

MICROSTRATEGY INC  
Form 10-Q  
October 29, 2015  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

**For the Quarterly Period Ended September 30, 2015**

**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 000-24435**

**MICROSTRATEGY INCORPORATED**  
**(Exact name of registrant as specified in its charter)**

**Delaware**

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

**51-0323571**

**(I.R.S. Employer  
Identification Number)**

**1850 Towers Crescent Plaza, Tysons Corner, VA**

**(Address of Principal Executive Offices)**

**22182**

**(Zip Code)**

**(703) 848-8600**

**(Registrant's telephone number, including area code)**

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

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

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

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

Large accelerated filer ☒ Accelerated filer ☐

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

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

The number of shares of the registrant's class A common stock and class B common stock outstanding on October 22, 2015 was 9,329,603 and 2,035,184, respectively.

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**MICROSTRATEGY INCORPORATED**

**FORM 10-Q**

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Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****MICROSTRATEGY INCORPORATED****CONSOLIDATED BALANCE SHEETS****(in thousands, except per share data)**

|                                             | <b>September 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|---------------------------------------------|-------------------------------|------------------------------|
|                                             | (unaudited)                   |                              |
| <b>Assets</b>                               |                               |                              |
| Current assets:                             |                               |                              |
| Cash and cash equivalents                   | \$ 230,188                    | \$ 146,919                   |
| Restricted cash                             | 487                           | 661                          |
| Short-term investments                      | 226,689                       | 198,547                      |
| Accounts receivable, net                    | 55,039                        | 78,633                       |
| Prepaid expenses and other current assets   | 12,078                        | 17,669                       |
| Deferred tax assets, net                    | 12,373                        | 19,936                       |
| <b>Total current assets</b>                 | <b>536,854</b>                | <b>462,365</b>               |
| Property and equipment, net                 | 68,862                        | 77,852                       |
| Capitalized software development costs, net | 17,807                        | 13,469                       |
| Deposits and other assets                   | 2,184                         | 3,951                        |
| Deferred tax assets, net                    | 2,247                         | 1,160                        |
| <b>Total assets</b>                         | <b>\$ 627,954</b>             | <b>\$ 558,797</b>            |
| <b>Liabilities and Stockholders Equity</b>  |                               |                              |
| Current liabilities:                        |                               |                              |
| Accounts payable and accrued expenses       | \$ 26,609                     | \$ 35,458                    |
| Accrued compensation and employee benefits  | 38,570                        | 50,588                       |
| Accrued restructuring costs                 | 98                            | 2,284                        |
| Deferred revenue and advance payments       | 115,504                       | 108,413                      |
| Deferred tax liabilities                    | 395                           | 557                          |
| <b>Total current liabilities</b>            | <b>181,176</b>                | <b>197,300</b>               |
| Deferred revenue and advance payments       | 10,297                        | 10,818                       |
| Other long-term liabilities                 | 20,166                        | 22,679                       |
| Deferred tax liabilities                    | 7,803                         | 3,529                        |
| <b>Total liabilities</b>                    | <b>219,442</b>                | <b>234,326</b>               |

**Commitments and Contingencies****Stockholders' Equity**

|                                                                                                                                                                                            |                   |                   |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|-------------------|
| Preferred stock undesignated, \$0.001 par value; 5,000 shares authorized; no shares issued or outstanding                                                                                  | 0                 | 0                 |
| Class A common stock, \$0.001 par value; 330,000 shares authorized; 15,734 shares issued and 9,329 shares outstanding, and 15,660 shares issued and 9,255 shares outstanding, respectively | 16                | 16                |
| Class B convertible common stock, \$0.001 par value; 165,000 shares authorized; 2,035 shares issued and outstanding, and 2,055 shares issued and outstanding, respectively                 | 2                 | 2                 |
| Additional paid-in capital                                                                                                                                                                 | 525,632           | 506,727           |
| Treasury stock, at cost; 6,405 shares                                                                                                                                                      | (475,184)         | (475,184)         |
| Accumulated other comprehensive loss                                                                                                                                                       | (6,047)           | (4,363)           |
| Retained earnings                                                                                                                                                                          | 364,093           | 297,273           |
| <b>Total stockholders' equity</b>                                                                                                                                                          | <b>408,512</b>    | <b>324,471</b>    |
| <b>Total liabilities and stockholders' equity</b>                                                                                                                                          | <b>\$ 627,954</b> | <b>\$ 558,797</b> |

The accompanying notes are an integral part of these Consolidated Financial Statements.

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**MICROSTRATEGY INCORPORATED**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share data)

|                                                  | <b>Three Months Ended<br/>September 30,</b> |                |
|--------------------------------------------------|---------------------------------------------|----------------|
|                                                  | <b>2015</b>                                 | <b>2014</b>    |
|                                                  | (unaudited)                                 | (unaudited)    |
| <b>Revenues:</b>                                 |                                             |                |
| Product licenses                                 | \$ 27,511                                   | \$ 33,969      |
| Subscription services                            | 6,546                                       | 5,993          |
| Total product licenses and subscription services | 34,057                                      | 39,962         |
| Product support                                  | 71,392                                      | 75,019         |
| Other services                                   | 24,087                                      | 36,221         |
| <b>Total revenues</b>                            | <b>129,536</b>                              | <b>151,202</b> |
| <b>Cost of revenues:</b>                         |                                             |                |
| Product licenses                                 | 2,680                                       | 1,542          |
| Subscription services                            | 3,075                                       | 4,502          |
| Total product licenses and subscription services | 5,755                                       | 6,044          |
| Product support                                  | 3,174                                       | 3,695          |
| Other services                                   | 15,755                                      | 25,214         |
| <b>Total cost of revenues</b>                    | <b>24,684</b>                               | <b>34,953</b>  |
| <b>Gross profit</b>                              | <b>104,852</b>                              | <b>116,249</b> |
| <b>Operating expenses:</b>                       |                                             |                |
| Sales and marketing                              | 36,403                                      | 58,195         |
| Research and development                         | 17,789                                      | 28,659         |
| General and administrative                       | 19,843                                      | 24,811         |
| Restructuring costs                              | 86                                          | 11,578         |
| <b>Total operating expenses</b>                  | <b>74,121</b>                               | <b>123,243</b> |
| <b>Income (loss) from operations</b>             | <b>30,731</b>                               | <b>(6,994)</b> |
| Interest income, net                             | 116                                         | 53             |
| Other income, net                                | 766                                         | 4,928          |

|                                                                                         |             |               |
|-----------------------------------------------------------------------------------------|-------------|---------------|
| <b>Income (loss) before income taxes</b>                                                | 31,613      | (2,013)       |
| Provision for (benefit from) income taxes                                               | 7,720       | (1,168)       |
| <b>Net income (loss)</b>                                                                | 23,893      | (845)         |
| <br><b>Basic earnings (loss) per share (1)</b>                                          | <br>\$ 2.10 | <br>\$ (0.07) |
| Weighted average shares outstanding used in computing basic earnings (loss) per share   | 11,365      | 11,301        |
| <br><b>Diluted earnings (loss) per share (1)</b>                                        | <br>\$ 2.06 | <br>\$ (0.07) |
| Weighted average shares outstanding used in computing diluted earnings (loss) per share | 11,589      | 11,301        |

(1) Basic and fully diluted earnings (loss) per share for class A and class B common stock are the same.  
The accompanying notes are an integral part of these Consolidated Financial Statements.

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**MICROSTRATEGY INCORPORATED**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

(in thousands, except per share data)

|                                                      | <b>Nine Months Ended<br/>September 30,</b> |              |
|------------------------------------------------------|--------------------------------------------|--------------|
|                                                      | <b>2015</b>                                | <b>2014</b>  |
|                                                      | (unaudited)                                | (unaudited)  |
| <b>Revenues:</b>                                     |                                            |              |
| Product licenses                                     | \$ 77,634                                  | \$ 91,208    |
| Subscription services                                | 20,285                                     | 16,317       |
| <br>Total product licenses and subscription services | <br>97,919                                 | <br>107,525  |
| Product support                                      | 211,444                                    | 221,069      |
| Other services                                       | 76,984                                     | 102,365      |
| <br><b>Total revenues</b>                            | <br>386,347                                | <br>430,959  |
| <br><b>Cost of revenues:</b>                         |                                            |              |
| Product licenses                                     | 5,895                                      | 5,456        |
| Subscription services                                | 9,800                                      | 13,829       |
| <br>Total product licenses and subscription services | <br>15,695                                 | <br>19,285   |
| Product support                                      | 9,734                                      | 10,713       |
| Other services                                       | 52,265                                     | 73,577       |
| <br><b>Total cost of revenues</b>                    | <br>77,694                                 | <br>103,575  |
| <br><b>Gross profit</b>                              | <br>308,653                                | <br>327,384  |
| <br><b>Operating expenses:</b>                       |                                            |              |
| Sales and marketing                                  | 109,142                                    | 178,028      |
| Research and development                             | 48,051                                     | 89,469       |
| General and administrative                           | 63,071                                     | 76,376       |
| Restructuring costs                                  | 261                                        | 11,578       |
| <br><b>Total operating expenses</b>                  | <br>220,525                                | <br>355,451  |
| <br><b>Income (loss) from operations</b>             | <br>88,128                                 | <br>(28,067) |
| Interest income, net                                 | 129                                        | 133          |
| Other income, net                                    | 2,601                                      | 3,336        |

|                                                                                         |             |               |
|-----------------------------------------------------------------------------------------|-------------|---------------|
| <b>Income (loss) before income taxes</b>                                                | 90,858      | (24,598)      |
| Provision for (benefit from) income taxes                                               | 24,038      | (6,934)       |
| <b>Net income (loss)</b>                                                                | 66,820      | (17,664)      |
| <br><b>Basic earnings (loss) per share (1)</b>                                          | <br>\$ 5.89 | <br>\$ (1.56) |
| Weighted average shares outstanding used in computing basic earnings (loss) per share   | 11,345      | 11,301        |
| <br><b>Diluted earnings (loss) per share (1)</b>                                        | <br>\$ 5.80 | <br>\$ (1.56) |
| Weighted average shares outstanding used in computing diluted earnings (loss) per share | 11,521      | 11,301        |

(1) Basic and fully diluted earnings (loss) per share for class A and class B common stock are the same.  
The accompanying notes are an integral part of these Consolidated Financial Statements.

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**MICROSTRATEGY INCORPORATED**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

(in thousands)

|                                                                                 | <b>Three Months Ended<br/>September 30,</b> |                   |
|---------------------------------------------------------------------------------|---------------------------------------------|-------------------|
|                                                                                 | <b>2015</b>                                 | <b>2014</b>       |
|                                                                                 | (unaudited)                                 | (unaudited)       |
| <b>Net income (loss)</b>                                                        | \$ 23,893                                   | \$ (845)          |
| Other comprehensive income (loss), net of applicable taxes:                     |                                             |                   |
| Foreign currency translation adjustment                                         | (597)                                       | (2,103)           |
| Less: reclassification adjustment for translation gain included in other income | 280                                         | 0                 |
| Foreign currency translation adjustment, net                                    | (317)                                       | (2,103)           |
| Unrealized (loss) gain on short-term investments                                | (21)                                        | 4                 |
| <b>Total other comprehensive loss</b>                                           | <b>(338)</b>                                | <b>(2,099)</b>    |
| <b>Comprehensive income (loss)</b>                                              | <b>\$ 23,555</b>                            | <b>\$ (2,944)</b> |

|                                                                                 | <b>Nine Months Ended<br/>September 30,</b> |                    |
|---------------------------------------------------------------------------------|--------------------------------------------|--------------------|
|                                                                                 | <b>2015</b>                                | <b>2014</b>        |
|                                                                                 | (unaudited)                                | (unaudited)        |
| <b>Net income (loss)</b>                                                        | \$ 66,820                                  | \$ (17,664)        |
| Other comprehensive income (loss), net of applicable taxes:                     |                                            |                    |
| Foreign currency translation adjustment                                         | (1,649)                                    | (2,186)            |
| Less: reclassification adjustment for translation gain included in other income | 280                                        | 0                  |
| Foreign currency translation adjustment, net                                    | (1,369)                                    | (2,186)            |
| Unrealized (loss) gain on short-term investments                                | (35)                                       | 23                 |
| <b>Total other comprehensive loss</b>                                           | <b>(1,404)</b>                             | <b>(2,163)</b>     |
| <b>Comprehensive income (loss)</b>                                              | <b>\$ 65,416</b>                           | <b>\$ (19,827)</b> |

The accompanying notes are an integral part of these Consolidated Financial Statements.

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**MICROSTRATEGY INCORPORATED**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

|                                                                                             | <b>Nine Months Ended<br/>September 30,</b> |             |
|---------------------------------------------------------------------------------------------|--------------------------------------------|-------------|
|                                                                                             | <b>2015</b>                                | <b>2014</b> |
|                                                                                             | (unaudited)                                | (unaudited) |
| <b>Operating activities:</b>                                                                |                                            |             |
| Net income (loss)                                                                           | \$ 66,820                                  | \$ (17,664) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities:    |                                            |             |
| Depreciation and amortization                                                               | 16,172                                     | 19,305      |
| Bad debt expense                                                                            | 683                                        | 2,242       |
| Unrealized net loss (gain) on foreign currency forward contracts                            | 1,641                                      | (926)       |
| Non-cash portion of adjustments to accrued restructuring costs                              | (127)                                      | 165         |
| Deferred taxes                                                                              | 11,015                                     | (12,337)    |
| Release of liabilities for unrecognized tax benefits                                        | (61)                                       | 0           |
| Share-based compensation expense                                                            | 12,503                                     | 8,561       |
| Excess tax benefits from share-based compensation arrangements                              | (963)                                      | 0           |
| Reclassification of foreign currency translation adjustment from other comprehensive income | (280)                                      | 0           |
| <b>Changes in operating assets and liabilities:</b>                                         |                                            |             |
| Accounts receivable                                                                         | 19,511                                     | 23,488      |
| Prepaid expenses and other current assets                                                   | 3,377                                      | (5,197)     |
| Deposits and other assets                                                                   | 1,562                                      | 412         |
| Accounts payable and accrued expenses                                                       | (4,933)                                    | (2,757)     |
| Accrued compensation and employee benefits                                                  | (10,275)                                   | (19,380)    |
| Accrued restructuring costs                                                                 | (1,940)                                    | 8,083       |
| Deferred revenue and advance payments                                                       | 11,153                                     | 11,723      |
| Other long-term liabilities                                                                 | (2,415)                                    | 603         |
| Net cash provided by operating activities                                                   | 123,443                                    | 16,321      |
| <b>Investing activities:</b>                                                                |                                            |             |
| Proceeds from redemption of short-term investments                                          | 316,000                                    | 222,300     |
| Purchases of property and equipment                                                         | (3,352)                                    | (11,856)    |
| Purchases of short-term investments                                                         | (344,033)                                  | (303,565)   |
| Capitalized software development costs                                                      | (9,598)                                    | (2,254)     |
| Decrease (increase) in restricted cash                                                      | 113                                        | (1,013)     |
| Net cash used in investing activities                                                       | (40,870)                                   | (96,388)    |
| <b>Financing activities:</b>                                                                |                                            |             |
| Proceeds from sale of class A common stock under exercise of employee stock options         | 5,439                                      | 0           |
| Excess tax benefits from share-based compensation arrangements                              | 963                                        | 0           |

|                                                                             |                   |                   |
|-----------------------------------------------------------------------------|-------------------|-------------------|
| Payments on capital lease obligations and other financing arrangements      | (1,430)           | (2,035)           |
| Net cash provided by (used in) financing activities                         | 4,972             | (2,035)           |
| <b>Effect of foreign exchange rate changes on cash and cash equivalents</b> | <b>(4,276)</b>    | <b>(2,063)</b>    |
| <b>Net increase (decrease) in cash and cash equivalents</b>                 | <b>83,269</b>     | <b>(84,165)</b>   |
| <b>Cash and cash equivalents, beginning of period</b>                       | <b>146,919</b>    | <b>220,171</b>    |
| <b>Cash and cash equivalents, end of period</b>                             | <b>\$ 230,188</b> | <b>\$ 136,006</b> |

**Supplemental disclosure of noncash investing and financing activities:**

|                                                                                  |       |      |
|----------------------------------------------------------------------------------|-------|------|
| Assets acquired under capital lease obligations and other financing arrangements | \$ 14 | \$ 0 |
|----------------------------------------------------------------------------------|-------|------|

The accompanying notes are an integral part of these Consolidated Financial Statements.

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**MICROSTRATEGY INCORPORATED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(unaudited)

**(1) Summary of Significant Accounting Policies**

***(a) Basis of Presentation***

Except for the Consolidated Balance Sheet of MicroStrategy Incorporated ( *MicroStrategy* or the *Company* ) as of December 31, 2014, which was derived from audited financial statements, the accompanying Consolidated Financial Statements are unaudited. In the opinion of management, all adjustments necessary for a fair statement of such financial position and results of operations have been included. All such adjustments are of a normal recurring nature unless otherwise disclosed. Interim results are not necessarily indicative of results for a full year.

Certain amounts in the prior year's Consolidated Financial Statements and Notes to Consolidated Financial Statements have been reclassified to conform to current year presentation. Revenues and cost of revenues have been reclassified in the Consolidated Statements of Operations to reflect the separate components of total product licenses and subscription services, and unrealized gains and losses on foreign currency forward contracts have been reclassified within the operating section in the Consolidated Statements of Cash Flows.

The Consolidated Financial Statements and Notes to Consolidated Financial Statements are presented as required by the United States Securities and Exchange Commission ( *SEC* ) and do not contain certain information included in the Company's annual financial statements and notes. These financial statements should be read in conjunction with the Company's audited financial statements and the notes thereto filed with the SEC in the Company's Annual Report on Form 10-K for the year ended December 31, 2014. There have been no significant changes in the Company's accounting policies since December 31, 2014.

The accompanying Consolidated Financial Statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

**(2) Recent Accounting Standards**

In May 2014, the Financial Accounting Standards Board ( *FASB* ) issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* ( *ASU 2014-09* ), which supersedes nearly all existing revenue recognition guidance. The standard's core principle is that an entity should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard creates a five-step model to achieve its core principle: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the separate performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. In addition, entities must disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Qualitative and quantitative disclosures are required about: (1) the entity's contracts with customers, (2) the significant judgments, and changes in judgments, made in applying the guidance to those contracts, and (3) any assets recognized from the costs to obtain or fulfill a contract with a customer. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic*

606) *Deferral of the Effective Date*, which defers the effective date of ASU 2014-09 to interim and annual periods beginning January 1, 2018. The standard allows entities to apply the standard retrospectively to each prior reporting period presented ( full retrospective adoption ) or retrospectively with the cumulative effect of initially applying the standard recognized at the date of initial application ( modified retrospective adoption ). The Company is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

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**MICROSTRATEGY INCORPORATED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(unaudited)

In April 2015, the FASB issued Accounting Standards Update No. 2015-05, *Intangibles – Goodwill and Other Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement* (ASU 2015-05), which provides guidance on which existing accounting model should be applied to cloud computing arrangements. Under ASU 2015-05, customers will apply the same criteria as vendors to determine whether a cloud computing arrangement contains a software license or is solely a service contract. Specifically, fees paid by a customer in a cloud computing arrangement will be subject to internal-use software guidance if the customer has both the contractual right to take possession of the software at any time without significant penalty and it is feasible for the customer to run the software on its own hardware. Arrangements that do not meet both of the criteria are considered service contracts, and separate accounting for a license will not be permitted. ASU 2015-05 is effective for interim and annual periods beginning January 1, 2016. The standard allows entities to apply the standard retrospectively or prospectively for all new transactions entered into or materially modified after the date of adoption. The Company utilizes certain cloud computing arrangements in its daily business operations and is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

**(3) Fair Value Measurements**

The Company measures certain assets and liabilities at fair value on a recurring basis. Fair value is defined as the price that is expected to be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company uses a three-level hierarchy that prioritizes fair value measurements based on the types of inputs used for the various valuation techniques. The three levels of the fair value hierarchy are described below:

- Level 1: Quoted (unadjusted) prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.
- Level 2: Inputs other than quoted prices that are either directly or indirectly observable, such as quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3: Inputs that are generally unobservable, supported by little or no market activity, and typically reflect management’s estimates of assumptions that market participants would use in pricing the asset or liability.

The categorization of an asset or liability within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The valuation techniques used by the Company when measuring fair value maximize the use of observable inputs and minimize the use of unobservable inputs.

The Company is exposed to certain risks related to its ongoing business operations, including the effect of changes in foreign exchange rates on the Company’s monetary assets and liabilities denominated in foreign currency. The

Company may use foreign currency forward contracts as part of its strategy to manage these risks, but does not hold or issue derivative instruments for trading purposes or speculation. The Company executes these instruments with financial institutions that hold an investment grade credit rating. These foreign currency forward contracts do not meet the requirements for hedge accounting and are recorded on the balance sheet as either an asset or liability measured at their fair value as of the reporting date. Changes in the fair value of derivative instruments, as measured using the three-level hierarchy described above, are recognized in Other income, net in the Company's Consolidated Statements of Operations.

Table of Contents**MICROSTRATEGY INCORPORATED****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(unaudited)

As of September 30, 2015, there were no financial assets or liabilities measured at fair value on a recurring basis. As of December 31, 2014, financial assets and liabilities measured at fair value on a recurring basis, by level within the fair value hierarchy, consisted of the following (in thousands):

| Line Item                                 | December 31, 2014<br>Fair Value Measurements<br>Using Input Types |          |         |          |
|-------------------------------------------|-------------------------------------------------------------------|----------|---------|----------|
|                                           | Level 1                                                           | Level 2  | Level 3 | Total    |
| <b>Non-hedging derivative assets:</b>     |                                                                   |          |         |          |
| Foreign currency forward contracts        |                                                                   |          |         |          |
| Prepaid expenses and other current assets | \$ 0                                                              | \$ 1,647 | \$ 0    | \$ 1,647 |

**Non-hedging derivative liabilities:**

|                                       |      |      |      |      |
|---------------------------------------|------|------|------|------|
| Foreign currency forward contracts    |      |      |      |      |
| Accounts payable and accrued expenses | \$ 0 | \$ 6 | \$ 0 | \$ 6 |

The fair value of our foreign currency forward contracts is determined using Level 2 observable market inputs to extrapolate forward points to be added to or subtracted from the closing market spot rate on the reporting date, and then discounted to present value.

Changes in the fair value of our foreign currency forward contracts (in thousands) for the three and nine months ended September 30, 2015 and 2014 were as follows:

| Location                                                     | Gain (Loss) on Derivative Instruments Recognized in Income |          |                   |          |
|--------------------------------------------------------------|------------------------------------------------------------|----------|-------------------|----------|
|                                                              | Three Months Ended                                         |          | Nine Months Ended |          |
|                                                              | September 30,                                              |          | September 30,     |          |
|                                                              | 2015                                                       | 2014     | 2015              | 2014     |
| <b>Non-hedging derivative instruments:</b>                   |                                                            |          |                   |          |
| Unrealized gain (loss) on foreign currency forward contracts |                                                            |          |                   |          |
| Other income, net                                            | \$ 0                                                       | \$ 1,012 | \$ (1,641)        | \$ 926   |
| Realized gain (loss) on foreign currency forward contracts   |                                                            |          |                   |          |
| Other income,                                                | \$ 0                                                       | \$ 0     | \$ 2,129          | \$ (562) |

net

The unrealized gain (loss) on foreign currency forward contracts line item in the above table includes both the unrealized fair value gains and losses on outstanding foreign currency forward contracts and the reversal of previous period unrealized gains and losses upon the settlement of foreign currency forward contracts. There were no foreign currency forward contracts outstanding as of September 30, 2015. There were no transfers among the levels within the fair value hierarchy during each of the three and nine months ended September 30, 2015 and 2014. As of September 30, 2015 and December 31, 2014, the Company had no assets or liabilities that were required to be measured at fair value on a non-recurring basis.

The Company also estimates the fair value of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses, accrued compensation and employee benefits, and accrued restructuring costs. The Company considers the carrying value of these instruments in the financial statements to approximate fair value due to their short maturities.

#### **(4) Short-term Investments**

The Company periodically invests a portion of its excess cash in short-term investment instruments. Substantially all of the Company's short-term investments are in U.S. Treasury securities, and the Company has the ability and intent to hold these investments to maturity. The stated maturity dates of these investments are between three months and one year from the purchase date. These held-to-maturity investments are recorded at amortized cost and included within

Short-term investments on the accompanying Consolidated Balance Sheets. The fair value of held-to-maturity investments in U.S. Treasury securities is determined based on quoted market prices in active markets for identical securities (Level 1 inputs).

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The amortized cost, carrying value, and fair value of held-to-maturity investments at September 30, 2015 were \$226.6 million, \$226.6 million, and \$226.7 million, respectively. The amortized cost, carrying value, and fair value of held-to-maturity investments at December 31, 2014 were \$198.5 million, \$198.5 million, and \$198.5 million, respectively. The gross unrecognized holding gains and losses were not material for each of the three and nine months ended September 30, 2015 and 2014. No other-than-temporary impairments related to these investments have been recognized in accumulated other comprehensive loss as of September 30, 2015 and December 31, 2014. As of September 30, 2015 and December 31, 2014, the Company's available-for-sale investments were not material.

**(5) Accounts Receivable**

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

|                                       | <b>September 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|---------------------------------------|-------------------------------|------------------------------|
| Billed and billable                   | \$ 115,389                    | \$ 187,470                   |
| Less: unpaid deferred revenue         | (56,599)                      | (104,425)                    |
| Accounts receivable, gross            | 58,790                        | 83,045                       |
| Less: allowance for doubtful accounts | (3,751)                       | (4,412)                      |
| Accounts receivable, net              | \$ 55,039                     | \$ 78,633                    |

The Company offsets its accounts receivable and deferred revenue for any unpaid items included in deferred revenue and advance payments.

The Company maintains an allowance for doubtful accounts which represents its best estimate of probable losses inherent in the accounts receivable balances. The Company evaluates specific accounts when it becomes aware that a customer may not be able to meet its financial obligations due to deterioration of its liquidity or financial viability, credit ratings, or bankruptcy. In addition, the Company periodically adjusts this allowance based upon its review and assessment of the aging of receivables.

**(6) Restructuring**

In September 2014, the Company committed to a restructuring plan (the "2014 Restructuring Plan") to streamline its workforce and spending to better align its cost structure with its business strategy, including reducing the Company's workforce by 777 employees, comprised of 217 employees in North America, 400 employees in Asia Pacific, 141 employees in Europe, the Middle East, and Africa, and 19 employees in Latin America. As of December 31, 2014, the Company had implemented substantially all of the 2014 Restructuring Plan. The Company does not expect future

costs associated with implementing the remainder of the 2014 Restructuring Plan, consisting primarily of the liquidation of certain foreign subsidiaries, to be material.

Costs associated with the 2014 Restructuring Plan included employee severance and related benefit costs (including outplacement services and continuing health insurance coverage), contract termination costs (including operating lease terminations for certain office space at the Company's corporate headquarters and other international locations), and other charges (including external consulting and advisory fees related to implementing the restructuring plan). The following table summarizes the major types of costs associated with the 2014 Restructuring Plan (in thousands) for each of the three and nine months ended September 30, 2015 and 2014, total costs incurred through September 30, 2015 and total costs expected to be incurred:

|                                         | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |           | Cumulative Cost<br>Incurred To<br>Date | Total Expected<br>Plan Costs |
|-----------------------------------------|-------------------------------------|-----------|------------------------------------|-----------|----------------------------------------|------------------------------|
|                                         | 2015                                | 2014      | 2015                               | 2014      |                                        |                              |
| Severance and related employee benefits | \$ 0                                | \$ 10,107 | \$ 0                               | \$ 10,107 | \$ 13,162                              | \$ 13,162                    |
| Contract termination costs              | 0                                   | 1,358     | 0                                  | 1,358     | 1,159                                  | 1,159                        |
| Other costs                             | 86                                  | 113       | 261                                | 113       | 672                                    | 749                          |
| Total restructuring costs               | \$ 86                               | \$ 11,578 | \$ 261                             | \$ 11,578 | \$ 14,993                              | \$ 15,070                    |

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The total restructuring costs above are reported as Restructuring costs under Operating expenses in the Company's Consolidated Statements of Operations.

Restructuring-related liabilities are reported as Accrued restructuring costs in the Company's Consolidated Balance Sheets. The following table presents a summary of changes in the restructuring-related liabilities (in thousands) for the nine months ended September 30, 2015:

|                                                  | Balance as of<br>January 1, 2015 | Costs<br>Incurred | Cash<br>Payments  | Non-cash<br>Settlements | Adjustments<br>and<br>Other | Balance<br>as of<br>September 30, 2015 |
|--------------------------------------------------|----------------------------------|-------------------|-------------------|-------------------------|-----------------------------|----------------------------------------|
| <b>Current:</b>                                  |                                  |                   |                   |                         |                             |                                        |
| Severance and related employee benefits          | \$ 2,215                         | \$ 0              | \$ (1,885)        | \$ 0                    | \$ (237)                    | \$ 93                                  |
| Contract termination costs                       | 0                                | 0                 | 0                 | 0                       | 0                           | 0                                      |
| Other costs                                      | 69                               | 261               | (315)             | 0                       | (10)                        | 5                                      |
| <b>Total current accrued restructuring costs</b> | <b>\$ 2,284</b>                  | <b>\$ 261</b>     | <b>\$ (2,200)</b> | <b>\$ 0</b>             | <b>\$ (247)</b>             | <b>\$ 98</b>                           |

**(7) Deferred Revenue and Advance Payments**

Deferred revenue and advance payments (in thousands) from customers consisted of the following, as of:

|                                                         | September 30,<br>2015 | December 31,<br>2014 |
|---------------------------------------------------------|-----------------------|----------------------|
| <b>Current:</b>                                         |                       |                      |
| Deferred product licenses revenue                       | \$ 13,155             | \$ 10,927            |
| Deferred subscription services revenue                  | 11,172                | 16,018               |
| Deferred product support revenue                        | 135,999               | 168,833              |
| Deferred other services revenue                         | 6,794                 | 10,564               |
| <br>Gross current deferred revenue and advance payments | <br>167,120           | <br>206,342          |
| Less: unpaid deferred revenue                           | (51,616)              | (97,929)             |
| <br>Net current deferred revenue and advance payments   | <br>\$ 115,504        | <br>\$ 108,413       |
| <br><b>Non-current:</b>                                 |                       |                      |

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|                                                         |           |           |
|---------------------------------------------------------|-----------|-----------|
| Deferred product licenses revenue                       | \$ 6,344  | \$ 8,012  |
| Deferred subscription services revenue                  | 808       | 750       |
| Deferred product support revenue                        | 6,962     | 7,505     |
| Deferred other services revenue                         | 1,166     | 1,047     |
| Gross non-current deferred revenue and advance payments | 15,280    | 17,314    |
| Less: unpaid deferred revenue                           | (4,983)   | (6,496)   |
| Net non-current deferred revenue and advance payments   | \$ 10,297 | \$ 10,818 |

The Company offsets its accounts receivable and deferred revenue for any unpaid items included in deferred revenue and advance payments.

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**(8) Commitments and Contingencies**

***(a) Commitments***

From time to time, the Company enters into certain types of contracts that require it to indemnify parties against third-party claims. These contracts primarily relate to agreements under which the Company has agreed to indemnify customers and partners for third-party claims arising from intellectual property infringement. The conditions of these obligations vary. Thus, the overall maximum amount of the Company's indemnification obligations cannot be reasonably estimated. Historically, the Company has not been obligated to make significant payments for these obligations and does not currently expect to incur any material obligations in the future. Accordingly, the Company has not recorded an indemnification liability on its balance sheets as of September 30, 2015 or December 31, 2014.

The Company leases office space and computer and other equipment under operating lease agreements. It also leases certain computer and other equipment under capital lease agreements and licenses certain software under other financing arrangements. Under the lease agreements, in addition to base rent, the Company is generally responsible for certain taxes, utilities and maintenance costs, and other fees; and several leases include options for renewal or purchase. As of December 31, 2014, the Company was leasing approximately 233,000 square feet of office space at a location in Northern Virginia that began serving as its corporate headquarters in October 2010. The Company gave written notice in August 2014 of its intent to terminate the lease with respect to 19,000 square feet of this office space, effective February 2015, as part of the 2014 Restructuring Plan. The Company never used the terminated lease space, and it remained vacant until it was terminated in February 2015. The term of the amended lease expires in December 2020.

At September 30, 2015 and December 31, 2014, deferred rent of \$16.6 million and \$18.9 million, respectively, is included in other long-term liabilities, and \$3.3 million and \$3.0 million, respectively, is included in current accrued expenses.

***(b) Contingencies***

In December 2011, DataTern, Inc. ( "DataTern" ) filed a complaint for patent infringement against the Company in the United States District Court for the District of Massachusetts (the "District Court" ). The complaint alleged that the Company infringes U.S. Patent No. 6,101,502 (the "502 Patent" ), allegedly owned by DataTern, by making, selling, or offering for sale several of the Company's products and services including MicroStrategy 9 , MicroStrategy Intelligence Server, MicroStrategy Business Intelligence Platform , MicroStrategy Cloud Personal, and other MicroStrategy applications for creating or using data mining, dashboards, business analytics, data storage and warehousing, and Web hosting support. The complaint accused the Company of willful infringement and sought an unspecified amount of damages, an award of attorneys' fees, and preliminary and permanent injunctive relief. In light of a judgment in a separate action involving DataTern in another jurisdiction, in February 2013, MicroStrategy and DataTern filed motions for summary judgment of non-infringement and the District Court entered summary judgment against DataTern. In March 2013, DataTern filed a notice of appeal with the United States Court of Appeals for the Federal

Circuit (the Federal Circuit ). In December 2014, the Federal Circuit issued an opinion vacating the District Court s summary judgment, stating that the claim construction on which the summary judgment was based was incorrect. In January 2015, the Federal Circuit ordered that the case be remanded for further proceedings, and in February 2015, the Company filed motions for summary judgment in the District Court on grounds of non-infringement and invalidity. On September 4, 2015, the District Court denied the Company s motions for summary judgment. The Company has received indemnification requests from certain of its channel partners and customers who were sued by DataTern in the District Court in lawsuits alleging infringement of the 502 Patent. The outcome of these matters is not presently determinable, and the Company cannot make a reasonable estimate of the possible loss or range of loss with respect to these matters at this time. Accordingly, no estimated liability for these matters has been accrued in the accompanying Consolidated Financial Statements.

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The Company is also involved in various other legal proceedings arising in the normal course of business. Although the outcomes of these other legal proceedings are inherently difficult to predict, management does not expect the resolution of these other legal proceedings to have a material adverse effect on the Company's financial position, results of operations, or cash flows.

The Company has contingent liabilities that, in management's judgment, are not probable of assertion. If such unasserted contingent liabilities were to be asserted, or become probable of assertion, the Company may be required to record significant expenses and liabilities in the period in which these liabilities are asserted or become probable of assertion.

**(9) Treasury Stock**

The Board of Directors has authorized the Company's repurchase of up to an aggregate of \$800.0 million of its class A common stock from time to time on the open market through April 29, 2018 (the "2005 Share Repurchase Program"), although the program may be suspended or discontinued by the Company at any time. The timing and amount of any shares repurchased will be determined by the Company's management based on its evaluation of market conditions and other factors. The 2005 Share Repurchase Program may be funded using the Company's working capital, as well as proceeds from any other funding arrangements that the Company may enter into in the future. During each of the three and nine months ended September 30, 2015 and 2014, the Company did not repurchase any shares of its class A common stock pursuant to the 2005 Share Repurchase Program. As of September 30, 2015, the Company had repurchased an aggregate of 3,826,947 shares of its class A common stock at an average price per share of \$90.23 and an aggregate cost of \$345.3 million. The average price per share and aggregate cost amounts disclosed above include broker commissions.

**(10) Income Taxes**

The Company and its subsidiaries conduct business in the U.S. and various foreign countries and are subject to taxation in numerous domestic and foreign jurisdictions. As a result of its business activities, the Company files tax returns that are subject to examination by various federal, state and local, and foreign tax authorities. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or foreign income tax examination by tax authorities for years before 2011. However, due to its use of state net operating loss ("NOL") and federal tax credit carryovers in the U.S., U.S. tax authorities may attempt to reduce or fully offset the amount of state NOL or federal tax credit carryovers from tax years ended in 2007 and forward that were used in later tax years. The Company's major foreign tax jurisdictions and tax years that remain subject to potential examination are Germany for tax years 2013 forward, Poland and China for tax years 2010 forward, Spain for tax years 2011 forward, and the United Kingdom for tax years 2013 forward. The Company settled a tax examination in Germany for years 2009 to 2012 in the first quarter of 2015 without a material assessment. The Company is currently under tax examination in the United States for tax years 2011 and 2012. To date, this audit has not resulted in any material assessment.

As of September 30, 2015, the Company had unrecognized tax benefits of \$2.7 million, which are recorded in other long-term liabilities. If recognized, \$1.9 million of these unrecognized tax benefits would impact the effective tax rate. The Company recognizes estimated accrued interest related to unrecognized income tax benefits in the provision for income tax accounts. Penalties relating to income taxes, if incurred, would also be recognized as a component of the Company's provision for income taxes. Over the next 12 months, the amount of the Company's liability for unrecognized tax benefits is not expected to change by a material amount. As of September 30, 2015, the amount of cumulative accrued interest expense on unrecognized income tax benefits was approximately \$0.5 million.

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The following table summarizes the Company's deferred tax assets, net of deferred tax liabilities and valuation allowance (in thousands), as of:

|                                                                              | <b>September 30, 2015</b> | <b>December 31, 2014</b> |
|------------------------------------------------------------------------------|---------------------------|--------------------------|
| Deferred tax assets, net of deferred tax liabilities                         | \$ 8,518                  | \$ 19,321                |
| Valuation allowance                                                          | (2,096)                   | (2,311)                  |
| Deferred tax assets, net of deferred tax liabilities and valuation allowance | \$ 6,422                  | \$ 17,010                |

The valuation allowance as of September 30, 2015 and December 31, 2014 primarily relates to certain foreign net operating loss carryforward and foreign tax credit carryforward tax assets. The Company has determined that there is insufficient positive evidence that it is more likely than not that such deferred tax assets will be realized.

The Company has estimated its annual effective tax rate for the full fiscal year 2015 and applied that rate to its income before income taxes in determining its provision for income taxes for the nine months ended September 30, 2015. The Company also records discrete items in each respective period as appropriate. The estimated effective tax rate is subject to fluctuation based upon the level and mix of earnings and losses by tax jurisdiction, foreign tax rate differentials, and the relative impact of permanent book to tax differences (e.g., non-deductible expenses). Each quarter, a cumulative adjustment is recorded for any fluctuations in the estimated annual effective tax rate as compared to the prior quarter. As a result of these factors, and due to potential changes in the Company's period to period results, fluctuations in the Company's effective tax rate and respective tax provisions or benefits may occur.

For the nine months ended September 30, 2015, the Company recorded a provision for income taxes of \$24.0 million that resulted in an effective tax rate of 26.5%, as compared to a benefit from income taxes of \$6.9 million that resulted in an effective tax rate of 28.2% for the nine months ended September 30, 2014. The change in the effective tax rate in 2015 is mainly due to changes in the forecasted overall income or loss amounts for 2015, a change in the expected proportion of U.S. versus foreign income, and changes in discrete tax benefits.

Except as discussed below, the Company intends to indefinitely reinvest its undistributed earnings of all of its foreign subsidiaries. Therefore, the annualized effective tax rate applied to the Company's pre-tax income does not include any provision for U.S. federal and state income taxes on the amount of the undistributed foreign earnings. U.S. federal tax laws, however, require the Company to include in its U.S. taxable income certain investment income earned outside of the U.S. in excess of certain limits (Subpart F deemed dividends). Because Subpart F deemed dividends are already required to be recognized in the Company's U.S. federal income tax return, the Company regularly repatriates Subpart F deemed dividends to the U.S. and no additional tax is incurred on the distribution. As of September 30, 2015 and December 31, 2014, the amount of cash and cash equivalents and short-term investments held by U.S. entities was \$196.4 million and \$139.1 million, respectively, and by non-U.S. entities was \$260.5 million and \$206.4 million,

respectively. If the cash and cash equivalents and short-term investments held by non-U.S. entities were to be repatriated to the U.S., the Company would generate U.S. taxable income to the extent of the Company's undistributed foreign earnings, which amounted to \$201.7 million at December 31, 2014. Although the tax impact of repatriating these earnings is difficult to determine, the Company would not expect the maximum effective tax rate that would be applicable to such repatriation to exceed the U.S. statutory rate of 35.0%, after considering applicable foreign tax credits.

In determining the Company's provision or benefit for income taxes, net deferred tax assets, liabilities, and valuation allowances, management is required to make judgments and estimates related to projections of domestic and foreign profitability, the timing and extent of the utilization of net operating loss carryforwards, applicable tax rates, transfer pricing methods, and prudent and feasible tax planning strategies. As a multinational company, the Company is required to calculate and provide for estimated income tax liabilities for each of the tax jurisdictions in which it operates. This process involves estimating current tax obligations and exposures in each jurisdiction, as well as making judgments regarding the future recoverability of deferred tax assets. Changes in the estimated level of annual pre-tax income, changes in tax laws, particularly changes related to the utilization of net operating losses in various jurisdictions, and changes resulting from tax audits can all affect the overall effective income tax rate which, in turn, impacts the overall level of income tax expense or benefit and net income.

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Judgments and estimates related to the Company's projections and assumptions are inherently uncertain; therefore, actual results could differ materially from projections. The timing and manner in which the Company will use research and development tax credit carryforward tax assets, alternative minimum tax credit carryforward tax assets, and foreign tax credit carryforward tax assets in any year, or in total, may be limited by provisions of the Internal Revenue Code regarding changes in the Company's ownership. Currently, the Company expects to use the tax assets, subject to Internal Revenue Code limitations, within the carryforward periods. Valuation allowances have been established where the Company has concluded that it is more likely than not that such deferred tax assets are not realizable. If the Company is unable to sustain profitability in future periods, it may be required to increase the valuation allowance against the deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred.

**(11) Share-based Compensation**

The Company's 2013 Stock Incentive Plan (as amended, the "2013 Equity Plan") authorizes the issuance of various types of share-based awards to the Company's employees, officers, directors, and other eligible participants. In addition, the 2013 Equity Plan provides for automatic annual stock option grants (with the first set of such annual grants awarded in May 2015) to the Company's non-employee directors in the amount of 5,000 shares of the Company's class A common stock per director, per year. As of September 30, 2015, the total number of shares of the Company's class A common stock authorized for issuance under the 2013 Equity Plan was 1,500,000 shares. In October 2015, the Board of Directors authorized, subject to stockholder approval, an increase in the total number of shares of the Company's class A common stock authorized for issuance under the 2013 Equity Plan from 1,500,000 shares to 1,700,000 shares.

During the third quarter of 2015, stock options to purchase an aggregate of 130,000 shares of class A common stock were granted to certain Company officers and employees pursuant to the 2013 Equity Plan. As of September 30, 2015, there were options to purchase 1,436,250 shares of class A common stock outstanding under the 2013 Equity Plan and no remaining shares of class A common stock authorized for issuance and not subject to outstanding awards under the 2013 Equity Plan.

The following table summarizes the Company's stock option activity (in thousands, except per share data and years) for the three months ended September 30, 2015:

|        | Stock Options Outstanding |           |                       |
|--------|---------------------------|-----------|-----------------------|
|        | Weighted Average          | Aggregate | Weighted Average      |
|        | Exercise                  | Intrinsic | Remaining Contractual |
|        | Price                     | Value     | Term                  |
| Shares | Per Share                 | Value     | (Years)               |

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|                                           |       |    |        |               |
|-------------------------------------------|-------|----|--------|---------------|
| Balance as of July 1, 2015                | 1,306 | \$ | 120.62 |               |
| Granted                                   | 130   |    | 201.25 |               |
| Exercised                                 | 0     |    | 0.00   | \$ 0          |
| Forfeited/Expired                         | 0     |    | 0.00   |               |
| Balance as of September 30, 2015          | 1,436 | \$ | 127.91 |               |
| Exercisable as of September 30, 2015      | 351   | \$ | 103.09 | \$ 32,800 7.6 |
| Expected to vest as of September 30, 2015 | 1,035 | \$ | 138.03 | \$ 61,105 8.8 |
| Total                                     | 1,386 | \$ | 129.18 | \$ 93,904 8.5 |

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Stock options outstanding as of September 30, 2015 are comprised of the following range of exercise prices per share (in thousands, except per share data and years):

| <b>Stock Options Outstanding at September 30, 2015</b> |               |                                        |                                                            |
|--------------------------------------------------------|---------------|----------------------------------------|------------------------------------------------------------|
| <b>Range of Exercise Prices per Share</b>              | <b>Shares</b> | <b>Weighted Average Exercise Price</b> | <b>Weighted Average Remaining Contractual Term (Years)</b> |
| \$ 92.84 - \$120.00                                    | 507           | \$ 94.49                               | 6.9                                                        |
| \$120.01 - \$150.00                                    | 514           | \$ 121.43                              | 8.6                                                        |
| \$150.01 - \$180.00                                    | 285           | \$ 165.66                              | 9.3                                                        |
| \$180.01 - \$201.25                                    | 130           | \$ 201.25                              | 9.9                                                        |
| <b>Total</b>                                           | <b>1,436</b>  | <b>\$ 127.91</b>                       | <b>8.2</b>                                                 |

An aggregate of 125,000 stock options with an aggregate fair value of \$5.3 million vested during the three months ended September 30, 2015. The Company expects the majority of unvested options at September 30, 2015 to fully vest in future years in accordance with their vesting schedules. Share-based compensation expense has been adjusted, where applicable, for any expected forfeitures. The weighted average grant date fair value of stock option awards using the Black-Scholes pricing model was \$82.89 for each share subject to a stock option granted during the three months ended September 30, 2015, based on the following assumptions:

| <b>Three months ended September 30, 2015</b> |       |
|----------------------------------------------|-------|
| Expected term of options in years            | 6.3   |
| Expected volatility                          | 39.0% |
| Risk-free interest rate                      | 1.9%  |
| Expected dividend yield                      | 0.0%  |

No stock option awards were granted during the three months ended September 30, 2014.

For the three and nine months ended September 30, 2015, the Company recognized approximately \$4.5 million and \$12.5 million, respectively, in share-based compensation expense from stock options granted under the 2013 Equity

Plan. For the three and nine months ended September 30, 2014, the Company recognized approximately \$3.9 million and \$8.6 million, respectively, in share-based compensation expense from stock options granted under the 2013 Equity Plan. As of September 30, 2015, there was approximately \$54.5 million of total unrecognized share-based compensation expense related to unvested stock options. The Company expects to recognize this remaining share-based compensation expense over a weighted average vesting period of approximately 3.0 years.

During the nine months ended September 30, 2015, the Company was able to recognize and utilize net operating loss carryforwards arising directly from tax deductions related to equity compensation in excess of compensation recognized for financial reporting that was generated under the 2013 Equity Plan. Accordingly, stockholders' equity increased by \$1.0 million during the nine months ended September 30, 2015. During the nine months ended September 30, 2014, no windfall tax benefits were realized from the exercise of stock options.

## **(12) Common Equity and Earnings per Share**

The Company has two classes of common stock: class A common stock and class B common stock. Holders of class A common stock generally have the same rights, including rights to dividends, as holders of class B common stock, except that holders of class A common stock have one vote per share while holders of class B common stock have ten votes per share. Each share of class B common stock is convertible at any time, at the option of the holder, into one share of class A common stock. As such, basic and fully diluted earnings per share for class A common stock and for class B common stock are the same. The Company has never declared or paid any cash dividends on either class A or class B common stock. As of September 30, 2015 and December 31, 2014, there were no shares of preferred stock issued or outstanding.

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Potential shares of common stock are included in the diluted earnings per share calculation when dilutive. Potential shares of common stock, consisting of common stock issuable upon exercise of outstanding stock options, are calculated using the treasury stock method. For the three and nine months ended September 30, 2015, stock options issued under the 2013 Equity Plan to purchase a weighted average of approximately 318,000 and 276,000 shares of common stock, respectively, were excluded from the diluted earnings per share calculation because their impact would have been anti-dilutive. For the three and nine months ended September 30, 2014, stock options issued under the 2013 Equity Plan to purchase a weighted average of approximately 1,260,000 and 970,000 shares of common stock, respectively, were excluded from the diluted earnings per share calculation because their impact would have been anti-dilutive.

**(13) Segment Information**

The Company manages its business in one operating segment. The Company's one operating segment is engaged in the design, development, marketing, and sales of analytics, mobile, and security software platforms through licensing arrangements and cloud-based subscriptions and related services. It includes MicroStrategy 10 Secure Enterprise™ (which consists of MicroStrategy Analytics™, MicroStrategy Mobile™, and Usher™) and MicroStrategy Secure Cloud. The following table presents total revenues, gross profit, and long-lived assets, excluding long-term deferred tax assets, (in thousands) according to geographic region:

| <b>Geographic regions:</b>                   | <b>Domestic</b> | <b>EMEA</b> | <b>Other Regions</b> | <b>Consolidated</b> |
|----------------------------------------------|-----------------|-------------|----------------------|---------------------|
| <b>Three months ended September 30, 2015</b> |                 |             |                      |                     |
| Total revenues                               | \$ 77,837       | \$ 40,450   | \$ 11,249            | \$ 129,536          |
| Gross profit                                 | \$ 62,583       | \$ 32,802   | \$ 9,467             | \$ 104,852          |
| <b>Three months ended September 30, 2014</b> |                 |             |                      |                     |
| Total revenues                               | \$ 89,732       | \$ 44,296   | \$ 17,174            | \$ 151,202          |
| Gross profit                                 | \$ 68,677       | \$ 33,019   | \$ 14,553            | \$ 116,249          |
| <b>Nine months ended September 30, 2015</b>  |                 |             |                      |                     |
| Total revenues                               | \$ 242,775      | \$ 109,447  | \$ 34,125            | \$ 386,347          |
| Gross profit                                 | \$ 195,435      | \$ 84,637   | \$ 28,581            | \$ 308,653          |
| <b>Nine months ended September 30, 2014</b>  |                 |             |                      |                     |
| Total revenues                               | \$ 252,879      | \$ 131,366  | \$ 46,714            | \$ 430,959          |
| Gross profit                                 | \$ 191,681      | \$ 96,864   | \$ 38,839            | \$ 327,384          |
| <b>As of September 30, 2015</b>              |                 |             |                      |                     |
| Long-lived assets                            | \$ 82,260       | \$ 4,089    | \$ 2,504             | \$ 88,853           |
| <b>As of September 30, 2014</b>              |                 |             |                      |                     |
| Long-lived assets                            | \$ 83,322       | \$ 6,160    | \$ 5,169             | \$ 94,651           |

The domestic region consists of the United States and Canada. The EMEA region includes operations in Europe, the Middle East, and Africa. The other regions include all other foreign countries, generally comprising Latin America

and the Asia Pacific region. For the three and nine months ended September 30, 2015 and 2014, no individual foreign country accounted for 10% or more of total consolidated revenues.

For the three and nine months ended September 30, 2015 and 2014, no individual customer accounted for 10% or more of total consolidated revenues.

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**MICROSTRATEGY INCORPORATED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(unaudited)

As of September 30, 2015 and December 31, 2014, no individual foreign country accounted for 10% or more of total consolidated assets.

**(14) Subsequent Events**

As discussed in Note 11, Share-based Compensation, in October 2015, the Board of Directors authorized, subject to stockholder approval, an increase in the total number of shares of the Company's class A common stock authorized for issuance under the 2013 Equity Plan from 1,500,000 shares to 1,700,000 shares.

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

**FORWARD-LOOKING INFORMATION**

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). For this purpose, any statements contained herein that are not statements of historical fact, including without limitation, certain statements regarding industry prospects and our results of operations or financial position, may be deemed to be forward-looking statements. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects," and similar expressions are intended to identify forward-looking statements. The important factors discussed under Part II. Item 1A. Risk Factors, among others, could cause actual results to differ materially from those indicated by forward-looking statements made herein and presented elsewhere by management from time to time. Such forward-looking statements represent management's current expectations and are inherently uncertain. Investors are warned that actual results may differ from management's expectations.

**Overview**

MicroStrategy® is a leading worldwide provider of enterprise software platforms. MicroStrategy provides system-of-record reporting and interactive visualization capabilities offered on any device or in the cloud. The Company's mission is to provide enterprise software platforms that are flexible, powerful, scalable, and user-friendly.

MicroStrategy 10 Secure Enterprise consolidates analytics, mobility, and security in a single integrated platform, available both as on-premises software and hosted as a service offering in the MicroStrategy Secure Cloud. MicroStrategy's enterprise platform combines traditional business intelligence functionality with data discovery, mobile analytics, and powerful enterprise security. MicroStrategy 10 Secure Enterprise builds on proven enterprise capabilities to make sophisticated, high-performance analytics more accessible, easier to use, and faster. MicroStrategy 10 Secure Enterprise consists of MicroStrategy Analytics, MicroStrategy Mobile, and Usher.

MicroStrategy 10 Secure Enterprise empowers organizations to analyze vast amounts of data and securely distribute actionable business insight throughout an enterprise via two distinct end-user platforms, MicroStrategy Analytics and MicroStrategy Desktop. MicroStrategy Analytics, which is included as part of MicroStrategy 10 Secure Enterprise, delivers reports and dashboards, and enables users to conduct ad hoc analysis and share insights anywhere, anytime, via mobile devices or the Web. It also combines the agility and productivity of self-service visual data discovery with the security, scalability, and governance features of enterprise-grade business intelligence. MicroStrategy Analytics is available both as on-premises software and hosted as a service offering in the MicroStrategy Secure Cloud. MicroStrategy Desktop is a standalone, on-premise visual data discovery tool designed to enable business users to analyze and understand their data. With MicroStrategy Desktop, business users can create stunning data visualizations and dashboards that provide new insight and new understanding in just minutes.

MicroStrategy Mobile enables organizations to rapidly build custom business applications that deliver analytics combined with transactions, multimedia, and custom workflows to mobile devices. The powerful code-free platform approach is designed to reduce the costs of development and enable organizations to deploy powerful mobile business apps quickly and cost-effectively. MicroStrategy Mobile is an easy, fast, and cost-effective vehicle for mobilizing an organization's information systems, including its data warehouses, business intelligence, ERP, CRM, and Web applications that are currently accessible only on the desktop. With MicroStrategy Mobile, businesses can transform their entire workforce into a connected and more productive mobile workforce using information-driven mobile apps that are significantly more robust and secure than their Web-only counterparts. With mobile access to critical corporate data and systems that drive the business, employees can have a virtual office in their hands at all times.

MicroStrategy Mobile is available both as on-premises software and hosted as a service offering in the MicroStrategy Secure Cloud.

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Usher, MicroStrategy's security solution, is a powerful mobile security platform designed to dematerialize traditional forms of identity verification (such as passwords, tokens, and physical badges) and replace them with a single mobile identity badge that is cryptographically linked to its owner's smartphone and dynamically linked to an enterprise's existing identity repositories. Usher works on standard Android and iOS smartphones, and also boasts an Apple Watch integration. By delivering strong, multi-factor authentication that can be extended to nearly every corporate system, Usher's enterprise mobile security solution addresses some of the biggest challenges facing corporations today - including authentication, cybersecurity, identity and access management, and resource authorization - while applying industry leading business intelligence and analytics to an enterprise's security infrastructure. Through the use of Bluetooth®, QR codes, or time-limited PIN codes, Usher users can log into applications, unlock doors, and validate each other's identities. Usher can also be used as a powerful workforce management resource because it is designed to enable managers to gain a new real-time window into the activity of their distributed workforces, while providing powerful interactive features to manage or direct them. Usher is available as an on-premises software platform and also as a hosted service.

MicroStrategy Secure Cloud is a platform for organizations that want to harness the power of MicroStrategy's enterprise solutions via the cloud. Compared to traditional on-premises approaches, MicroStrategy Secure Cloud is architected to deliver best-of-breed MicroStrategy software via the cloud, with pre-configured, ready to go servers, coupled with the required supporting infrastructure with metadata databases, relational databases, and big data storage. With MicroStrategy Secure Cloud, customers can launch enterprise analytics environments within minutes and use our full MicroStrategy 10 Secure Enterprise offering on a subscription basis.

MicroStrategy Analytics, MicroStrategy Mobile, and MicroStrategy Secure Cloud together with related product and support services, continue to generate the vast majority of our revenue. During each of the three and nine months ended September 30, 2015 and 2014, we did not generate significant revenues from Usher.

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The following table sets forth certain operating highlights (in thousands) for the three and nine months ended September 30, 2015 and 2014:

|                                                  | <b>Three Months Ended<br/>September 30,</b> |                   | <b>Nine Months Ended<br/>September 30,</b> |                    |
|--------------------------------------------------|---------------------------------------------|-------------------|--------------------------------------------|--------------------|
|                                                  | <b>2015</b>                                 | <b>2014</b>       | <b>2015</b>                                | <b>2014</b>        |
| <b>Revenues</b>                                  |                                             |                   |                                            |                    |
| Product licenses                                 | \$ 27,511                                   | \$ 33,969         | \$ 77,634                                  | \$ 91,208          |
| Subscription services                            | 6,546                                       | 5,993             | 20,285                                     | 16,317             |
| Total product licenses and subscription services | 34,057                                      | 39,962            | 97,919                                     | 107,525            |
| Product support                                  | 71,392                                      | 75,019            | 211,444                                    | 221,069            |
| Other services                                   | 24,087                                      | 36,221            | 76,984                                     | 102,365            |
| <b>Total revenues</b>                            | <b>129,536</b>                              | <b>151,202</b>    | <b>386,347</b>                             | <b>430,959</b>     |
| <b>Cost of revenues</b>                          |                                             |                   |                                            |                    |
| Product licenses                                 | 2,680                                       | 1,542             | 5,895                                      | 5,456              |
| Subscription services                            | 3,075                                       | 4,502             | 9,800                                      | 13,829             |
| Total product licenses and subscription services | 5,755                                       | 6,044             | 15,695                                     | 19,285             |
| Product support                                  | 3,174                                       | 3,695             | 9,734                                      | 10,713             |
| Other services                                   | 15,755                                      | 25,214            | 52,265                                     | 73,577             |
| <b>Total cost of revenues</b>                    | <b>24,684</b>                               | <b>34,953</b>     | <b>77,694</b>                              | <b>103,575</b>     |
| <b>Gross profit</b>                              | <b>104,852</b>                              | <b>116,249</b>    | <b>308,653</b>                             | <b>327,384</b>     |
| <b>Operating expenses</b>                        |                                             |                   |                                            |                    |
| Sales and marketing                              | 36,403                                      | 58,195            | 109,142                                    | 178,028            |
| Research and development                         | 17,789                                      | 28,659            | 48,051                                     | 89,469             |
| General and administrative                       | 19,843                                      | 24,811            | 63,071                                     | 76,376             |
| Restructuring costs                              | 86                                          | 11,578            | 261                                        | 11,578             |
| <b>Total operating expenses</b>                  | <b>74,121</b>                               | <b>123,243</b>    | <b>220,525</b>                             | <b>355,451</b>     |
| <b>Income (loss) from operations</b>             | <b>\$ 30,731</b>                            | <b>\$ (6,994)</b> | <b>\$ 88,128</b>                           | <b>\$ (28,067)</b> |

The analytics market is highly competitive and our results of operations depend on our ability to market and sell offerings that provide customers with greater value than those offered by our competitors. Within the analytics market we compete with many different vendors, including (1) large software vendors (megavendors), such as IBM, SAP, Microsoft, and Oracle, that provide one or more products that directly compete with our products; (2) open source

analytics vendors such as TIBCO JasperSoft and Pentaho; (3) various other analytics software providers, such as Qlik, Tableau Software, Information Builders, and the SAS Institute; (4) pure-play mobile analytics vendors, such as MeLLmo (Roambi), that do not offer an analytics platform, but offer a mobile user interface that can be used as an extension to existing analytics platforms; and (5) other vendors offering cloud-based offerings, such as GoodData and Birst. Our success depends on the effectiveness with which we can differentiate our product from both the megavendors and other analytics vendors across large, mid-sized, and small opportunities.

Organizations recently have sought, and we expect may continue to seek, to standardize their various analytics applications around a single software platform. This trend presents both opportunities and challenges for our business. It offers us the opportunity to increase the size of transactions with new customers and to expand the size of our analytics installations with existing customers. On the other hand, it presents the challenge that we may not be able to penetrate accounts that a competitor has penetrated or in which a competitor is the incumbent analytics provider.

The market for mobile business apps is rapidly changing, highly competitive, and complex with many competitors and different offerings ranging from fully custom-coded applications to plug-and-play solutions. While organizations vary greatly in their approach to, and pace of adoption of, mobile solutions, they are increasingly accelerating the transition of their businesses onto mobile devices, such as tablets and smartphones. Over the next few years, we expect that organizations will continue to construct their information and systems to take advantage of the efficiencies and cost savings of mobile computing. Ultimately, we expect that the majority of routine business tasks and workflows will become available as mobile-optimized touch-enabled apps.

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In addition, there is increased market demand for analysis of a wider variety of data sources, including sensor data, social data, web log data, and other data types. These new data sources are driving massive increases in the volume of data that can potentially be analyzed ( Big Data ), which in turn is accelerating development of new storage technologies like Hadoop and NoSQL databases. The demand for analytics on Big Data represents an opportunity for MicroStrategy, as it opens up new potential applications and use cases for our technology. It also creates a challenge as we will need to continually enhance our technology to support emerging data sources; deliver faster performance necessary to support analysis against large scale data sets; and support analysis of a wider variety of data types, such as unstructured, semi-structured, and streaming data.

We have undertaken a number of initiatives to address these opportunities and challenges, including:

a major simplification of our product packaging structure aimed at delivering the best end-to-end customer and partner experience, making it easier to acquire and deploy the MicroStrategy platform, and delivering free upgrades to premium capabilities for existing customers, empowering customers to realize the full potential of their analytical applications;

release of MicroStrategy 10 Secure Enterprise, which consolidates analytics, mobility, and security in a single integrated platform;

improved access to MicroStrategy Analytics through MicroStrategy Secure Cloud, optimally configured to be scalable and elastic, ready to grow with an enterprise's cloud applications, and also built to scale to meet usage spikes from a user's analytics and mobile apps;

enhancement of our ability to support new enterprise-scale requirements for analytics, where we are currently a technology leader, with a focus on supporting more varied database platforms, providing higher performance, and providing greater ability to manage and administer large-scale analytics operations, such as a massively scalable, in-memory analytics service designed to deliver high performance for complex analytical applications that have the largest data sets and highest user concurrency;

extension of our technology to provide greater support for the latest trend in self-service analytics, which is often referred to as governed data discovery or agile analytics, by adding new user interface flows, new visualizations, new exploration features, and new self-service capabilities for the preparation of data;

enhancement of our mobile application platform for creating and deploying analytics applications to the expanding community of mobile device users; and

maintenance of a dedicated performance engineering team and conduct of research and development focused on providing our customers with the highest levels of performance for analytics applications of all sizes and for security solutions.

In the third quarter of 2014, we committed to a restructuring plan (the 2014 Restructuring Plan ) to streamline our workforce and spending to better align our cost structure with our business strategy. We implemented substantially all of this plan by the end of the fourth quarter of 2014. See Note 6, Restructuring, to the Consolidated Financial Statements for further detail on the 2014 Restructuring Plan. In addition to the 2014 Restructuring Plan, we have implemented other internal cost-savings initiatives. Our results of operations also reflect the impact of additional cost reductions resulting from employee turnover that has occurred outside of the 2014 Restructuring Plan. We expect the cost savings both related to and occurring outside of the 2014 Restructuring Plan will continue to result in decreases in our operating expenses in 2015 as compared to the same periods in 2014.

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As of September 30, 2015, we had a total of 1,939 employees, of whom 917 were based in the United States and 1,022 were based internationally. Of our 1,939 employees, 507 were engaged in sales and marketing, 464 in research and development, 667 in subscription, product support, consulting, and education services, and 301 in finance, administration, and corporate operations. The following table summarizes employee headcount, as of the dates indicated and reflects changes resulting from the 2014 Restructuring Plan as well as new hires and employee turnover outside of the 2014 Restructuring Plan:

|                            | <b>September 30,<br/>2014</b> | <b>December 31,<br/>2014</b> | <b>September 30,<br/>2015</b> |
|----------------------------|-------------------------------|------------------------------|-------------------------------|
| Subscription services      | 61                            | 57                           | 33                            |
| Product support            | 144                           | 138                          | 127                           |
| Consulting                 | 676                           | 600                          | 480                           |
| Education                  | 35                            | 24                           | 27                            |
| Sales and marketing        | 827                           | 662                          | 507                           |
| Research and development   | 965                           | 645                          | 464                           |
| General and administrative | 417                           | 344                          | 301                           |
| <b>Total headcount</b>     | <b>3,125</b>                  | <b>2,470</b>                 | <b>1,939</b>                  |

As of December 31, 2014, we were leasing approximately 233,000 square feet of office space at a location in Northern Virginia that began serving as our corporate headquarters in October 2010. Our lease for this property expires in 2020. We gave written notice in August 2014 of our intent to terminate the lease with respect to 19,000 square feet of this office space, effective February 2015, as part of the 2014 Restructuring Plan. We never used the terminated lease space and it remained vacant until it was terminated in February 2015. We recognized and paid all related lease termination costs associated with this terminated lease space during the third quarter of 2014. We recognize lease expense on continuing operating leases ratably over the term of the lease.

As discussed in Note 11, Share-based Compensation, to the Consolidated Financial Statements, we have outstanding stock options to purchase shares of our class A common stock under the 2013 Equity Plan. Share-based compensation expense (in thousands) from these stock option awards was recognized in the following operating expense line items in our Consolidated Statements of Operations for the periods indicated:

|                                               | <b>Three Months Ended<br/>September 30,<br/>2015      2014</b> |                 | <b>Nine Months<br/>Ended<br/>September 30,<br/>2015      2014</b> |                 |
|-----------------------------------------------|----------------------------------------------------------------|-----------------|-------------------------------------------------------------------|-----------------|
| Sales and marketing                           | \$ 808                                                         | \$ 200          | \$ 2,022                                                          | \$ 324          |
| Research and development                      | 359                                                            | 407             | 615                                                               | 1,025           |
| General and administrative                    | 3,379                                                          | 3,272           | 9,866                                                             | 7,212           |
| <b>Total share-based compensation expense</b> | <b>\$ 4,546</b>                                                | <b>\$ 3,879</b> | <b>\$ 12,503</b>                                                  | <b>\$ 8,561</b> |

As of September 30, 2015, we estimate that approximately \$54.5 million of additional share-based compensation expense for options granted under the 2013 Equity Plan will be recognized over a remaining weighted average period of 3.0 years.

We base our internal operating expense forecasts on expected revenue trends and strategic objectives. Many of our expenses, such as office leases and certain personnel costs, are relatively fixed. Accordingly, any shortfall in revenue may cause significant variation in our operating results. We therefore believe that quarter-to-quarter comparisons of our operating results may not be a good indication of our future performance.

**Table of Contents****Non-GAAP Financial Measures**

We are providing a supplemental financial measure for income (loss) from operations that excludes the impact of our share-based compensation arrangements and restructuring activities. This financial measure is not a measurement of financial performance under generally accepted accounting principles in the United States ( GAAP ) and, as a result, this financial measure may not be comparable to similarly titled measures of other companies. Management uses this non-GAAP financial measure internally to help understand, manage, and evaluate our business performance and to help make operating decisions. We believe that this non-GAAP financial measure is also useful to investors and analysts in comparing our performance across reporting periods on a consistent basis because it excludes a significant non-cash share-based compensation expense that we believe is not reflective of the Company's general business performance and significant restructuring charges that we believe are not reflective of ongoing operating results. In addition, accounting for share-based compensation arrangements requires significant management judgment and the resulting expense could vary significantly in comparison to other companies. Therefore, we believe the use of this non-GAAP financial measure can also facilitate comparison of our operating results to those of our competitors.

Non-GAAP financial measures are subject to material limitations as they are not in accordance with, or a substitute for, measurements prepared in accordance with GAAP. For example, we expect that share-based compensation expense, which is excluded from our non-GAAP financial measure, will continue to be a significant recurring expense over the coming years and is an important part of the compensation provided to certain employees, officers, and directors. Our non-GAAP financial measure is not meant to be considered in isolation and should be read only in conjunction with our Consolidated Financial Statements, which have been prepared in accordance with GAAP. We rely primarily on such Consolidated Financial Statements to understand, manage, and evaluate our business performance, and use the non-GAAP financial measure only supplementally.

The following is a reconciliation of our non-GAAP financial measure to its most directly comparable GAAP measure (in thousands) for the periods indicated:

|                                                                  | <b>Three Months<br/>Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|------------------------------------------------------------------|-------------------------------------------------|-------------|--------------------------------------------|-------------|
|                                                                  | <b>2015</b>                                     | <b>2014</b> | <b>2015</b>                                | <b>2014</b> |
| <b>Reconciliation of non-GAAP income (loss) from operations:</b> |                                                 |             |                                            |             |
| Income (loss) from operations                                    | \$ 30,731                                       | \$ (6,994)  | \$ 88,128                                  | \$ (28,067) |
| Share-based compensation expense                                 | 4,546                                           | 3,879       | 12,503                                     | 8,561       |
| Restructuring costs                                              | 86                                              | 11,578      | 261                                        | 11,578      |
| Non-GAAP income (loss) from operations                           | \$ 35,363                                       | \$ 8,463    | \$ 100,892                                 | \$ (7,928)  |

**Critical Accounting Policies**

Our discussion and analysis of our financial condition and results of operations are based upon our Consolidated Financial Statements, which have been prepared in accordance with GAAP.

The preparation of our Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, and equity and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates, particularly estimates relating to revenue recognition, allowance for doubtful accounts, valuation of property and equipment, accrued restructuring costs, litigation and contingencies, valuation of net deferred tax assets, share-based compensation, and fair value measurements of our derivative financial instruments have a material impact on our financial statements and are discussed in detail throughout our analysis of the results of operations discussed below. In some cases, changes in accounting estimates are reasonably likely to occur from period to period.

In addition to evaluating estimates relating to the items discussed above, we also consider other estimates and judgments, including, but not limited to, software development costs, provision for income taxes, and other contingent liabilities, including liabilities that we deem not probable of assertion. We base our estimates on historical experience and various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets, liabilities, and equity that are not readily apparent from other sources. Actual results and outcomes could differ from these estimates and assumptions.

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We do not have any material ownership interest in any special purpose or other entities that are not wholly-owned and/or consolidated into our Consolidated Financial Statements. Additionally, we do not have any material related party transactions.

The section **Critical Accounting Policies** included in Item 7 and the section **Summary of Significant Accounting Policies** (Note 2) included in Item 15 of our Annual Report on Form 10-K for the year ended December 31, 2014 provide a more detailed explanation of the judgments made in these areas and a discussion of our accounting estimates and policies. There have been no significant changes in such estimates and policies since December 31, 2014.

**Impact of Foreign Currency Exchange Rate Fluctuations on Results of Operations**

We conduct a significant portion of our business in currencies other than the U.S. dollar, the currency in which we report our Consolidated Financial Statements. As currency rates change from quarter over quarter and year over year, our results of operations may be impacted. The table below summarizes the impact (in thousands) of fluctuations in foreign currency exchange rates on certain components of our Consolidated Statements of Operations by showing the increase (decrease) in revenues or expenses, as applicable, from the same period in the prior year. The term **international** refers to operations outside of the United States and Canada.

|                                              | <b>Three Months Ended<br/>September 30,</b> |             | <b>Nine Months<br/>Ended<br/>September 30,</b> |             |
|----------------------------------------------|---------------------------------------------|-------------|------------------------------------------------|-------------|
|                                              | <b>2015</b>                                 | <b>2014</b> | <b>2015</b>                                    | <b>2014</b> |
| International product licenses revenues      | \$ (1,857)                                  | \$ (227)    | \$ (4,663)                                     | \$ (589)    |
| International subscription services revenues | (94)                                        | 28          | (314)                                          | 106         |
| International product support revenues       | (5,302)                                     | (239)       | (15,714)                                       | 56          |
| International other services revenues        | (1,826)                                     | (85)        | (5,911)                                        | 109         |
| Cost of product support revenues             | (168)                                       | 34          | (433)                                          | 87          |
| Cost of other services revenues              | (1,566)                                     | 21          | (5,265)                                        | 337         |
| Sales and marketing expenses                 | (2,462)                                     | (71)        | (6,987)                                        | 16          |
| Research and development expenses            | (69)                                        | 23          | (100)                                          | 323         |
| General and administrative expenses          | (584)                                       | (49)        | (1,897)                                        | (86)        |

For example, if there had been no change to foreign currency exchange rates from 2014 to 2015, international product licenses revenues would have been \$14.5 million rather than \$12.7 million and \$33.5 million rather than \$28.9 million for the three and nine months ended September 30, 2015, respectively. If there had been no change to foreign currency exchange rates from 2014 to 2015, international product support revenues would have been \$33.6 million rather than \$28.3 million and \$97.9 million rather than \$82.2 million for the three and nine months ended September 30, 2015, respectively. If there had been no change to foreign currency exchange rates from 2014 to 2015, sales and marketing expenses would have been \$38.9 million rather than \$36.4 million and \$116.1 million rather than \$109.1 million for the three and nine months ended September 30, 2015, respectively.

**Table of Contents****Results of Operations****Comparison of the three and nine months ended September 30, 2015 and 2014****Revenues**

Except as otherwise indicated herein, the term "domestic" refers to operations in the United States and Canada, and the term "international" refers to operations outside of the United States and Canada.

**Product licenses and subscription services revenues.** The following table sets forth product licenses and subscription services revenues (in thousands) and related percentage changes for the periods indicated:

|                                                           | Three Months Ended<br>September 30,<br>2015 |             |        | Nine Months Ended<br>September 30,<br>2015 |             |        |
|-----------------------------------------------------------|---------------------------------------------|-------------|--------|--------------------------------------------|-------------|--------|
|                                                           | 2014                                        | %<br>Change |        | 2014                                       | %<br>Change |        |
| Product Licenses and Subscription Services Revenues:      |                                             |             |        |                                            |             |        |
| Product Licenses                                          |                                             |             |        |                                            |             |        |
| Domestic                                                  | \$ 14,851                                   | \$ 18,534   | -19.9% | \$ 48,762                                  | \$ 49,411   | -1.3%  |
| International                                             | 12,660                                      | 15,435      | -18.0% | 28,872                                     | 41,797      | -30.9% |
| Total product licenses revenues                           | 27,511                                      | 33,969      | -19.0% | 77,634                                     | 91,208      | -14.9% |
| Subscription Services                                     |                                             |             |        |                                            |             |        |
| Domestic                                                  | 5,702                                       | 5,260       | 8.4%   | 17,946                                     | 14,191      | 26.5%  |
| International                                             | 844                                         | 733         | 15.1%  | 2,339                                      | 2,126       | 10.0%  |
| Total subscription services revenues                      | 6,546                                       | 5,993       | 9.2%   | 20,285                                     | 16,317      | 24.3%  |
| Total product licenses and subscription services revenues | \$ 34,057                                   | \$ 39,962   | -14.8% | \$ 97,919                                  | \$ 107,525  | -8.9%  |

The following table sets forth a summary, grouped by size, of the number of recognized product licenses transactions for the periods indicated:

|                                                                                          | Three Months Ended<br>September 30,<br>2015 |    | Nine Months Ended<br>September 30,<br>2015 |    |
|------------------------------------------------------------------------------------------|---------------------------------------------|----|--------------------------------------------|----|
|                                                                                          | 2014                                        |    | 2014                                       |    |
| Product Licenses Transactions with Recognized Licenses Revenue in the Applicable Period: |                                             |    |                                            |    |
| More than \$1.0 million in licenses revenue recognized                                   | 4                                           | 5  | 11                                         | 11 |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized                   | 8                                           | 8  | 20                                         | 20 |
| Total                                                                                    | 12                                          | 13 | 31                                         | 31 |

|                                                                        |   |   |    |    |
|------------------------------------------------------------------------|---|---|----|----|
| <i>Domestic:</i>                                                       |   |   |    |    |
| More than \$1.0 million in licenses revenue recognized                 | 2 | 3 | 9  | 9  |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 4 | 3 | 13 | 8  |
| Total                                                                  | 6 | 6 | 22 | 17 |
| <i>International:</i>                                                  |   |   |    |    |
| More than \$1.0 million in licenses revenue recognized                 | 2 | 2 | 2  | 2  |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 4 | 5 | 7  | 12 |
| Total                                                                  | 6 | 7 | 9  | 14 |

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The following table sets forth the recognized revenue (in thousands) attributable to product licenses transactions, grouped by size, and related percentage changes for the periods indicated:

|                                                                        | Three Months<br>Ended<br>September 30,<br>20152014 |           |        | %<br>Change | Nine Months<br>Ended<br>September 30,<br>20152014 |        |  | %<br>Change |
|------------------------------------------------------------------------|----------------------------------------------------|-----------|--------|-------------|---------------------------------------------------|--------|--|-------------|
| Product Licenses Revenue Recognized in the Applicable Period:          |                                                    |           |        |             |                                                   |        |  |             |
| More than \$1.0 million in licenses revenue recognized                 | \$ 6,053                                           | \$ 7,130  | -15.1% | \$ 18,238   | \$ 16,567                                         | 10.1%  |  |             |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 5,856                                              | 5,541     | 5.7%   | 14,454      | 13,146                                            | 9.9%   |  |             |
| Less than \$0.5 million in licenses revenue recognized                 | 15,602                                             | 21,298    | -26.7% | 44,942      | 61,495                                            | -26.9% |  |             |
| Total                                                                  | 27,511                                             | 33,969    | -19.0% | 77,634      | 91,208                                            | -14.9% |  |             |
| Domestic:                                                              |                                                    |           |        |             |                                                   |        |  |             |
| More than \$1.0 million in licenses revenue recognized                 | 2,648                                              | 4,024     | -34.2% | 14,833      | 13,461                                            | 10.2%  |  |             |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 3,030                                              | 1,919     | 57.9%  | 9,718       | 5,349                                             | 81.7%  |  |             |
| Less than \$0.5 million in licenses revenue recognized                 | 9,173                                              | 12,591    | -27.1% | 24,211      | 30,601                                            | -20.9% |  |             |
| Total                                                                  | 14,851                                             | 18,534    | -19.9% | 48,762      | 49,411                                            | -1.3%  |  |             |
| International:                                                         |                                                    |           |        |             |                                                   |        |  |             |
| More than \$1.0 million in licenses revenue recognized                 | 3,405                                              | 3,106     | 9.6%   | 3,405       | 3,106                                             | 9.6%   |  |             |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 2,826                                              | 3,622     | -22.0% | 4,736       | 7,797                                             | -39.3% |  |             |
| Less than \$0.5 million in licenses revenue recognized                 | 6,429                                              | 8,707     | -26.2% | 20,731      | 30,894                                            | -32.9% |  |             |
| Total                                                                  | \$ 12,660                                          | \$ 15,435 | -18.0% | \$ 28,872   | \$ 41,797                                         | -30.9% |  |             |

Product licenses revenues decreased \$6.5 million and \$13.6 million for the three and nine months ended September 30, 2015, respectively, as compared to the same periods in the prior year. For the three months ended September 30, 2015 and 2014, product licenses transactions with more than \$0.5 million in recognized revenue represented 43.3% and 37.3%, respectively, of our product licenses revenues. For the nine months ended September 30, 2015, our top three product licenses transactions totaled \$6.5 million in recognized revenue, or 8.4% of total product licenses revenues, compared to \$6.2 million, or 6.8% of total product licenses revenues, for the nine months ended September 30, 2014.

**Domestic product licenses revenues.** Domestic product licenses revenues decreased \$3.7 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a decrease in the number of transactions with less than \$0.5 million in recognized revenue and a decrease in the number and average deal size of transactions with more than \$1.0 million in recognized revenue, partially offset by an increase in the number and average deal size of transactions with recognized revenue between \$0.5 million and \$1.0 million.

Domestic product licenses revenues decreased \$0.6 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a decrease in the number of transactions with less than \$0.5 million in recognized revenue, partially offset by an increase in the number and average deal size of transactions

with recognized revenue between \$0.5 million and \$1.0 million and an increase in the average deal size of transactions with more than \$1.0 million in recognized revenue.

***International product licenses revenues.*** International product licenses revenues decreased \$2.8 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a decrease in the average deal size of transactions with less than \$0.5 million in recognized revenue and a decrease in the number and average deal size of transactions with recognized revenue between \$0.5 million and \$1.0 million, partially offset by an increase in the average deal size of transactions with more than \$1.0 million in recognized revenue.

International product licenses revenues decreased \$12.9 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a decrease in the number and average deal size of transactions with less than \$0.5 million in recognized revenue and a decrease in the number of transactions with recognized revenue between \$0.5 million and \$1.0 million, partially offset by an increase in the average deal size of transactions with more than \$1.0 million in recognized revenue.

***Subscription services revenues.*** Subscription services revenues are derived primarily from our cloud services offerings that are recognized on a subscription basis over the service period of the contract.

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Subscription services revenues increased \$0.6 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to an increase in the number of new subscription services customers and an increase in the use of subscription services by existing customers. Subscription services revenues increased \$4.0 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to an increase in the number of new subscription services customers and an increase in the use of subscription services by existing customers, partially offset by the recognition of \$1.0 million in previously deferred revenue for one large customer in the same period of the prior year.

**Product support revenues.** The following table sets forth product support revenues (in thousands) and related percentage changes for the periods indicated:

|                                | Three Months<br>Ended<br>September 30,<br>2015 |           |             | Nine Months Ended<br>September 30,<br>2015 |            |             |
|--------------------------------|------------------------------------------------|-----------|-------------|--------------------------------------------|------------|-------------|
|                                | 2015                                           | 2014      | %<br>Change | 2015                                       | 2014       | %<br>Change |
| Product Support Revenues:      |                                                |           |             |                                            |            |             |
| Domestic                       | \$ 43,071                                      | \$ 43,364 | -0.7%       | \$ 129,225                                 | \$ 127,743 | 1.2%        |
| International                  | 28,321                                         | 31,655    | -10.5%      | 82,219                                     | 93,326     | -11.9%      |
| Total product support revenues | \$ 71,392                                      | \$ 75,019 | -4.8%       | \$ 211,444                                 | \$ 221,069 | -4.4%       |

Product support revenues are derived from providing technical software support and software updates and upgrades to customers. Product support revenues are recognized ratably over the term of the contract, which is generally one year. Product support revenues decreased \$3.6 million and \$9.6 million for the three and nine months ended September 30, 2015, respectively, as compared to the same periods in the prior year, primarily due to \$5.3 million and \$15.7 million negative foreign exchange impacts, respectively, partially offset by new product and premium support contracts. See **Impact of Foreign Currency Exchange Rate Fluctuations on Results of Operations** for further information on the negative foreign exchange impact on our results of operations for the three and nine months ended September 30, 2015.

**Other services revenues.** The following table sets forth other services revenues (in thousands) and related percentage changes in these revenues for the periods indicated:

|                           | Three Months<br>Ended<br>September 30,<br>2015 |           |             | Nine Months Ended<br>September 30,<br>2015 |           |             |
|---------------------------|------------------------------------------------|-----------|-------------|--------------------------------------------|-----------|-------------|
|                           | 2015                                           | 2014      | %<br>Change | 2015                                       | 2014      | %<br>Change |
| Other Services Revenues:  |                                                |           |             |                                            |           |             |
| Consulting                |                                                |           |             |                                            |           |             |
| Domestic                  | \$ 12,826                                      | \$ 20,391 | -37.1%      | \$ 42,248                                  | \$ 54,660 | -22.7%      |
| International             | 9,192                                          | 12,421    | -26.0%      | 28,227                                     | 36,850    | -23.4%      |
| Total consulting revenues | 22,018                                         | 32,812    | -32.9%      | 70,475                                     | 91,510    | -23.0%      |

|                               |           |           |        |           |            |        |
|-------------------------------|-----------|-----------|--------|-----------|------------|--------|
| Education                     | 2,069     | 3,409     | -39.3% | 6,509     | 10,855     | -40.0% |
| Total other services revenues | \$ 24,087 | \$ 36,221 | -33.5% | \$ 76,984 | \$ 102,365 | -24.8% |

**Consulting revenues.** Consulting revenues are derived from helping customers plan and execute the deployment of our software. Consulting revenues decreased for the three and nine months ended September 30, 2015, as compared to the same periods in the prior year, primarily due to a decrease in billable hours worldwide, partially offset by an increase in the average bill rate.

**Education revenues.** Education revenues are derived from the education and training that we provide to our customers to enhance their ability to fully utilize the features and functionality of our software. These offerings include self-tutorials, custom course development, joint training with customers' internal staff, and standard course offerings, with pricing dependent on the specific offering delivered. Education revenues decreased for the three and nine months ended September 30, 2015, as compared to the same periods in the prior year, primarily due to lower overall contract values and a decrease in onsite and online course delivery.

**Table of Contents****Costs and Expenses**

**Cost of revenues.** The following table sets forth cost of revenues (in thousands) and related percentage changes for the periods indicated:

|                                                  | Three Months<br>Ended<br>September 30 |           |             | Nine Months Ended<br>September 30 |            |             |
|--------------------------------------------------|---------------------------------------|-----------|-------------|-----------------------------------|------------|-------------|
|                                                  | 2015                                  | 2014      | %<br>Change | 2015                              | 2014       | %<br>Change |
| <b>Cost of Revenues:</b>                         |                                       |           |             |                                   |            |             |
| Product licenses and subscription services:      |                                       |           |             |                                   |            |             |
| Product licenses                                 | \$ 2,680                              | \$ 1,542  | 73.8%       | \$ 5,895                          | \$ 5,456   | 8.0%        |
| Subscription services                            | 3,075                                 | 4,502     | -31.7%      | 9,800                             | 13,829     | -29.1%      |
| Total product licenses and subscription services | 5,755                                 | 6,044     | -4.8%       | 15,695                            | 19,285     | -18.6%      |
| Product support                                  | 3,174                                 | 3,695     | -14.1%      | 9,734                             | 10,713     | -9.1%       |
| Other services:                                  |                                       |           |             |                                   |            |             |
| Consulting                                       | 14,723                                | 23,841    | -38.2%      | 49,526                            | 68,830     | -28.0%      |
| Education                                        | 1,032                                 | 1,373     | -24.8%      | 2,739                             | 4,747      | -42.3%      |
| Total other services                             | 15,755                                | 25,214    | -37.5%      | 52,265                            | 73,577     | -29.0%      |
| Total cost of revenues                           | \$ 24,684                             | \$ 34,953 | -29.4%      | \$ 77,694                         | \$ 103,575 | -25.0%      |

**Cost of product licenses revenues.** Cost of product licenses revenues consists of amortization of capitalized software development costs, referral fees paid to channel partners, the costs of product manuals and media, and royalties paid to third-party software vendors. Capitalized software development costs are generally amortized over a useful life of three years.

Cost of product licenses revenues increased \$1.1 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$1.5 million increase in amortization of capitalized software development costs related to MicroStrategy 10 Secure Enterprise, which was made generally available in June 2015, partially offset by a \$0.2 million decrease in referral fees related to channel partners. Cost of product licenses revenues increased \$0.4 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$2.0 million increase in amortization of capitalized software development costs related to MicroStrategy 10 Secure Enterprise, which was made generally available in June 2015, partially offset by a \$0.8 million decrease in referral fees related to channel partners, a \$0.4 million decrease in amortization of capitalized software development costs related to MicroStrategy 9.2.1, which became fully amortized in June 2014, and a \$0.3 million decrease in amortization of capitalized software development costs related to MicroStrategy 9.2, which became fully amortized in March 2014. We expect to amortize the remaining balance of our products' capitalized software development costs as of September 30, 2015 ratably over the applicable remaining amortization periods as follows:

**Capitalized Software  
Development Costs, Net, Remaining  
as of September 30, 2015 Amortization Period**

**(in thousands)                      (in months)**

|                                                     |                  |    |
|-----------------------------------------------------|------------------|----|
| MicroStrategy 9.4                                   | \$ 1,812         | 12 |
| MicroStrategy 10 Secure Enterprise                  | 15,995           | 32 |
| <b>Total capitalized software development costs</b> | <b>\$ 17,807</b> |    |

All of the above software form part of MicroStrategy 10 Secure Enterprise.

**Cost of subscription services revenues.** Cost of subscription services revenues consists of equipment, facility and other related support costs, and personnel and related overhead costs. Cost of subscription services revenues decreased \$1.4 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$0.8 million decrease in compensation and related costs due to a decrease in staffing levels, a \$0.7 million decrease in equipment, facility, and other related support costs, which included a \$0.4 million decrease related to certain reclassifications of depreciation costs to research and development expenses, and a \$0.1 million decrease in consulting and advisory costs, partially offset by a \$0.1 million increase in third-party hosting service provider fees. Subscription services headcount decreased 45.9% to 33 at September 30, 2015 from 61 at September 30, 2014.

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Cost of subscription services revenues decreased \$4.0 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, due to a \$2.6 million decrease in equipment, facility, and other related support costs, which included a \$1.4 million decrease related to certain reclassifications of depreciation costs to research and development expenses, a \$0.7 million decrease in consulting and advisory costs, a \$0.7 million decrease in compensation and related costs due to a decrease in staffing levels, and a \$0.2 million decrease in recruiting costs, partially offset by a \$0.2 million increase in third-party hosting service provider fees.

**Cost of product support revenues.** Cost of product support revenues consists of product support personnel and related overhead costs. Cost of product support revenues decreased \$0.5 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$0.4 million decrease in compensation and related costs due to a decrease in staffing levels. Product support headcount decreased 11.8% to 127 at September 30, 2015 from 144 at September 30, 2014.

Cost of product support revenues decreased \$1.0 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, due to a \$1.0 million decrease in compensation and related costs due to a decrease in staffing levels and a \$0.1 million decrease in travel and entertainment expenditures, partially offset by a \$0.1 million increase in facility and other related support costs.

**Cost of consulting revenues.** Cost of consulting revenues consists of personnel and related overhead costs. Cost of consulting revenues decreased \$9.1 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$4.1 million decrease in compensation and related costs due to a decrease in staffing levels, a \$2.7 million decrease in subcontractor costs, a \$1.6 million decrease in travel and entertainment expenditures, a \$0.7 million decrease in facility and other related support costs, and a \$0.1 million decrease in recruiting costs. Consulting headcount decreased 29.0% to 480 at September 30, 2015 from 676 at September 30, 2014.

Cost of consulting revenues decreased \$19.3 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$9.2 million decrease in compensation and related costs due to a decrease in staffing levels, a \$4.0 million decrease in travel and entertainment expenditures, a \$4.0 million decrease in subcontractor costs, a \$1.7 million decrease in facility and other related support costs, and a \$0.3 million decrease in recruiting costs.

**Cost of education revenues.** Cost of education revenues consists of personnel and related overhead costs. Cost of education revenues decreased \$0.3 million for the three months ended September 30, 2015, as compared to the same period in the prior year, due to a \$0.1 million decrease in subcontractor costs, a \$0.1 million decrease in travel and entertainment expenditures, and a \$0.1 million decrease in facility and other related support costs. Education headcount decreased 22.9% to 27 at September 30, 2015 from 35 at September 30, 2014.

Cost of education revenues decreased \$2.0 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$0.8 million decrease in compensation and related costs due to a decrease in staffing levels, a \$0.4 million decrease in travel and entertainment expenditures, a \$0.4 million decrease in subcontractor costs, and a \$0.3 million decrease in facility and other related support costs.

**Sales and marketing expenses.** Sales and marketing expenses consists of personnel costs, commissions, office facilities, travel, advertising, public relations programs, and promotional events, such as trade shows, seminars, and technical conferences. The following table sets forth sales and marketing expenses (in thousands) and related percentage changes for the periods indicated:

|                              | Three Months<br>Ended<br>September 30,<br>2015      2014 |           |             | Nine Months Ended<br>September 30,<br>2015      2014 |            |             |
|------------------------------|----------------------------------------------------------|-----------|-------------|------------------------------------------------------|------------|-------------|
|                              |                                                          |           | %<br>Change |                                                      |            | %<br>Change |
| Sales and marketing expenses | \$ 36,403                                                | \$ 58,195 | -37.4%      | \$ 109,142                                           | \$ 178,028 | -38.7%      |

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Sales and marketing expenses decreased \$21.8 million for the three months ended September 30, 2015, as compared to the same period in the prior year, due to a \$14.6 million decrease in compensation and related costs due to a decrease in staffing levels, a \$3.0 million decrease in marketing and advertising costs, a \$1.9 million decrease in travel and entertainment expenditures, a \$1.6 million decrease in facility and other related support costs, a \$0.7 million decrease in recruiting costs, and a \$0.6 million decrease in consulting and advisory costs, partially offset by a \$0.6 million increase in share-based compensation expense related to the grant of stock options under the 2013 Equity Plan. Sales and marketing headcount decreased 38.7% to 507 at September 30, 2015 from 827 at September 30, 2014.

As a result of stock options granted under the 2013 Equity Plan, we expect that share-based compensation expense, a portion of which is recognized as sales and marketing expense, will continue to be a recurring expense. As of September 30, 2015, we estimate that approximately \$13.0 million of additional share-based compensation expense will be recognized as sales and marketing expense over a remaining weighted average period of 3.4 years. See

Overview and Note 11, Share-based Compensation, to the Consolidated Financial Statements for further information regarding the 2013 Equity Plan and related share-based compensation expense.

Sales and marketing expenses decreased \$68.9 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$46.3 million decrease in compensation and related costs due to a decrease in staffing levels, a \$9.2 million decrease in marketing and advertising costs, a \$7.5 million decrease in travel and entertainment expenditures, a \$3.5 million decrease in facility and other related support costs, a \$2.2 million decrease in recruiting costs, and a \$1.7 million decrease in consulting and advisory costs, partially offset by a \$1.7 million increase in share-based compensation expense related to the grant of stock options under the 2013 Equity Plan.

**General and administrative expenses.** General and administrative expenses consists of personnel and related overhead costs, and other costs of our executive, finance, human resources, information systems, and administrative departments, as well as third-party consulting, legal, and other professional fees. The following table sets forth general and administrative expenses (in thousands) and related percentage changes for the periods indicated:

|                                     | Three Months<br>Ended<br>September 30, |           |             | Nine Months<br>Ended<br>September 30, |           |             |
|-------------------------------------|----------------------------------------|-----------|-------------|---------------------------------------|-----------|-------------|
|                                     | 2015                                   | 2014      | %<br>Change | 2015                                  | 2014      | %<br>Change |
| General and administrative expenses | \$ 19,843                              | \$ 24,811 | -20.0%      | \$ 63,071                             | \$ 76,376 | -17.4%      |

General and administrative expenses decreased \$5.0 million for the three months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$2.9 million decrease in compensation and related costs due to a decrease in staffing levels, a \$1.1 million decrease in legal, consulting, and other advisory costs, a \$0.7 million decrease in facility and other related support costs, a \$0.3 million decrease in travel and entertainment expenditures, a \$0.1 million decrease in other aircraft-related operating costs, and a \$0.1 million decrease in recruiting costs, partially offset by a \$0.2 million increase in bad debt expense and a \$0.1 million increase in share-based compensation expense related to the grant of stock options under the 2013 Equity Plan. General and administrative headcount decreased 27.8% to 301 at September 30, 2015 from 417 at September 30, 2014. Having substantially implemented the 2014 Restructuring Plan, we do not expect to increase general and administrative headcount significantly in the near term.



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As a result of stock options granted under the 2013 Equity Plan, we expect that share-based compensation expense, a significant portion of which is recognized as general and administrative expense, will continue to be a significant recurring expense. As of September 30, 2015, we estimate that approximately \$34.8 million of additional share-based compensation expense will be recognized as general and administrative expense over a remaining weighted average period of 2.7 years. See Overview and Note 11, Share-based Compensation, to the Consolidated Financial Statements for further information regarding the 2013 Equity Plan and related share-based compensation expense.

General and administrative expenses decreased \$13.3 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$9.2 million decrease in compensation and related costs due to a decrease in staffing levels, a \$2.2 million decrease in legal, consulting, and other advisory costs, a \$1.9 million decrease in facility and other related support costs, a \$1.1 million decrease in travel and entertainment expenditures, a \$0.8 million decrease in other aircraft-related operating costs, and a \$0.5 million decrease in recruiting costs, partially offset by a \$2.7 million increase in share-based compensation expense related to the grant of stock options under the 2013 Equity Plan.

**Research and development expenses.** Research and development expenses consists of the personnel costs for our software engineering personnel, depreciation of equipment, and other related costs. The following table summarizes research and development expenses and amortization of capitalized software development costs (in thousands) and related percentage changes for the periods indicated:

|                                                                                                      | Three Months<br>Ended<br>September 30,<br>2015      2014 |           |  | %<br>Change | Nine Months<br>Ended<br>September 30,<br>2015      2014 |           |  | %<br>Change |
|------------------------------------------------------------------------------------------------------|----------------------------------------------------------|-----------|--|-------------|---------------------------------------------------------|-----------|--|-------------|
| Gross research and development expenses before capitalized software development costs                | \$ 17,789                                                | \$ 30,913 |  | -42.5%      | \$ 57,649                                               | \$ 91,723 |  | -37.1%      |
| Capitalized software development costs                                                               | 0                                                        | (2,254)   |  | -100.0%     | (9,598)                                                 | (2,254)   |  | 325.8%      |
| Total research and development expenses                                                              | \$ 17,789                                                | \$ 28,659 |  | -37.9%      | \$ 48,051                                               | \$ 89,469 |  | -46.3%      |
| Amortization of capitalized software development costs included in cost of product licenses revenues | \$ 2,496                                                 | \$ 1,171  |  | 113.2%      | \$ 5,260                                                | \$ 4,090  |  | 28.6%       |

Research and development expenses, before capitalization of software development costs, decreased \$13.1 million for the three months ended September 30, 2015, as compared to the same period in the prior year, due to a \$10.7 million decrease in compensation and related costs due to a decrease in staffing levels, a \$1.5 million decrease in facility and other related support costs, a \$0.9 million decrease in consulting and advisory costs, and a \$0.3 million decrease in travel and entertainment expenditures, partially offset by a \$0.3 million increase in recruiting costs. Research and development headcount decreased 51.9% to 464 at September 30, 2015 from 965 at September 30, 2014.

As a result of stock options granted under the 2013 Equity Plan, we expect that share-based compensation expense, a portion of which is recognized as research and development expense, will continue to be a recurring expense. As of September 30, 2015, we estimate that approximately \$6.7 million of additional share-based compensation expense

will be recognized as research and development expense over a remaining weighted average period of 3.6 years. See Overview and Note 11, Share-based Compensation, to the Consolidated Financial Statements for further information regarding the 2013 Equity Plan and related share-based compensation expense.

Research and development expenses, before capitalization of software development costs, decreased \$34.1 million for the nine months ended September 30, 2015, as compared to the same period in the prior year, primarily due to a \$26.1 million decrease in compensation and related costs due to a decrease in staffing levels, a \$3.6 million decrease in facility and other related support costs, a \$2.0 million decrease in consulting and advisory costs, a \$1.0 million decrease in recruiting costs, a \$0.8 million decrease in travel and entertainment expenditures, and a \$0.4 million decrease in share-based compensation expense related to the pre-vesting forfeitures of certain stock options under the 2013 Equity Plan.

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**Restructuring costs.** In the third quarter of 2014, we adopted the 2014 Restructuring Plan, which included a workforce reduction of 777 employees. Restructuring costs consisted primarily of employee severance and related benefit costs, contract termination costs, and other related costs associated with our restructuring activities. As of December 31, 2014, we had implemented substantially all of the 2014 Restructuring Plan. No material restructuring costs were incurred during the three and nine months ended September 30, 2015. The following table summarizes restructuring costs (in thousands) and related percentage changes for the periods indicated:

|                     | Three Months Ended<br>September 30, |           |             | Nine Months Ended<br>September 30, |           |             |
|---------------------|-------------------------------------|-----------|-------------|------------------------------------|-----------|-------------|
|                     | 2015                                | 2014      | %<br>Change | 2015                               | 2014      | %<br>Change |
| Restructuring costs | \$ 86                               | \$ 11,578 | -99.3%      | \$ 261                             | \$ 11,578 | -97.7%      |

We do not expect future costs associated with implementing the remainder of the 2014 Restructuring Plan, consisting primarily of the liquidation of certain foreign subsidiaries, to be material. See Note 6, Restructuring, to the Consolidated Financial Statements for further information regarding the 2014 Restructuring Plan and related restructuring costs by major cost category.

**Other Income, Net**

Other income, net is comprised primarily of realized and unrealized gains and losses on our foreign currency forward contracts and foreign currency transaction gains and losses. For the three months ended September 30, 2015, other income, net, of \$0.8 million was comprised primarily of \$0.4 million in foreign currency transaction net gains, arising mainly from the revaluation of U.S. dollar denominated cash balances held at international locations and a \$0.3 million foreign currency translation gain reclassified from other comprehensive income that resulted from the completion of the liquidation of one of our foreign subsidiaries as part of the 2014 Restructuring Plan. For the nine months ended September 30, 2015, other income, net, of \$2.6 million was comprised primarily of \$1.4 million in foreign currency transaction net gains, arising mainly from the revaluation of U.S. dollar denominated cash balances held at international locations, \$0.5 million in net realized and unrealized gains from the settlement of certain foreign currency forward contracts, and a \$0.3 million foreign currency translation gain reclassified from other comprehensive income that resulted from the completion of the liquidation of one of our foreign subsidiaries as part of the 2014 Restructuring Plan.

**Provision for (Benefit from) Income Taxes**

We have estimated an annual effective tax rate for the full fiscal year 2015 and applied that rate to the income before income taxes in determining the provision for income taxes for the nine months ended September 30, 2015. We also record discrete items in each respective period as appropriate. The estimated effective tax rate is subject to fluctuation based upon the level and mix of earnings and losses by tax jurisdiction, foreign tax rate differentials, and the relative impact of permanent book to tax differences (e.g., non-deductible expenses). Each quarter, a cumulative adjustment is recorded for any fluctuations in the estimated annual effective tax rate as compared to the prior quarter. As a result of these factors, and due to potential changes in our period to period results, fluctuations in our effective tax rate and respective tax provisions or benefits may occur.

For the nine months ended September 30, 2015, we recorded a provision for income taxes of \$24.0 million that resulted in an effective tax rate of 26.5%, as compared to a benefit from income taxes of \$6.9 million that resulted in an effective tax rate of 28.2% for the nine months ended September 30, 2014. The change in the effective tax rate in

2015 is mainly due to changes in the forecasted overall income or loss amounts for 2015, a change in the expected proportion of U.S. versus foreign income, and changes in discrete tax benefits.

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As of September 30, 2015, we estimated that we had no U.S. federal net operating loss carryforwards and \$1.2 million of foreign net operating loss carryforwards. As of September 30, 2015, we estimated that we had foreign net operating loss carryforwards, other temporary differences and carryforwards, and credits that resulted in deferred tax assets, net of valuation allowances and deferred tax liabilities, of \$6.4 million. As of September 30, 2015, we had a valuation allowance of \$2.1 million primarily related to certain foreign tax credit carryforwards and foreign net operating loss carryforwards that, in our present estimation, more likely than not will not be realized.

If we are unable to sustain profitability in future periods, we may be required to increase the valuation allowance against our deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred. We will continue to regularly assess the realizability of deferred tax assets.

**Deferred Revenue and Advance Payments**

Deferred revenue and advance payments represent subscription services, product support, and other services fees that are collected in advance and recognized over the contract service period and product licenses revenues relating to multiple-element software arrangements that include future deliverables.

The following table summarizes deferred revenue and advance payments (in thousands), as of:

|                                                         | September 30,<br>2015 | December 31,<br>2014 | September 30,<br>2014 |
|---------------------------------------------------------|-----------------------|----------------------|-----------------------|
| <b>Current:</b>                                         |                       |                      |                       |
| Deferred product licenses revenue                       | \$ 13,155             | \$ 10,927            | \$ 10,010             |
| Deferred subscription services revenue                  | 11,172                | 16,018               | 10,382                |
| Deferred product support revenue                        | 135,999               | 168,833              | 145,917               |
| Deferred other services revenue                         | 6,794                 | 10,564               | 10,216                |
| Gross current deferred revenue and advance payments     | 167,120               | 206,342              | 176,525               |
| Less: unpaid deferred revenue                           | (51,616)              | (97,929)             | (55,818)              |
| Net current deferred revenue and advance payments       | \$ 115,504            | \$ 108,413           | \$ 120,707            |
| <b>Non-current:</b>                                     |                       |                      |                       |
| Deferred product licenses revenue                       | \$ 6,344              | \$ 8,012             | \$ 7,700              |
| Deferred subscription services revenue                  | 808                   | 750                  | 669                   |
| Deferred product support revenue                        | 6,962                 | 7,505                | 7,062                 |
| Deferred other services revenue                         | 1,166                 | 1,047                | 951                   |
| Gross non-current deferred revenue and advance payments | 15,280                | 17,314               | 16,382                |
| Less: unpaid deferred revenue                           | (4,983)               | (6,496)              | (4,903)               |
| Net non-current deferred revenue and advance payments   | \$ 10,297             | \$ 10,818            | \$ 11,479             |
| <b>Total current and non-current:</b>                   |                       |                      |                       |
| Deferred product licenses revenue                       | \$ 19,499             | \$ 18,939            | \$ 17,710             |

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|                                                                     |            |            |            |
|---------------------------------------------------------------------|------------|------------|------------|
| Deferred subscription services revenue                              | 11,980     | 16,768     | 11,051     |
| Deferred product support revenue                                    | 142,961    | 176,338    | 152,979    |
| Deferred other services revenue                                     | 7,960      | 11,611     | 11,167     |
| Gross current and non-current deferred revenue and advance payments | 182,400    | 223,656    | 192,907    |
| Less: unpaid deferred revenue                                       | (56,599)   | (104,425)  | (60,721)   |
| Net current and non-current deferred revenue and advance payments   | \$ 125,801 | \$ 119,231 | \$ 132,186 |

We offset our accounts receivable and deferred revenue for any unpaid items included in deferred revenue and advance payments.

Total gross deferred revenue and advance payments decreased \$41.3 million as of September 30, 2015, as compared to December 31, 2014, primarily due to the recognition of previously deferred subscription services, product support, and other services revenues and a strengthening of the U.S. dollar, partially offset by an increase in deferred revenue from new product licenses contracts. Total gross deferred revenue and advance payments decreased \$10.5 million as of September 30, 2015, as compared to September 30, 2014, primarily due to a strengthening of the U.S. dollar and the recognition of previously deferred product support and other services revenues, partially offset by an increase in deferred revenue from new product licenses and subscription services contracts.

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We expect to recognize approximately \$167.1 million of deferred revenue and advance payments over the next 12 months. However, the timing and ultimate recognition of our deferred revenue and advance payments depend on our performance of various service obligations, and the amount of deferred revenue and advance payments at any date should not be considered indicative of revenues for any succeeding period.

As of September 30, 2015, we had entered into certain additional agreements that include future minimum commitments by our customers to purchase products, subscription services, product support, or other services through 2020 totaling approximately \$138.4 million. Revenue relating to such future commitments by our customers is not included in our deferred revenue balances. Revenue relating to such agreements will be recognized during the period in which all revenue recognition criteria are met. The timing and ultimate recognition of any revenue from such customer purchase commitments depend on our customers' meeting their future purchase commitments and our meeting our associated performance obligations related to those purchase commitments.

## **Liquidity and Capital Resources**

**Liquidity.** Our principal sources of liquidity are cash and cash equivalents and on-going collection of our accounts receivable. Cash and cash equivalents include holdings in bank demand deposits, money market instruments, and U.S. Treasury securities. We also periodically invest a portion of our excess cash in short-term investments with stated maturity dates between three months and one year from the purchase date.

As of September 30, 2015, total accrued restructuring costs were \$0.1 million and are expected to be paid in the next 12 months. We do not expect future costs associated with implementing the remainder of the 2014 Restructuring Plan, consisting primarily of the liquidation of certain foreign subsidiaries, to be material. In addition to the 2014 Restructuring Plan, we have implemented other internal cost-saving initiatives. Our results of operations also reflect the impact of additional cost reductions resulting from employee turnover that has occurred outside of the 2014 Restructuring Plan. We expect the cost savings both related to and occurring outside of the 2014 Restructuring Plan will continue to result in decreases in our operating expenses in 2015 as compared to the same periods in 2014.

As of September 30, 2015 and December 31, 2014, the amount of cash and cash equivalents and short-term investments held by U.S. entities were \$196.4 million and \$139.1 million, respectively, and by non-U.S. entities were \$260.5 million and \$206.4 million, respectively. We earn a significant amount of our revenues outside the U.S. and, except for Subpart F deemed dividends, we intend to indefinitely reinvest undistributed earnings of all of our non-U.S. entities. We do not anticipate needing to repatriate the cash or cash equivalents held by non-U.S. entities to the U.S. to finance our U.S. operations. However, if we were to elect to repatriate these amounts, we would generate U.S. taxable income to the extent of our undistributed foreign earnings, which amounted to \$201.7 million at December 31, 2014. Although the tax impact of repatriating these earnings is difficult to determine and our effective tax rate could increase as a result of any such repatriation, we would not expect the maximum effective tax rate that would be applicable to such repatriation to exceed the U.S. statutory rate of 35.0%, after considering applicable foreign tax credits.

We believe that existing cash and cash equivalents and short-term investments held by us and cash and cash equivalents anticipated to be generated by us are sufficient to meet working capital requirements, anticipated capital expenditures, and contractual obligations for at least the next 12 months.

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The following table sets forth a summary of our cash flows (in thousands) and related percentage changes for the periods indicated:

|                                                     | <b>Nine Months Ended</b> |             | <b>%</b>      |
|-----------------------------------------------------|--------------------------|-------------|---------------|
|                                                     | <b>September 30,</b>     | <b>2014</b> | <b>Change</b> |
|                                                     | <b>2015</b>              |             |               |
| Net cash provided by operating activities           | \$ 123,443               | \$ 16,321   | 656.3%        |
| Net cash used in investing activities               | \$ (40,870)              | \$ (96,388) | -57.6%        |
| Net cash provided by (used in) financing activities | \$ 4,972                 | \$ (2,035)  | -344.3%       |

**Net Cash Provided by Operating Activities.** The primary source of our cash provided by operating activities is cash collections of our accounts receivable from customers following the sales and renewals of our software licenses, technical software support, software updates and upgrades, as well as consulting, education, and subscription services. Our primary uses of cash in operating activities are for personnel related expenditures for software development, personnel related expenditures for providing consulting, education, and subscription services, and for sales and marketing costs, general and administrative costs, and income taxes.

Net cash provided by operating activities was \$123.4 million and \$16.3 million for the nine months ended September 30, 2015 and 2014, respectively. The increase in net cash provided by operating activities during the nine months ended September 30, 2015, as compared to the same period in the prior year, was due to a \$84.5 million increase in net income and a \$23.6 million increase from changes in non-cash items, offset by a \$0.9 million decrease from changes in operating assets and liabilities. Non-cash items consist of depreciation and amortization, bad debt expense, unrealized net gains and losses on foreign currency forward contracts, the non-cash portion of adjustments to accrued restructuring costs, deferred taxes, release of liabilities for unrecognized tax benefits, share-based compensation expense, excess tax benefits from share-based compensation arrangements, and reclassification of foreign currency translation adjustments that resulted from the completion of the liquidation of certain foreign subsidiaries.

**Net Cash Used in Investing Activities.** The changes in net cash used in investing activities relate to purchases and redemptions of short-term investments, expenditures on property and equipment, capitalized software development costs, and changes in restricted cash. Net cash used in investing activities was \$40.9 million and \$96.4 million for the nine months ended September 30, 2015 and 2014, respectively. The decrease in net cash used in investing activities for the nine months ended September 30, 2015, as compared to the same period in the prior year, was due to a \$93.7 million increase in proceeds from the redemption of U.S. Treasury securities, an \$8.5 million decrease in purchases of property and equipment, and a \$1.1 million decrease in restricted cash, partially offset by a \$40.5 million increase in purchases of short-term investments and a \$7.3 million increase in capitalized software development costs.

**Net Cash Provided by (Used in) Financing Activities.** The changes in net cash provided by (used in) financing activities relate to the exercise of stock options under the 2013 Equity Plan, excess tax benefits from share-based compensation arrangements, and payments on capital lease and other financing arrangements. Net cash provided by financing activities was \$5.0 million for the nine months ended September 30, 2015. Net cash used in financing activities was \$2.0 million for the nine months ended September 30, 2014. The increase in net cash provided by financing activities for the nine months ended September 30, 2015, as compared to the same period in the prior year, was due to a \$5.4 million increase in proceeds from the exercise of stock options under the 2013 Equity Plan, a \$1.0 million increase in excess tax benefits from share-based compensation arrangements, and a \$0.6 million decrease in payments on capital lease and other financing arrangements.



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**Contractual Obligations.** As disclosed in Note 8, Commitments and Contingencies, to the Consolidated Financial Statements, we lease office space and computer and other equipment under operating lease agreements. We also lease certain computer and other equipment under capital lease agreements and license certain software under other financing arrangements. Under the lease agreements, in addition to base rent, we are generally responsible for certain taxes, utilities and maintenance costs, and other fees; and several leases include options for renewal or purchase. The following table shows future minimum rent payments under noncancellable operating and capital leases and agreements with initial terms of greater than one year, net of total future minimum rent payments to be received under noncancellable sublease agreements (in thousands), based on the expected due dates of the various installments as of September 30, 2015:

|                                                 | Payments due by period ended September 30, |           |           |           |            |
|-------------------------------------------------|--------------------------------------------|-----------|-----------|-----------|------------|
|                                                 | Total                                      | 2016      | 2017-2018 | 2019-2020 | Thereafter |
| <i>Contractual Obligations:</i>                 |                                            |           |           |           |            |
| Operating leases                                | \$ 94,602                                  | \$ 24,235 | \$ 35,897 | \$ 26,917 | \$ 7,553   |
| Capital leases and other financing arrangements | 228                                        | 172       | 50        | 6         | 0          |
| Total                                           | \$ 94,830                                  | \$ 24,407 | \$ 35,947 | \$ 26,923 | \$ 7,553   |

**Unrecognized Tax Benefits.** As of September 30, 2015, we had \$2.7 million of total gross unrecognized tax benefits, including interest accrued, recorded in other long-term liabilities. The timing of any payments that could result from these unrecognized tax benefits will depend on a number of factors, and accordingly the amount and period of any future payments cannot be estimated. We do not expect a significant tax payment related to these obligations during 2015.

**Off-Balance Sheet Arrangements.** As of September 30, 2015, we did not have any off-balance sheet arrangements that had or were reasonably likely to have a current or future material impact on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

**Recent Accounting Standards**

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance. The standard's core principle is that an entity should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard creates a five-step model to achieve its core principle: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the separate performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. In addition, entities must disclose sufficient information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Qualitative and quantitative disclosures are required about: (1) the entity's contracts with customers, (2) the significant judgments, and changes in judgments, made in applying the guidance to those contracts, and (3) any assets recognized from the costs to obtain or fulfill a contract with a customer. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606) - Deferral of the Effective Date*, which defers the effective date of ASU 2014-09 to interim and annual periods beginning January 1, 2018. The standard allows entities to apply the standard retrospectively to each prior reporting period presented (full retrospective adoption) or retrospectively with the cumulative effect of initially applying the standard recognized at the date of

initial application ( modified retrospective adoption ). The Company is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

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In April 2015, the FASB issued Accounting Standards Update No. 2015-05, *Intangibles – Goodwill and Other Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement* (ASU 2015-05), which provides guidance on which existing accounting model should be applied to cloud computing arrangements. Under ASU 2015-05, customers will apply the same criteria as vendors to determine whether a cloud computing arrangement contains a software license or is solely a service contract. Specifically, fees paid by a customer in a cloud computing arrangement will be subject to internal-use software guidance if the customer has both the contractual right to take possession of the software at any time without significant penalty and it is feasible for the customer to run the software on its own hardware. Arrangements that do not meet both of the criteria are considered service contracts, and separate accounting for a license will not be permitted. ASU 2015-05 is effective for interim and annual periods beginning January 1, 2016. The standard allows entities to apply the standard retrospectively or prospectively for all new transactions entered into or materially modified after the date of adoption. The Company utilizes certain cloud computing arrangements in its daily business operations and is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

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

The following discussion about our market risk exposures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements.

We are exposed to the impact of both interest rate changes and foreign currency fluctuations.

**Interest Rate Risk.** We face exposure to changes in interest rates primarily relating to our investments. We generally invest our excess cash in short-term, highly-rated, fixed-rate financial instruments. These fixed-rate instruments are subject to interest rate risk and may fall in value if interest rates increase. As of September 30, 2015, we held approximately \$226.6 million of investments in U.S. Treasury securities with stated maturity dates between three months and one year from the purchase date, and we intend to hold these investments until maturity.

**Foreign Currency Risk.** We conduct a significant portion of our business in currencies other than the U.S. dollar, the currency in which we report our Consolidated Financial Statements. International revenues accounted for 39.9% and 40.7% of our total revenues for the three months ended September 30, 2015 and 2014, respectively, and 37.2% and 41.3% of our total revenues for the nine months ended September 30, 2015 and 2014, respectively. We anticipate that international revenues will continue to account for a significant portion of our total revenues. The functional currency of each of our foreign subsidiaries is the local currency.

Assets and liabilities of our foreign subsidiaries are translated into U.S. dollars at exchange rates in effect as of the applicable balance sheet date and any resulting translation adjustments are included as an adjustment to stockholders equity. Revenues and expenses generated from these subsidiaries are translated at average monthly exchange rates during the quarter in which the transactions occur. Gains and losses from transactions in local currencies are included in net income.

As a result of transacting in multiple currencies and reporting our financial statements in U.S. dollars, our operating results may be adversely impacted by currency exchange rate fluctuations in the future. The impact of foreign currency exchange rate fluctuations on current and comparable periods is described in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations.

We cannot predict the effect of exchange rate fluctuations upon our future results. We attempt to minimize our foreign currency risk by converting our excess foreign currency held in foreign jurisdictions to U.S. dollar denominated cash and investment accounts. Although we were not party to any foreign currency forward contracts as of September 30, 2015, from time to time we have entered into foreign currency forward contracts to hedge certain risks associated with foreign currency exchange exposure, and may do so again in the future. We manage the use of foreign exchange derivative instruments centrally, and we do not hold or enter into derivative financial instruments for speculative trading purposes. See Note 3, Fair Value Measurements, to the Consolidated Financial Statements for further information on foreign currency forward contracts. We cannot be sure that any future hedging techniques will be successful or that our business, results of operations, financial condition, and cash flows will not be materially adversely affected by exchange rate fluctuations.

As of September 30, 2015 and December 31, 2014, a 10% adverse change in foreign currency exchange rates versus the U.S. dollar, before applying the impact of outstanding foreign currency forward contracts for the period ending December 31, 2014, would have decreased our aggregate reported cash and cash equivalents and short-term investments by 0.3% and 0.3%, respectively. The exposure to an adverse change in foreign currency rates as of September 30, 2015 remained unchanged primarily due to a strengthening of the U.S. dollar offset by an increase of cash balances in our non-U.S. dollar-based bank accounts as compared to December 31, 2014. If average exchange rates during the nine months ended September 30, 2015 had changed unfavorably by 10%, our revenues for the nine

months ended September 30, 2015 would have decreased by 3.3%. During the nine months ended September 30, 2015, our revenues were lower by 6.4% as a result of a 15.1% unfavorable change in weighted average exchange rates, as compared to the same period in the prior year.

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**Item 4. Controls and Procedures**

***Evaluation of disclosure controls and procedures.*** Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this quarterly report. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their control objectives. Based on the evaluation of our disclosure controls and procedures as of the end of the period covered by this quarterly report, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were not effective at the reasonable assurance level because of a material weakness related to the control activities performed by the third-party service organization, as described in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2014. Although we have not received an adequate Service Organization Control ( SOC ) 1 Type 2 report from the third-party service organization, management believes, based on substantive testing performed, that the financial statements included in this quarterly report fairly present in all material respects our financial condition, results of operations, and cash flows for the periods presented. The Company has been monitoring the third-party service organization's compliance with its obligation to provide an adequate SOC 1 Type 2 report for the current fiscal year.

***Changes in internal controls.*** No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended September 30, 2015 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II - OTHER INFORMATION**

**Item 1. Legal Proceedings**

In December 2011, DataTern, Inc. ( "DataTern" ) filed a complaint for patent infringement against the Company in the United States District Court for the District of Massachusetts (the "District Court" ). The complaint alleged that the Company infringes U.S. Patent No. 6,101,502 (the "502 Patent" ), allegedly owned by DataTern, by making, selling, or offering for sale several of the Company's products and services including MicroStrategy 9, MicroStrategy Intelligence Server, MicroStrategy Business Intelligence Platform, MicroStrategy Cloud Personal, and other MicroStrategy applications for creating or using data mining, dashboards, business analytics, data storage and warehousing, and Web hosting support. The complaint accused the Company of willful infringement and sought an unspecified amount of damages, an award of attorneys' fees, and preliminary and permanent injunctive relief. In light of a judgment in a separate action involving DataTern in another jurisdiction, in February 2013, MicroStrategy and DataTern filed motions for summary judgment of non-infringement and the District Court entered summary judgment against DataTern. In March 2013, DataTern filed a notice of appeal with the United States Court of Appeals for the Federal Circuit (the "Federal Circuit" ). In December 2014, the Federal Circuit issued an opinion vacating the District Court's summary judgment, stating that the claim construction on which the summary judgment was based was incorrect. In January 2015, the Federal Circuit ordered that the case be remanded for further proceedings, and in February 2015, MicroStrategy filed motions for summary judgment in the District Court on grounds of non-infringement and invalidity. On September 4, 2015, the District Court denied the Company's motions for summary judgment. We have received indemnification requests from certain of our channel partners and customers who were sued by DataTern in the District Court in lawsuits alleging infringement of the 502 Patent. The outcome of these matters is not presently determinable.

We are also involved in various other legal proceedings arising in the normal course of business. Although the outcomes of these other legal proceedings are inherently difficult to predict, we do not expect the resolution of these other legal proceedings to have a material adverse effect on our financial position, results of operations, or cash flows.

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### **Item 1A. Risk Factors**

You should carefully consider the risks described below before making an investment decision. The risks and uncertainties described below are not the only ones facing MicroStrategy. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations.

If any of the following risks actually occur, our business, financial condition, or results of operations could be materially adversely affected. In such case, the market price of our class A common stock could decline and you may lose all or part of your investment.

#### **Our quarterly operating results, revenues, and expenses may fluctuate significantly, which could have an adverse effect on the market price of our stock**

For a number of reasons, including those described below, our operating results, revenues, and expenses have in the past varied and may in the future vary significantly from quarter to quarter. These fluctuations could have an adverse effect on the market price of our class A common stock.

*Fluctuations in Quarterly Operating Results.* Our quarterly operating results may fluctuate, in part, as a result of:

the size, timing, volume, and execution of significant orders and shipments;

the mix of products and services ordered by customers, including product licenses and subscription offerings, which can affect the extent to which revenue is recognized immediately or over future quarterly periods;

the timing of the release or delivery of new or enhanced offerings, which may affect the period in which we are able to recognize revenue;

the timing of announcements of new offerings by us or our competitors;

changes in our pricing policies or those of our competitors;

market acceptance of new and enhanced versions of our products and services;

the length of our sales cycles;

seasonal or other buying patterns of our customers;

changes in our operating expenses, including the impact of our recent restructuring activities;

planned major maintenance activities related to our owned corporate aircraft;

the timing of research and development projects and the capitalization of software development costs;

personnel changes, including the impact of our recent restructuring activities;

our use of channel partners;

utilization of our consulting and education services, which can be affected by delays or deferrals of customer implementation of our software products;

changes in foreign currency exchange rates;

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our profitability and expectations for future profitability and its effect on our deferred tax assets and net income for the period in which any adjustment to our net deferred tax asset valuation allowance may be made;

increases or decreases in our liability for unrecognized tax benefits; and

changes in customer decision making processes or customer budgets.

*Limited Ability to Adjust Expenses.* We base our operating expense budgets on expected revenue trends and strategic objectives. Many of our expenses, such as office leases and certain personnel costs, are relatively fixed. We may be unable to adjust spending quickly enough to offset any unexpected revenue shortfall. Accordingly, any shortfall in revenue may cause significant variation in operating results in any quarter. For example, although we have implemented substantially all of the 2014 Restructuring Plan that is designed to reduce our operating expenses, if our revenues in the future are not sufficient to offset our operating expenses, or we are unable to adjust our operating expenses in a timely manner in response to any shortfall in anticipated revenue, we may incur operating losses.

Based on the above factors, we believe that quarter-to-quarter comparisons of our operating results are not a good indication of our future performance. It is possible that in one or more future quarters, our operating results may be below the expectations of public market analysts and investors. In that event, the market price of our class A common stock may fall.

**The market price of our class A common stock has been and may continue to be volatile**

The market price of our class A common stock historically has been volatile and may continue to be volatile. The market price of our class A common stock may fluctuate widely in response to various factors, some of which are beyond our control. These factors include, but are not limited to:

quarterly variations in our results of operations or those of our competitors;

announcements about our earnings that are not in line with analyst expectations, the likelihood of which may be enhanced because it is our policy not to give guidance relating to our anticipated financial performance in future periods;

announcements by us or our competitors of acquisitions, dispositions, new offerings, significant contracts, commercial relationships, or capital commitments;

the emergence of new sales channels in which we are unable to compete effectively;

our ability to develop, market, and deliver new and enhanced offerings on a timely basis;

commencement of, or our involvement in, litigation;

any major change in our board, management, or governing documents;

changes in governmental regulations or in the status of our regulatory approvals;

recommendations by securities analysts or changes in earnings estimates;

announcements by our competitors of their earnings that are not in line with analyst expectations;

the volume of shares of our class A common stock available for public sale;

sales or purchases of stock by us or by our stockholders, and issuances of awards under our stock incentive plan;

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short sales, hedging, and other derivative transactions involving shares of our class A common stock; and

general economic conditions and slow or negative growth of related markets.

In addition, the stock market in general, and the market for technology companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of technology companies. These broad market and industry factors may seriously harm the market price of our class A common stock, regardless of our actual operating performance.

**We may not be able to sustain or increase profitability in the future**

We generated net income for the nine months ended September 30, 2015; however, we may not be able to sustain or increase profitability on a quarterly or annual basis in the future. If our revenues are not sufficient to offset our operating expenses, or we are unable to adjust our operating expenses in a timely manner in response to any shortfall in anticipated revenue, our profitability may decrease, we may cease to be profitable, or we may incur operating losses. As a result, our business, results of operations, and financial condition may be materially adversely affected.

As of September 30, 2015, we had \$14.6 million of deferred tax assets, net of a \$2.1 million valuation allowance, and if we are unable to sustain profitability in the future, we may be required to increase the valuation allowance against these deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred.

**We face risks arising from our restructuring activities**

In September 2014, we committed to a restructuring plan to streamline our workforce and spending to better align our cost structure with our business strategy. We implemented substantially all of the plan in 2014, including a workforce reduction of 777 employees worldwide. See Note 6, Restructuring, to the consolidated financial statements filed with this Quarterly Report on Form 10-Q for further information relating to the restructuring plan. The restructuring, including the organizational, operational, and strategic changes that have taken place during and following the implementation of the restructuring plan, presents significant potential risks that may impair our ability to achieve anticipated cost reductions or otherwise harm our business, including:

a decrease in employee morale, which could lead to voluntary departures of key employees;

failure to meet operational targets or customer requirements due to the termination or attrition of employees, or a decrease in employee morale;

failure to maintain adequate controls and procedures while consolidating operational and administrative infrastructure following the execution of the restructuring;

diversion of management attention from ongoing business activities; and

employment by our competitors of employees whose positions were eliminated in connection with the restructuring.

**Economic uncertainty, particularly in the retail industry, could materially adversely affect our business and results of operations**

In recent years, the United States and other significant markets have experienced cyclical downturns and worldwide economic conditions remain uncertain. Economic uncertainty and associated macroeconomic conditions make it extremely difficult for our customers and us to accurately forecast and plan future business activities, and could cause our customers to slow spending on our products and services, which could delay and lengthen sales cycles. Furthermore, during uncertain economic times our customers may face issues gaining timely access to sufficient credit, which could result in an impairment of their ability to make timely payments to us. If that were to occur, we may be required to increase our allowance for doubtful accounts and our results would be negatively impacted.

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Furthermore, we have a significant number of customers in the retail industry. A significant downturn in this industry may cause organizations to react by reducing their capital expenditures in general or by specifically reducing their spending on information technology. In addition, customers in this industry may delay or cancel information technology projects or seek to lower their costs by renegotiating vendor contracts. Customers with excess information technology resources may choose to develop in-house software solutions rather than obtain those solutions from us. Moreover, competitors may respond to challenging market conditions by lowering prices and attempting to lure away our customers.

We cannot predict the timing, strength, or duration of any economic slowdown or any subsequent recovery generally, or in the retail industry in particular. If the conditions in the general economy and the markets in which we operate worsen from present levels, our business, financial condition, and results of operations could be materially adversely affected.

### **We may have exposure to greater than anticipated tax liabilities**

We are subject to income taxes and non-income taxes in a variety of domestic and foreign jurisdictions. Our future income taxes could be materially adversely affected by earnings that are lower than anticipated in jurisdictions where we have lower statutory rates and earnings that are higher than anticipated in jurisdictions where we have higher statutory rates, by changes in the valuation of our deferred tax assets and liabilities, changes in the amount of unrecognized tax benefits, or by changes in tax laws, regulations, accounting principles, or interpretations thereof.

Further changes in the tax laws of foreign jurisdictions could arise, whether as a result of the base erosion and profit shifting (BEPS) project undertaken by the Organisation for Economic Co-operation and Development (OECD) or otherwise. The OECD, which represents a coalition of member countries, has issued recommendations that, in some cases, would make substantial changes to numerous long-standing tax positions and principles. These contemplated changes, to the extent adopted by OECD members and/or other countries, could increase tax uncertainty and may adversely affect our provision for income taxes. In addition, in the United States various proposals for broad reform of the existing U.S. corporate tax system are under evaluation by various legislative and administrative bodies, but it is not possible to accurately determine the overall impact of such proposals on our effective tax rate at this time.

Our determination of our tax liability is subject to review by applicable domestic and foreign tax authorities. For example, we are currently under tax examination in the U.S. Any adverse outcome of such reviews could have an adverse effect on our operating results and financial condition. The determination of our worldwide provision for income taxes and other tax liabilities requires significant judgment and, in the ordinary course of business, there are many transactions and calculations where the ultimate tax determination is uncertain. Moreover, as a multinational business, we have subsidiaries that engage in many intercompany transactions in a variety of tax jurisdictions where the ultimate tax determination is uncertain.

We also have contingent tax liabilities that, in management's judgment, are not probable of assertion. If such unasserted contingent liabilities were to be asserted, or become probable of assertion, we may be required to record significant expenses and liabilities in the period in which these liabilities are asserted or become probable of assertion.

As a result of these and other factors, the ultimate amount of tax obligations owed may differ from the amounts recorded in our financial statements and any such difference may materially affect our financial results in future periods in which we change our estimates of our tax obligations or in which the ultimate tax outcome is determined.



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**If the market for analytics products fails to grow as we expect, or if businesses fail to adopt our offerings, our business, operating results, and financial condition could be materially adversely affected**

Nearly all of our revenues to date have come from sales of analytics products and related technical support, consulting, and education services. We expect these sales to account for a large portion of our revenues for the foreseeable future. Although demand for analytics products has grown in recent years, the market for analytics offerings continues to evolve. Resistance from consumer and privacy groups to increased commercial collection and use of data on spending patterns and other personal behavior and governmental restrictions on the collection and use of personal data may impair the further growth of this market, as may other developments. We cannot be sure that this market will continue to grow or, even if it does grow, that businesses will adopt our solutions.

We have spent, and intend to keep spending, considerable resources to educate potential customers about analytics offerings in general and our offerings in particular. However, we cannot be sure that these expenditures will help any of our offerings achieve any additional market acceptance. If the market fails to grow or grows more slowly than we currently expect or businesses fail to adopt our offerings, our business, operating results, and financial condition could be materially adversely affected.

**Our products face intense competition, which may lead to lower prices for our products and services, reduced gross margins, loss of market share, and reduced revenue**

The analytics platform market is highly competitive and subject to rapidly changing technology paradigms. Within the analytics space, we compete with many different vendors, including (i) large software vendors (megavendors), such as IBM, SAP, Microsoft, and Oracle, that provide one or more products that directly compete with our products; (ii) open source analytics vendors such as TIBCO JasperSoft and Pentaho; (iii) various other analytics software providers, such as Qlik, Tableau Software, Information Builders, and the SAS Institute; (iv) pure-play mobile analytics vendors, such as MeLLmo (Roambi), that do not offer an analytics platform but offer a mobile user interface that can be used as an extension to existing analytics platforms; and (v) other vendors offering cloud-based offerings, such as GoodData and Birst. Our future success depends on the effectiveness with which we can differentiate and compete with these vendors and other potential competitors across different sizes of analytics implementation projects. Failure to maintain adequate technology differentiation from these competitors could materially adversely affect our recurring software maintenance revenue and new license and subscription revenues from both existing and prospective customers.

Some of our competitors have longer operating histories and significantly greater financial, technical, and marketing resources than we do. As a result, they may be able to respond more quickly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion, sale, and marketing of their offerings than we can, such as offering certain analytics products free of charge when bundled with other software offerings. In addition, many of our competitors have strong relationships with current and potential customers, extensive industry and specialized business knowledge, as well as corresponding proprietary technologies that they can leverage, such as multidimensional databases and ERP repositories. As a result, they may be able to prevent us from penetrating new accounts or expanding within existing accounts.

Increased competition may lead to price cuts, reduced gross margins, and loss of market share. We may not be able to compete successfully against current and future competitors and the failure to meet the competitive pressures we face may have a material adverse effect on our business, operating results, and financial condition.

Current and future competitors may also make strategic acquisitions or establish cooperative relationships among themselves or with others. By doing so, these competitors may increase their ability to meet the needs of our potential

customers by virtue of their expanded offerings. Our current or prospective channel partners may establish cooperative relationships with our current or future competitors. These relationships may limit our ability to sell our analytics offerings through specific distribution channels. Accordingly, new competitors or alliances among current and future competitors may emerge and rapidly gain significant market share. These developments could limit our ability to obtain revenues from new customers and to sustain software maintenance revenues from our installed customer base. In addition, basic office productivity software suites, such as Microsoft Office, could evolve to offer advanced analysis and reporting capabilities that may reduce the demand for our analytics offerings.

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Usher competes with technologies categorized as user authentication products, which are dominated by a few companies such as the RSA division of EMC, CA, SafeNet, Vasco, and Gemalto. These competitors focus primarily on traditional forms of identity verification such as smart cards, tokens, and password managers. These companies have significant name recognition and offer solutions with security architectures that are familiar to IT buyers. Usher also competes with companies with newer solutions, often involving mobile technology, including Telesign, Authentify, SecurEnvoy, Daon, Entrust, and Duo Security. To date, we have expended significant resources in the development and marketing of Usher, which has not generated significant revenues. Failure to adequately differentiate and market our technology from these competitors could materially adversely affect our ability to generate significant revenues from Usher.

**We depend on revenue from a single suite of products and related services**

Our MicroStrategy Analytics software and related products and services account for a substantial portion of our revenue. Because of this revenue concentration, our business could be harmed by a decline in demand for, or in the adoption or prices of, our MicroStrategy Analytics software as a result of, among other factors, any change in our pricing model, increased competition, maturation in the markets for these products, or other risks described in this document.

**If we are unable to develop and release product enhancements and new offerings to respond to rapid technological change in a timely and cost-effective manner, our business, operating results, and financial condition could be materially adversely affected**

The market for our offerings is characterized by rapid technological change, frequent new product introductions and enhancements, changing customer demands, and evolving industry standards. The introduction of offerings embodying new technologies can quickly make existing offerings obsolete and unmarketable. We believe that our future success depends largely on three factors:

our ability to continue to support a number of popular operating systems and databases;

our ability to maintain and improve our current offerings; and

our ability to rapidly develop new offerings and product enhancements that achieve market acceptance, maintain technological competitiveness, and meet an expanding range of customer requirements.

Analytics applications are inherently complex, and it can take a long time and require significant research and development expenditures to develop and test new offerings and product enhancements. In addition, customers may delay their purchasing decisions because they anticipate that new or enhanced versions of our offerings will soon become available. We cannot be sure that we will succeed in developing, marketing, and delivering on a timely and cost-effective basis new or enhanced offerings that respond to technological change or new customer requirements, nor can we be sure that any new or enhanced offerings, such as MicroStrategy 10 Secure Enterprise, which was made generally available in June 2015, will achieve market acceptance. Moreover, even if we introduce a new offering, we may experience a decline in revenues of our existing offerings that is not fully matched by the new offering's revenue. For example, customers may delay making purchases of a new offering to permit them to make a more thorough evaluation of the offering, or until industry and marketplace reviews become widely available. Some customers may hesitate migrating to a new offering due to concerns regarding the complexity of migration and product infancy issues.

on performance. In addition, we may lose existing customers who choose a competitor's offering rather than migrate to our new offering. This could result in a temporary or permanent revenue shortfall and materially adversely affect our business.

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**A substantial customer shift from the deployment of MicroStrategy Analytics based on a perpetual software license to our cloud services offerings could affect the timing of revenue recognition and materially adversely affect our operating results**

We offer our analytics platform in the form of a perpetual software license and a cloud-based Platform-as-a-Service subscription. The payment streams and revenue recognition timing for our perpetual software licenses are different from those for our subscription services. For perpetual software licenses, customers typically pay us a lump sum soon after entering into a software license agreement and revenue is typically recognized upon delivery of the software to the customer. For subscription services, customers typically make periodic payments over the subscription period and revenue is typically recognized ratably over the subscription period. As a result, if a substantial number of current or new customers shift to subscribing to our cloud services offerings instead of purchasing perpetual software licenses for MicroStrategy Analytics, the resulting change in payment terms and revenue recognition may materially adversely affect our operating results and cash flows for the reporting periods during which such a shift occurs.

**Our investment in new business strategies and initiatives could disrupt the operations of our ongoing business and present risks that we have not adequately anticipated**

We have invested, and in the future may invest, in new business strategies and initiatives. For example, in recent years we have introduced a number of innovative technologies designed to enable companies to capitalize on Big Data, mobile applications, cloud-based services, and security trends in the marketplace. These endeavors may involve significant risks and uncertainties, including distraction of management from other business operations, the dedication of significant research and development, sales and marketing, and other resources to these new initiatives at the expense of our other business operations, generation of insufficient revenue to offset expenses associated with new initiatives, incompatibility of our new technologies with third-party platforms, inadequate return of capital, and other risks that we may not have adequately anticipated. For example, we have expended significant resources in the development and marketing of Usher, which has not generated significant revenues to date. Because new strategies and initiatives are inherently risky, these strategies and initiatives may not be successful and could materially adversely affect our financial condition and operating results.

**Business disruptions, including interruptions, delays, or failures in service from our third-party data center hosting facilities and other third-party services, could materially adversely affect our operating results or result in a material weakness in our internal controls that could adversely affect the market price of our stock**

A significant portion of our research and development activities or certain other critical business operations are concentrated in facilities in Northern Virginia, China, and Poland. In addition, we serve our customers, and manage certain critical internal processes, using third-party data center hosting facilities located in the United States and England and other third-party services, including Amazon Web Services and other cloud services. We are a highly automated business, and a disruption or failure of our systems, or the third-party hosting facilities or other services that we use, could cause delays in completing sales and providing services. Such disruptions or failures could include a major earthquake, fire, cyber-attack, act of terrorism or other catastrophic event, or a decision by one of our third-party service providers to close facilities that we use without adequate notice or other unanticipated problems with the third-party services that we use, including a failure to meet service standards.

Any such disruptions or failures could (i) result in the destruction or disruption of any of our critical business operations, controls, or procedures or information technology systems, (ii) severely affect our ability to conduct normal business operations, (iii) result in a material weakness in our internal control over financial reporting, (iv) cause our customers to terminate their subscriptions, (v) result in our issuing credits or paying penalties or fines, (vi) harm our reputation, (vii) adversely affect our attrition rates or our ability to attract new customers, or (viii) cause

our offerings to be perceived as not being secure, any of which could materially adversely affect our future operating results.

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For example, as described in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2014, we have a material weakness that resulted from a failure by a third-party service organization to provide an adequate SOC 1 Type 2 report. If we are unable to appropriately remediate this material weakness, any ineffectiveness of our internal controls could have a material adverse effect on our operating results, cause us to fail to meet our reporting obligations, cause management to devote significant resources to improving internal controls, or reduce the market's confidence in our financial statements, which could adversely affect the market price of our stock.

**We use channel partners and if we are unable to maintain successful relationships with them, our business, operating results, and financial condition could be materially adversely affected**

In addition to our direct sales force, we use channel partners such as resellers, value-added resellers, system integrators and consulting firms, original equipment manufacturers, and technology partners to license and support our products. For the nine months ended September 30, 2015, transactions by channel partners for which we recognized revenues accounted for 19.4% of our total product licenses revenues. Our channel partners may offer customers the products and services of several different companies, including offerings that compete with ours. Because our channel partners generally do not have an exclusive relationship with us, we cannot be certain that they will prioritize or provide adequate resources to selling our products. Moreover, divergence in strategy or contract defaults by any of these channel partners may materially adversely affect our ability to develop, market, sell, or support our offerings.

Although we believe that direct sales will continue to account for a majority of product licenses revenues, we seek to maintain a significant level of sales activities through our channel partners. There can be no assurance that our channel partners will continue to cooperate with us. In addition, actions taken or omitted to be taken by such parties may materially adversely affect us. Our ability to achieve revenue growth in the future will depend in part on our ability to maintain successful relationships with our channel partners. If we are unable to maintain our relationships with these channel partners, our business, results of operations, and financial condition could be materially adversely affected.

In addition, we rely on our channel partners to operate in accordance with the terms of their contractual agreements with us. For example, our agreements with our channel partners limit the terms and conditions pursuant to which they are authorized to resell or distribute our software and offer technical support and related services. We also typically require our channel partners to represent to us the dates and details of product licenses transactions sold through to end user customers. If our channel partners do not comply with their contractual obligations to us, our business, results of operations, and financial condition may be materially adversely affected.

**Our recognition of deferred revenue and advance payments and future customer purchase commitments is subject to future performance obligations and may not be representative of revenues for succeeding periods**

Our gross current and non-current deferred revenue and advance payments totaled \$182.4 million as of September 30, 2015. We offset our accounts receivable and deferred revenue for any unpaid items, which totaled \$56.6 million, resulting in net current and non-current deferred revenue and advance payments of \$125.8 million as of September 30, 2015. The timing and ultimate recognition of our deferred revenue and advance payments depend on various factors, including our performance of various service obligations.

We have entered into certain additional agreements that include future minimum commitments by our customers to purchase product licenses, subscription services, product support, or other services through 2020 totaling approximately \$138.4 million. These future commitments are not included in our deferred revenue balances. Because of the possibility of customer changes or delays in customer development or implementation schedules or budgets, and the need for us to satisfactorily perform product support and other services, deferred revenue and advance payments at any particular date may not be representative of actual revenue for any succeeding period.



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**Our international operations are complex and expose us to risks that could have a material adverse effect on our business, operating results, and financial condition**

We receive a significant portion of our total revenues from international sales, and conduct our business activities in various foreign countries, including some emerging markets where we have limited experience, where the challenges of conducting our business can be significantly different from those we have faced in more developed markets, and where business practices may create internal control risks. International revenues accounted for 39.9% and 40.7% of our total revenues for the three months ended September 30, 2015 and 2014, respectively, and 37.2% and 41.3% of our total revenues for the nine months ended September 30, 2015 and 2014, respectively. Our international operations require significant management attention and financial resources.

There are certain risks inherent in our international business activities including:

fluctuations in foreign currency exchange rates;

new, or changes in, regulatory requirements;

tariffs, export and import restrictions, restrictions on foreign investments, sanctions, and other trade barriers or protection measures;

costs of localizing offerings;

lack of acceptance of localized offerings;

difficulties in and costs of staffing, managing, and operating our international operations;

tax issues, including restrictions on repatriating earnings;

weaker intellectual property protection;

economic weakness or currency related crises;

the burden of complying with a wide variety of laws, including those relating to labor matters, consumer and data protection, privacy, network security, and encryption;

generally longer payment cycles and greater difficulty in collecting accounts receivable;

our ability to adapt to sales practices and customer requirements in different cultures;

corporate espionage; and

political instability and security risks in the countries where we are doing business.

Various corporate tax reform bills and other proposals are currently under consideration by Congress and the Obama Administration. These proposals include, among other items, corporate income tax rate changes in varying, uncertain, or unspecified amounts, the reduction or elimination of certain corporate tax incentives, modifications to the existing regime for taxing overseas earnings (including the introduction of a minimum tax on adjusted unrepatriated foreign earnings), and measures to prevent base erosion and profit shifting. It is not clear whether, or to what extent, these proposals may be enacted. Although the overall impact that such proposals may have on our future effective tax rate is unclear at this time, significant changes to the U.S. taxation of our international income could have a material adverse effect on our results of operations.

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From time to time, we may undertake various potential intercompany transactions and legal entity restructurings that involve our international subsidiaries. We consider various factors in evaluating these potential transactions and restructurings, including the alignment of our corporate structure with our organizational objectives, the operational and tax efficiency of our corporate structure, and the long-term cash flows and cash needs of our business. Such transactions and restructurings could negatively impact our overall tax rate and result in additional tax liabilities.

In addition, compliance with foreign and U.S. laws and regulations that are applicable to our international operations is complex and may increase our cost of doing business in international jurisdictions, and our international operations could expose us to fines and penalties if we fail to comply with these regulations. These laws and regulations include import and export requirements and anti-bribery laws, such as the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, and local laws prohibiting corrupt payments to governmental officials. Although we have implemented policies and procedures designed to help ensure compliance with these laws, there can be no assurance that our employees, partners, and other persons with whom we do business will not take actions in violation of our policies or these laws. Any violations of these laws could subject us to civil or criminal penalties, including substantial fines or prohibitions on our ability to offer our products and services to one or more countries, and could also materially damage our reputation and our brand.

These factors may have a material adverse effect on our future sales and, consequently, on our business, operating results, and financial condition.

**We may lose sales, or sales may be delayed, due to the long sales and implementation cycles of certain of our products, which could reduce our revenues**

To date, our customers have typically invested substantial time, money, and other resources and involved many people in the decision to license our software products and purchase our consulting and education services. As a result, we may wait nine months or more after the first contact with a customer for that customer to place an order while it seeks internal approval for the purchase of our products or services. During this long sales cycle, events may occur that affect the size and/or timing of the order or even cause it to be canceled. For example, our competitors may introduce new offerings, or the customer's own budget and purchasing priorities may change.

Even after an order is placed, the time it takes to deploy our products and complete consulting engagements can vary widely. Implementing some of our offerings can take several months, depending on the customer's needs, and may begin only with a pilot program. It may be difficult to deploy our products if the customer has complicated deployment requirements, which typically involve integrating databases, hardware, and software from different vendors. If a customer hires a third party to deploy our products, we cannot be sure that our products will be deployed successfully.

**Our results in any particular period may depend upon the number and volume of large transactions in that period and these transactions may involve lengthier, more complex, and more unpredictable sales cycles than other transactions**

As existing and potential customers seek to standardize on a single analytics vendor or require greater vendor capacity to meet their growing analytics needs, our business may experience larger transactions at the enterprise level and larger transactions may account for a greater proportion of our business. The presence or absence of one or more large transactions in a particular period may have a material positive or negative effect on our revenue and operating results for that period. For the nine months ended September 30, 2015 and 2014, our top three product licenses transactions with recognized revenue totaled \$6.5 million and \$6.2 million, respectively, or 8.4% and 6.8% of total product licenses revenues, respectively. These transactions represent significant business and financial decisions for our

customers, require considerable effort on the part of customers to assess alternative products, and often require additional levels of management approval. In addition, large transactions are often more complex than smaller transactions. These factors generally lengthen the typical sales cycle and increase the risk that customers may postpone or delay purchasing decisions from one period to another subsequent or later period or that customers will alter their purchasing requirements. The sales effort and service delivery scope for larger transactions also require us to use additional resources to execute the transaction. These factors could result in lower than anticipated revenue and earnings for a particular period or in lower estimated revenue and earnings in future periods.

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### **We face a variety of risks in doing business with the U.S. and foreign governments, various state and local governments, and government agencies, including risks related to the procurement process, budget constraints and cycles, termination of contracts, and compliance with government contracting requirements**

Our customers include the U.S. government and a number of state and local governments and government agencies. There are a variety of risks in doing business with government entities, including:

*Procurement.* Contracting with public sector customers is highly competitive and can be time-consuming and expensive, requiring that we incur significant up-front time and expense without any assurance that we will win a contract.

*Budgetary Constraints and Cycles.* Demand and payment for our products and services are impacted by public sector budgetary cycles and funding availability, with funding reductions or delays adversely impacting public sector demand for our products and services.

*Termination of Contracts.* Public sector customers often have contractual or other legal rights to terminate current contracts for convenience or due to a default. If a contract is terminated for convenience, which can occur if the customer's needs change, we may only be able to collect fees for products or services delivered prior to termination and settlement expenses. If a contract is terminated because of default, we may not recover even those amounts, and we may be liable for excess costs incurred by the customer for procuring alternative products or services.

*Compliance with Government Contracting Requirements.* Government contractors are required to comply with a variety of complex laws, regulations, and contractual provisions relating to the formation, administration, or performance of government contracts that give public sector customers substantial rights and remedies, many of which are not typically found in commercial contracts. These may include rights with respect to price protection, the accuracy of information provided to the government, contractor compliance with socio-economic policies, and other terms that are particular to government contracts. U.S. government and state and local governments and government agencies routinely investigate and audit contractors for compliance with these requirements. If, as a result of an audit or review, it is determined that we have failed to comply with these requirements, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, cost associated with the triggering of price reduction clauses, fines, and suspensions or debarment from future government business, and we may suffer harm to our reputation.

Our customers also include a number of foreign governments and government agencies. Similar procurement, budgetary, contract, and audit risks also apply to our doing business with these entities. In addition, compliance with complex regulations and contracting provisions in a variety of jurisdictions can be expensive and consume significant management resources. In certain jurisdictions our ability to win business may be constrained by political and other factors unrelated to our competitive position in the market. Each of these difficulties could materially adversely affect our business and results of operations.

### **We depend on technology licensed to us by third parties, and the loss of this technology could impair our software, delay implementation of our offerings, or force us to pay higher license fees**

We license third-party technologies that we incorporate into our existing offerings. There can be no assurance that the licenses for such third-party technologies will not be terminated or that we will be able to license third-party software for future offerings. In addition, we may be unable to renegotiate acceptable third-party license terms or we may be subject to infringement liability if third-party software that we license is found to infringe intellectual property rights of others. Changes in or the loss of third-party licenses could lead to a material increase in the costs of licensing or to

our software offerings becoming inoperable or their performance being materially reduced, with the result that we may need to incur additional development costs to ensure continued performance of our offerings, and we may experience a decreased demand for our offerings.

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**If we are unable to recruit or retain skilled personnel, or if we lose the services of any of our key management personnel, our business, operating results, and financial condition could be materially adversely affected**

Our future success depends on our continuing ability to attract, train, assimilate, and retain highly skilled personnel. Competition for these employees is intense. We may not be able to retain our current key employees or attract, train, assimilate, or retain other highly skilled personnel in the future. For example, our restructuring activities may adversely impact our ability to attract or retain key employees. Our future success also depends in large part on the continued service of key management personnel, particularly Michael J. Saylor, our Chairman of the Board of Directors and Chief Executive Officer. If we lose the services of Mr. Saylor or other key personnel, or if we are unable to attract, train, assimilate, and retain the highly skilled personnel we need, our business, operating results, and financial condition could be materially adversely affected.

**The emergence of new industry standards may materially adversely affect the demand for our existing offerings**

The emergence of new industry standards in related fields may materially adversely affect the demand for our existing offerings. This could happen if new Web standards and technologies or new standards in the field of operating system support emerged that were incompatible with customer deployments of our software offerings. For example, if we are unable to adapt our software offerings on a timely basis to new standards in database access technology, the ability of our software offerings to access customer databases could be impaired.

**The nature of our software offerings makes them particularly vulnerable to undetected errors, or bugs, which could cause problems with how the offerings perform and which could, in turn, reduce demand for our offerings, reduce our revenue, and lead to product liability claims against us**

Software as complex as ours may contain errors and/or defects. Although we test our software offerings extensively, we have in the past discovered software errors in our offerings after their introduction. Despite testing by us and by our current and potential customers, errors may be found in new offerings or releases after commercial shipments begin. This could result in lost revenue, damage to our reputation, or delays in market acceptance, which could have a material adverse effect upon our business, operating results, and financial condition. We may also have to expend resources and capital to correct these defects.

Our agreements with customers typically contain provisions designed to limit our exposure to product liability, warranty, and other claims. It is possible, however, that these provisions may not be effective under the laws of certain domestic or international jurisdictions and we may be exposed to product liability, warranty, and other claims. A successful product liability claim against us could have a material adverse effect on our business, operating results, and financial condition.

**Changes in laws or regulations relating to privacy or the protection or transfer of personal data, or any actual or perceived failure by us or our third-party service providers to comply with such laws and regulations or applicable privacy policies, could materially adversely affect our business**

Aspects of our business, including our cloud services offerings and Usher, involve processing, storing, and transmitting personal data, which is subject to certain privacy policies, and certain federal, state, and foreign laws and regulations relating to privacy and data protection. The amount of customer and employee data that we store through our cloud services offerings, networks, and other systems, including personal data, is increasing. In recent years, the collection and use of personal data by companies have come under increased regulatory and public scrutiny. For example, in the United States, protected health information is subject to the Health Insurance Portability and

Accountability Act ( HIPAA ). HIPAA has been supplemented by the Health Information Technology for Economic and Clinical Health Act with the result of increased civil and criminal penalties for noncompliance. Under HIPAA, entities performing certain functions and creating, receiving, maintaining, or transmitting protected health information provided by covered entities and other business associates are directly subject to HIPAA. Our access to protected health information through our cloud services offerings triggers obligations to comply with certain privacy rules and data security requirements under HIPAA. Any systems failure or security breach that results in the release of, or unauthorized access to, personal data, or any failure or perceived failure by us or our third-party service providers to comply with applicable privacy policies or any applicable laws or regulations relating to privacy or data protection, could result in proceedings against us by governmental entities or others. Such proceedings could result in the imposition of sanctions, fines, penalties, liabilities, and/or governmental orders requiring that we change our data practices, any of which could have a material adverse effect on our business, operating results, and financial condition.

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Various federal, state, and foreign legislative, regulatory, or other governmental bodies may enact new or additional laws or regulations, or issue rulings that invalidate prior laws or regulations (such as the recent ruling by the European Court of Justice invalidating the U.S.-EU Safe Harbor Framework), concerning privacy and data protection that could materially adversely impact our business. Complying with these varying and changing requirements could cause us to incur substantial costs, require us to change our business practices, or limit our ability to provide certain products in certain jurisdictions, any of which could materially adversely affect our business and operating results. Additionally, the legislation and regulation regarding mobile data collection continue to evolve and if laws or regulations restricting or limiting the collection or use of mobile data are enacted, they may reduce demand for certain of our services or require changes to our business practices, which could materially adversely affect our business and operating results.

**If we or our third-party service providers experience a security breach and unauthorized parties obtain access to our customers' data, our data, or our cloud services offerings, networks, or other systems, our offerings may be perceived as not being secure, our reputation may be harmed, demand for our offerings may be reduced, our operations may be disrupted, we may incur significant legal liabilities, and our business could be materially adversely affected**

As part of our business, we process, store, and transmit our customers' information and data as well as our own, including in our cloud services offerings, networks, and other systems. There can be no assurance that any security measures that have been implemented will be effective against all security threats. For example, security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, fraudulent inducement of employees or customers to disclose sensitive information such as user names or passwords, and employee error or malfeasance. Such breach could result in someone obtaining unauthorized access to our customers' data, our data (including our proprietary information or trade secrets), or our cloud services offerings, networks, or other systems. Because there are many different security breach techniques and such techniques continue to evolve, we may be unable to anticipate attempted security breaches and implement adequate preventative measures. Third parties may also conduct attacks designed to temporarily deny customers access to our services. Any security breach or successful denial of service attack could result in a loss of customer confidence in the security of our offerings and damage to our brand, reducing the demand for our offerings and our revenue, disrupt our normal business operations, require us to spend material resources to correct the breach, expose us to legal liabilities including litigation and indemnity obligations, and materially adversely affect our operating results. These risks will increase as we continue to grow the number and scale of our cloud-based offerings and process, store, and transmit increasingly large amounts of our customers' information and data, which may include proprietary or confidential data or personal or identifying information.

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### **Our intellectual property is valuable, and any inability to protect it could reduce the value of our products, services, and brand**

We rely on a combination of copyrights, patents, trademarks, trade secrets, confidentiality procedures, and contractual commitments to protect our intellectual property. Despite our efforts, these measures can only provide limited protection. Unauthorized third parties may try to copy or reverse engineer portions of our products or otherwise obtain and use our intellectual property. Any patents owned by us may be invalidated, circumvented, or challenged. Any of our pending or future patent applications, whether or not being currently challenged, may not be issued with the scope of the claims we seek, if at all. Moreover, recent amendments to and developing jurisprudence regarding U.S. patent law may affect our ability to protect our intellectual property and defend against claims of patent infringement. In addition, the laws of some countries do not provide the same level of protection of our intellectual property as do the laws of the United States. If we cannot protect our intellectual property against unauthorized copying or use, we may not remain competitive.

### **Third parties may claim we infringe their intellectual property rights**

We periodically receive notices from others claiming we are infringing their intellectual property rights, principally patent and trademark rights. We expect the number of such claims will increase as we continue to expand our offerings and branding, the number of offerings and level of competition in our industry segments grow, the functionality of offerings overlap, and the volume of issued patents, patent applications, and trademark registrations continues to increase. Responding to any infringement claim, regardless of its validity, could:

be time-consuming, costly, and/or result in litigation;

divert management's time and attention from developing our business;

require us to pay monetary damages or enter into royalty and licensing agreements that we would not normally find acceptable;

require us to stop selling certain of our offerings;

require us to redesign certain of our offerings using alternative non-infringing technology or practices, which could require significant effort and expense;

require us to rename certain of our offerings or entities; or

require us to satisfy indemnification obligations to our customers.

Additionally, while we monitor our use of third-party software, including open source software, we cannot assure you that our processes for controlling such use in our products will be effective. If we inadvertently embed certain types of open source software into one or more of our products, or if third-party software that we license is found to infringe

intellectual property rights of others, we could subject ourselves to infringement liability and be required to re-engineer our products, to discontinue the sale of our products if re-engineering could not be accomplished on a timely or cost-effective basis, or to make available to certain third parties or generally available, in source code form, our proprietary code, any of which could materially adversely affect our business, operating results, and financial condition.

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If a successful infringement claim is made against us and we fail to develop or license a substitute technology or brand name, as applicable, our business, results of operations, financial condition, or cash flows could be materially adversely affected.

For example, in December 2011, we were sued by DataTern, which alleged that certain of our analytics products infringe its patents, and we have received indemnification requests from certain of our channel partners and customers who were also named as defendants in connection with this matter. This matter is described in further detail in this Quarterly Report on Form 10-Q under Part II. Item 1. Legal Proceedings.

### **Pending or future litigation could have a material adverse impact on our results of operation and financial condition**

In addition to intellectual property litigation, from time to time, we have been subject to other litigation. Regardless of the merits of any claims that may be brought against us, pending or future litigation could result in a diversion of management's attention and resources and we may be required to incur significant expenses defending against these claims. If we are unable to prevail in litigation we could incur substantial liabilities. Where we can make a reasonable estimate of the liability relating to pending litigation and determine that it is probable, we record a related liability. As additional information becomes available, we assess the potential liability and revise estimates as appropriate. However, because of uncertainties relating to litigation, the amount of our estimates could be wrong.

### **Because of the rights of our two classes of common stock, and because we are controlled by Michael J. Saylor, who beneficially owns the majority of our class B common stock, Mr. Saylor could transfer control of MicroStrategy to a third party without the approval of our Board of Directors or our other stockholders, prevent a third party from acquiring MicroStrategy, or limit your ability to influence corporate matters**

We have two classes of common stock: class A common stock and class B common stock. Holders of our class A common stock generally have the same rights as holders of our class B common stock, except that holders of class A common stock have one vote per share while holders of class B common stock have ten votes per share. As of October 22, 2015, holders of our class B common stock owned 2,035,184 shares of class B common stock, or 68.6% of the total voting power. Michael J. Saylor, our Chairman and Chief Executive Officer, beneficially owned 2,011,668 shares of class B common stock, or 67.8% of the total voting power, as of October 22, 2015. Accordingly, Mr. Saylor is able to control MicroStrategy through his ability to determine the outcome of elections of our directors, amend our certificate of incorporation and by-laws, and take other actions requiring the vote or consent of stockholders, including mergers, going-private transactions, and other extraordinary transactions and their terms.

Our certificate of incorporation allows holders of class B common stock to transfer shares of class B common stock, subject to the approval of stockholders possessing a majority of the outstanding class B common stock. Mr. Saylor or a group of stockholders possessing a majority of the outstanding class B common stock could, without the approval of our Board of Directors or our other stockholders, transfer voting control of MicroStrategy to a third party. Such a transfer of control could have a material adverse effect on our business, operating results, and financial condition. Mr. Saylor or a group of stockholders possessing a majority of the outstanding class B common stock will also be able to prevent a change of control of MicroStrategy, regardless of whether holders of class A common stock might otherwise receive a premium for their shares over the then current market price. In addition, this concentrated control limits stockholders' ability to influence corporate matters and, as a result, we may take actions that our non-controlling stockholders do not view as beneficial or that conflict with their interests. As a result, the market price of our class A common stock could be materially adversely affected.



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**We rely on the controlled company exemption from certain corporate governance requirements for NASDAQ-listed companies, which could make our class A common stock less attractive to some investors or otherwise materially adversely affect our stock price**

Because we qualify as a controlled company under the corporate governance rules for NASDAQ-listed companies, we are not required to have a majority of our Board of Directors be comprised of independent directors. Additionally, our Board of Directors is not required to have an independent compensation or nominating committee, or to have the independent directors exercise the nominating function. We also are not required to have the compensation of our executive officers be determined by a compensation committee of independent directors. In addition, we are not required to empower our Compensation Committee with the authority to engage the services of any compensation consultants, legal counsel, or other advisors, or to have the Compensation Committee assess the independence of compensation consultants, legal counsel, and other advisors that it engages.

In light of our status as a controlled company, our Board of Directors has determined not to establish an independent nominating committee or have its independent directors exercise the nominating function, and has elected instead to have the Board of Directors be directly responsible for nominating members of the board. A majority of our Board of Directors is currently comprised of independent directors, and our Board of Directors has established a compensation committee comprised entirely of independent directors. The Compensation Committee determines the compensation of our chief executive officer. However, our Board of Directors has authorized our chief executive officer to determine the compensation of executive officers other than himself, rather than having such compensation determined by the Compensation Committee, except that certain executive officer compensation that is intended to qualify as performance-based compensation for purposes of Section 162(m) of the Internal Revenue Code is determined by the Compensation Committee pursuant to the requirements of Section 162(m). Awards under our 2013 Equity Plan are also approved by the Compensation Committee. Additionally, while our Compensation Committee is empowered with the authority to retain and terminate outside counsel, compensation consultants, and other experts or consultants, it is not required to assess their independence.

Although currently a majority of our Board of Directors is comprised of independent directors and the Compensation Committee is comprised entirely of independent directors, we may elect in the future not to have independent directors constitute a majority of the Board of Directors or the Compensation Committee, have our chief executive officer's compensation determined by a compensation committee of independent directors, or have a compensation committee of the Board of Directors at all.

Accordingly, should the interests of our controlling stockholder differ from those of other stockholders, the other stockholders may not have the same protections that are afforded to stockholders of companies that are required to follow all of the corporate governance rules for NASDAQ-listed companies. Our status as a controlled company could make our class A common stock less attractive to some investors or otherwise materially adversely affect our stock price.

**Revenue recognition accounting pronouncements may materially adversely affect our reported results of operations**

We continuously review our compliance with all new and existing revenue recognition accounting pronouncements. In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance. See Note 2, Recent Accounting Standards, to the Consolidated Financial Statements in Part I. Item 1. Financial Statements of this Quarterly Report on Form 10-Q for further information regarding ASU 2014-09. We are currently evaluating the impact of this guidance on our consolidated financial position, results of operations, and cash flows. Depending upon

the outcome of these ongoing reviews and the potential issuance of further accounting pronouncements, implementation guidelines, and interpretations, we may be required to modify our reported results, revenue recognition policies, or business practices, which could materially adversely affect our results of operations.

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**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

During the three months ended September 30, 2015, we did not repurchase any equity securities registered by us pursuant to Section 12 of the Exchange Act. See Note 9, Treasury Stock, to the Consolidated Financial Statements in Part I. Item 1. Financial Statements for further information regarding the Company's share repurchase plan.

**Item 6. Exhibits**

We hereby file as part of this Quarterly Report on Form 10-Q the exhibits listed in the Index to Exhibits.

All other items not included in this Quarterly Report on Form 10-Q are omitted because they are not applicable or the answers thereto are none.

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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.

**MICROSTRATEGY INCORPORATED**

By: /s/ Michael J. Saylor  
Michael J. Saylor  
Chairman of the Board of Directors  
and Chief Executive Officer

By: /s/ Phong Le  
Phong Le  
Senior Executive Vice President &  
Chief Financial Officer

By: /s/ Douglas K. Thede  
Douglas K. Thede  
Senior Executive Vice President,  
Finance

Date: October 29, 2015

**Table of Contents****INDEX TO EXHIBITS**

| <b>Exhibit<br/>Number</b> | <b>Description</b>                                                                                                                                                                                                                                                                       |
|---------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3.1                       | Second Restated Certificate of Incorporation of the registrant (filed as Exhibit 3.1 to the registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2003 (File No. 000-24435) and incorporated by reference herein).                                         |
| 3.2                       | Amended and Restated By-Laws of the registrant (filed as Exhibit 3.1 to the registrant's Current Report on Form 8-K (File No. 000-24435) filed on January 30, 2015 and incorporated by reference herein).                                                                                |
| 4.1                       | Form of Certificate of Class A Common Stock of the registrant (filed as Exhibit 4.1 to the registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003 (File No. 000-24435) and incorporated by reference herein).                                           |
| 10.1                      | Summary of Compensation for Phong Le (set forth in Item 5.02 of the registrant's Current Report on Form 8-K filed on July 27, 2015, as amended by the registrant's Current Report on Form 8-K/A filed on September 14, 2015 (File Nos. 000-24435) and incorporated by reference herein). |
| 10.2                      | Amendment No. 3 to the MicroStrategy Incorporated 2013 Stock Incentive Plan (filed as Exhibit 10.1 to the registrant's Current Report on Form 8-K (File No. 000-24435) filed on October 26, 2015 and incorporated by reference herein).                                                  |
| 31.1                      | Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Chairman of the Board of Directors and Chief Executive Officer.                                                                                                                                                        |
| 31.2                      | Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Senior Executive Vice President & Chief Financial Officer.                                                                                                                                                             |
| 32.1                      | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                                                                                                                                  |
| 101.INS                   | XBRL Instance Document                                                                                                                                                                                                                                                                   |
| 101.SCH                   | XBRL Taxonomy Extension Schema                                                                                                                                                                                                                                                           |
| 101.CAL                   | XBRL Taxonomy Extension Calculation Linkbase                                                                                                                                                                                                                                             |
| 101.DEF                   | XBRL Taxonomy Extension Definition Linkbase                                                                                                                                                                                                                                              |
| 101.LAB                   | XBRL Taxonomy Extension Label Linkbase                                                                                                                                                                                                                                                   |
| 101.PRE                   | XBRL Taxonomy Extension Presentation Linkbase                                                                                                                                                                                                                                            |

Management contracts and compensatory plans or arrangements