitations as analytical tools and should not be considered in isolation or as a substitute for our financial results prepared in accordance with GAAP. Some of the limitations associated with our use of these non-GAAP financial measures are:

Items such as stock-based compensation do not directly affect our cash flow position; however, such items reflect economic costs to us and are not reflected in our Adjusted EBITDA, and therefore these non-GAAP measures do not reflect the full economic effect of these items.

Non-GAAP financial measures are not based on any comprehensive set of accounting rules or principles and therefore other companies may calculate similarly titled non-GAAP financial measures differently than we do, limiting the usefulness of those measures for comparative purposes.

Our management exercises judgment in determining which types of charges or other items should be excluded from the non-GAAP financial measures we use.

We compensate for these limitations by relying primarily upon our GAAP results and using non-GAAP financial measures only supplementally.

### INFLATION

We do not believe that inflation had a material impact on our business and operating results during the periods presented.

### OFF-BALANCE SHEET ARRANGEMENTS

Since inception, we have not engaged in any off-balance sheet activities as defined in Item 303(a)(4) of Regulation S-K.

### RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, “Revenue From Contracts with Customers.” The guidance requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. The guidance also requires expanded disclosures relating to the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

Additionally, qualitative and quantitative disclosures are required about customer contracts, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract. ASU 2014-09 is effective for annual periods beginning after December 15, 2016, including interim periods within that reporting period, using one of two prescribed retrospective methods. Early adoption is not permitted. We are evaluating the impact of the amended revenue recognition guidance on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, “Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern.” The guidance requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date of issuance of the entity's financial statements. The entity must also provide certain disclosures if there is substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods thereafter. Early adoption is permitted. We do not anticipate a material impact on our financial statements upon adoption.



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PRIVATE SECURITIES LITIGATION REFORM ACT

The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” for forward-looking statements. Such “forward-looking” information is included in this Form 10-Q, including Item 2 of Part I, and in other materials filed or to be filed by the Company with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by the Company). Forward-looking statements include all statements based on future expectations. This Form 10-Q contains forward-looking statements that involve risks and uncertainties, including (i) expected compliance with the conditions specified in our Job Creation Agreement; (ii) our expectation that our losses will continue; (iii) the broadening of the commercial launch of the CAD System; (iv) the expectation of selling our products internationally in the future; (v) our expectation of increased revenue and increased selling, general and administrative expenses; (vi) our plans to continue to expand our sales and marketing efforts; (vii) our expectation that gross margin in the remainder of fiscal 2015 will be similar to the three months ended September 30, 2014; (viii) our expectation that we will incur research and development expenses in future quarters at amounts above the amounts incurred for the three months ended September 30, 2014; (ix) our belief that our current cash and cash equivalents and available debt will be sufficient to fund working capital requirements, capital expenditures and operations for the foreseeable future; (x) our intention to retain any future earnings to support operations; (xi) our dividend expectations; (xii) the potential to raise additional capital in the future; and (xiii) our plans regarding construction of a new headquarters, including the expected completion date and costs of construction and furnishing, equipping and opening the headquarters.

In some cases, you can identify forward-looking statements by the following words: “anticipate,” “believe,” “continue,” “could,” “estimate,” “expect,” “intend,” “may,” “ongoing,” “plan,” “potential,” “predict,” “project,” “should,” “will,” “would,” these terms or other comparable terminology, although not all forward-looking statements contain these words. Forward-looking statements are only predictions and are not guarantees of performance. These statements are based on our management’s beliefs and assumptions, which in turn are based on their interpretation of currently available information.

These statements involve known and unknown risks, uncertainties and other factors that may cause our results or our industry’s actual results, levels of activity, performance or achievements to be materially different from the information expressed or implied by these forward-looking statements.

These factors include regulatory developments in the U.S. and foreign countries; FDA and similar foreign clearances and approvals; approval of our products for distribution in foreign countries; approval of products for reimbursement and the level of reimbursement; dependence on market growth; the experience of physicians regarding the effectiveness and reliability of the PAD and CAD Systems; the reluctance of physicians, hospitals and other organizations to accept new products; the potential for unanticipated delays in enrolling medical centers and patients for clinical trials; actual clinical trial and study results; the impact of competitive products and pricing; unanticipated developments affecting our estimates regarding expenses, future revenues and capital requirements; unanticipated delays or costs related to the construction and furnishing of our new headquarters; the difficulty of successfully managing operating costs; our inability to expand our sales and marketing organization; our actual research and development efforts and needs; our ability to obtain and maintain intellectual property protection for product candidates; our actual financial resources and our ability to obtain additional financing; fluctuations in results and expenses based on new product introductions, sales mix, unanticipated warranty claims, and the timing of project expenditures; and general economic conditions. These and additional risks and uncertainties are described more fully in our Form 10-K filed with the SEC on August 28, 2014. Copies of filings made with the SEC are available through the SEC’s electronic data gathering analysis and retrieval system (EDGAR) at [www.sec.gov](http://www.sec.gov).

You should read these risk factors and the other cautionary statements made in this Form 10-Q as being applicable to all related forward-looking statements wherever they appear in this Form 10-Q. We cannot assure you that the

forward-looking statements in this Form 10-Q will prove to be accurate. Furthermore, if our forward-looking statements prove to be inaccurate, the inaccuracy may be material. You should read this Form 10-Q completely. Other than as required by law, we undertake no obligation to update these forward-looking statements, even though our situation may change in the future.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The primary objective of our investment activities is to preserve our capital for the purpose of funding operations, while at the same time maximizing the income we receive from our investments without significantly increasing risk or decreasing availability. To achieve these objectives, our investment policy allows us to maintain a portfolio of cash equivalents and investments in a variety of marketable securities, including money market funds, U.S. government securities, and certain bank obligations. Our cash and cash equivalents as of September 30, 2014 include liquid money market accounts. Due to the short-term nature of these investments, we believe that there is no material exposure to interest rate risk. Our line of credit balance as of September 30, 2014 has a floating interest rate equal to the Wall Street Journal's prime rate. We believe that there is no material exposure to interest rate risk related to our line of credit.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer, referred to collectively herein as the Certifying Officers, are responsible for establishing and maintaining our disclosure controls and procedures. The Certifying Officers have reviewed and evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934 (the "Exchange Act")) as of September 30, 2014. Based on that review and evaluation, which included inquiries made to certain other employees of the Company, the Certifying Officers have concluded that, as of the end of the period covered by this Report, the Company's disclosure controls and procedures, as designed and implemented, are effective.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the three months ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



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PART II. — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, including the important information in the section entitled “Private Securities Litigation Reform Act,” you should carefully consider the “Risk Factors” discussed in our Form 10-K for the year ended June 30, 2014 filed with the SEC on August 28, 2014 for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in this report, and materially adversely affect our financial condition or future results. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial might materially adversely affect our actual business, financial condition and/or operating results.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

Fifth Amendment to Loan and Security Agreement with Silicon Valley Bank

On September 29, 2014, the Company entered into the Fifth Amendment to Loan and Security Agreement (the “Amendment”) with Silicon Valley Bank (“SVB”). The Amendment amends the Company’s existing credit facility with SVB established pursuant to the Loan and Security Agreement between the parties, dated March 29, 2010, as amended on December 27, 2011, June 29, 2012, May 10, 2013 and June 26, 2014 (the “Loan Agreement”).

The Amendment amends the Loan Agreement by extending the maturity date of the \$15.0 million revolving line of credit from September 30, 2014 to December 31, 2014.

The foregoing description of the material terms of the Amendment does not purport to be a complete description of the rights and obligations of the parties thereunder and is qualified in its entirety by reference to the full text of the Amendment, which is filed as Exhibit 10.1 to this Form 10-Q.

Separation Agreement with James Flaherty

On September 30, 2014, the Company executed a separation agreement and release (the “Separation Agreement”) with James Flaherty, its former Chief Administrative Officer and Development Director.

Under the Separation Agreement, Mr. Flaherty received a severance package consisting of (1) \$295,250, to be paid in 26 installments on the Company's regular payroll schedule, commencing with the first scheduled payday on or following April 1, 2015, (2) in lieu of COBRA coverage, executive retiree medical and dental benefits for Mr. Flaherty and covered dependents, if applicable, through the earlier of (a) Mr. Flaherty's 65th birthday or (b) his eligibility for Medicare, and (3) acceleration of the vesting of 8,964 shares of equity awards previously granted to Mr. Flaherty that would have vested within the 12 month period following September 30, 2014 had Mr. Flaherty remained employed during such period. In exchange, Mr. Flaherty executed a release of claims agreement, will continue to be bound by the terms of any restrictive covenant agreements he had with the Company, and will provide consulting services as mutually agreed by Mr. Flaherty and the Company through December 31, 2015, at a rate of \$150 per hour.

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The foregoing description of the material terms of the Separation Agreement does not purport to be a complete description of the rights and obligations of the parties thereunder and is qualified in its entirety by reference to the full text of the Separation Agreement, which is filed as Exhibit 10.2 to this Form 10-Q.

ITEM 6. EXHIBITS

(a) Exhibits — See Exhibit Index on page following signatures

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SIGNATURES

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

Dated: November 7, 2014

CARDIOVASCULAR SYSTEMS, INC.

By /s/ David L. Martin  
David L. Martin  
President and Chief Executive Officer  
(Principal Executive Officer)

By /s/ Laurence L. Betterley  
Laurence L. Betterley  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX  
CARDIOVASCULAR SYSTEMS, INC.  
FORM 10-Q

Exhibit No. Description

10.1	Fifth Amendment to Loan and Security Agreement, dated September 29, 2014, by and between Cardiovascular Systems, Inc. and Silicon Valley Bank.
10.2	Separation Agreement and Release, dated September 30, 2014, between Cardiovascular Systems, Inc. and James Flaherty.
31.1*	Certification of President and Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of President and Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Financial statements from the quarterly report on Form 10-Q of the Company for the quarter ended September 30, 2014, formatted in XBRL: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Cash Flows, and (iv) the Notes to Financial Statements.

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\*Furnished herewith.