

VEEVA SYSTEMS INC
Form 10-Q
September 08, 2016

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 July 31, 2016

or

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

For the transition period from _____ to _____.

Commission File Number: 001-36121

Veeva Systems Inc.

(Exact name of registrant as specified in its charter)

Delaware 20-8235463
(State or other jurisdiction of (IRS Employer

incorporation or organization) Identification No.)

4280 Hacienda Drive

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Pleasanton, California 94588

(Address of principal executive offices)

(925) 452-6500

(Registrant's telephone number, including area code)

N/A

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

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

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

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

Large accelerated filer

Accelerated filer

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

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

As of August 26, 2016, there were 101,205,941 shares of the Registrant's Class A common stock outstanding and 34,983,637 shares of the Registrant's Class B common stock outstanding.

VEEVA SYSTEMS INC.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements that are based on our beliefs and assumptions and on information currently available to us. Forward-looking statements include information concerning our possible or assumed future results of operations and expenses, business strategies and plans, trends, market sizing, competitive position, industry environment and potential growth opportunities and product capabilities, among other things. Forward-looking statements include all statements that are not historical facts and, in some cases, can be identified by terms such as “anticipates,” “believes,” “could,” “estimates,” “expects,” “intends,” “may,” “plans,” “potential,” “predicts,” “projects,” “seeks,” “would,” “tracking to,” “on track” or similar expressions and the negatives of those terms.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements, including those described in “Risk Factors,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this report. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Any forward-looking statement made by us in this report speaks only as of the date on which it is made. Except as required by law, we disclaim any obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

As used in this report, the terms “Veeva,” “Registrant,” “we,” “us,” and “our” mean Veeva Systems Inc. and its subsidiaries unless the context indicates otherwise.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.
VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except number of shares and par value)

	July 31, 2016 (Unaudited)	January 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 210,365	\$ 132,179
Short-term investments	269,190	214,024
Accounts receivable, net of allowance for doubtful accounts of \$431 and \$542, respectively	88,963	144,798
Prepaid expenses and other current assets	18,575	9,963
Total current assets	587,093	500,964
Property and equipment, net	47,195	47,469
Capitalized internal-use software, net	862	979
Goodwill	95,804	95,804
Intangible assets, net	43,386	47,500
Deferred income taxes, noncurrent	9,402	9,359
Other long-term assets	3,490	3,724
Total assets	\$ 787,232	\$ 705,799
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 6,384	\$ 4,600
Accrued compensation and benefits	12,382	12,451
Accrued expenses and other current liabilities	9,294	11,059
Income tax payable	3,337	750
Deferred revenue	176,718	157,419
Total current liabilities	208,115	186,279
Deferred income taxes, noncurrent	9,870	10,622
Other long-term liabilities	4,139	3,649
Total liabilities	222,124	200,550
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Class A common stock, \$0.00001 par value; 800,000,000 shares authorized,	1	1

98,860,696 and 87,359,026 issued and outstanding at July 31, 2016 and

January 31, 2016, respectively

Class B common stock, \$0.00001 par value; 190,000,000 shares authorized,

37,111,374 and 46,186,159 issued and outstanding at July 31, 2016 and

January 31, 2016, respectively

Additional paid-in capital	—	—
Accumulated other comprehensive income	395,386	361,691
Retained earnings	869	172
Total stockholders' equity	168,852	143,385
Total liabilities and stockholders' equity	565,108	505,249
	\$ 787,232	\$705,799

See Notes to Condensed Consolidated Financial Statements.

VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share data)

	Three Months Ended		Six Months Ended	
	July 31, 2016 (Unaudited)	2015	July 31, 2016	2015
Revenues:				
Subscription services	\$105,211	\$75,280	\$201,243	\$144,174
Professional services and other	26,136	22,827	49,868	43,856
Total revenues	131,347	98,107	251,111	188,030
Cost of revenues⁽¹⁾:				
Cost of subscription services	23,108	16,819	44,853	32,692
Cost of professional services and other	19,087	16,654	38,433	32,766
Total cost of revenues	42,195	33,473	83,286	65,458
Gross profit	89,152	64,634	167,825	122,572
Operating expenses⁽¹⁾:				
Research and development	23,563	15,255	45,636	28,212
Sales and marketing	28,908	18,057	55,631	33,553
General and administrative	12,859	8,969	24,930	17,529
Total operating expenses	65,330	42,281	126,197	79,294
Operating income	23,822	22,353	41,628	43,278
Other income (expense), net	(1,362)	(445)	1,385	318
Income before income taxes	22,460	21,908	43,013	43,596
Provision for income taxes	9,502	8,502	17,546	17,208
Net income	\$12,958	\$13,406	\$25,467	\$26,388
Net income attributable to Class A and Class B common				
stockholders, basic and diluted	\$12,957	\$13,390	\$25,465	\$26,357
Net income per share attributable to Class A and Class B common				
stockholders:				
Basic	\$0.10	\$0.10	\$0.19	\$0.20
Diluted	\$0.09	\$0.09	\$0.17	\$0.18
Weighted-average shares used to compute net income per share				
attributable to Class A and Class B common stockholders:				
Basic	135,126	131,799	134,531	131,455
Diluted	147,155	144,871	146,690	144,870
Other comprehensive income (loss):				
Net change in unrealized gains (losses) on available-for-sale	\$98	\$(76)	\$272	\$(79)

investments				
Net change in cumulative foreign currency translation gain	312	41	425	33
Comprehensive income	\$13,368	\$13,371	\$26,164	\$26,342

(1)

Includes stock-based compensation as follows:

Cost of revenues:

Cost of subscription services	\$288	\$136	\$497	\$247
Cost of professional services and other	1,507	973	2,685	1,715
Research and development	2,812	1,643	5,206	3,026
Sales and marketing	3,342	1,755	5,797	2,875
General and administrative	2,065	1,104	3,972	2,547
Total stock-based compensation	\$10,014	\$5,611	\$18,157	\$10,410

See Notes to Condensed Consolidated Financial Statements.

VEEVA SYSTEMS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Three Months Ended		Six Months Ended	
	July 31, 2016 (Unaudited)	2015	July 31, 2016	2015
Cash flows from operating activities				
Net income	\$ 12,958	\$ 13,406	\$ 25,467	\$ 26,388
Adjustments to reconcile net income to net cash provided by				
operating activities:				
Depreciation and amortization	3,470	1,344	6,875	2,368
Amortization of premiums on short-term investments	469	750	889	1,513
Stock-based compensation	10,014	5,611	18,157	10,410
Deferred income taxes	36	—	(802)	—
Bad debt expense (recovery)	90	245	(115)	238
Changes in operating assets and liabilities:				
Accounts receivable	(7,277)	1,995	55,950	25,531
Income taxes	1,264	(3,019)	1,644	(157)
Prepaid expenses and other current and long-term assets	(9,466)	(5,560)	(8,076)	(5,527)
Accounts payable	1,805	560	1,871	(200)
Accrued expenses and other current liabilities	1,800	1,673	(1,105)	337
Deferred revenue	(4,058)	(1,651)	19,299	(3,848)
Other long-term liabilities	641	(172)	1,052	(80)
Net cash provided by operating activities	11,746	15,182	121,106	56,973
Cash flows from investing activities				
Purchases of short-term investments	(116,219)	(67,078)	(183,959)	(167,915)
Maturities and sales of short-term investments	58,151	69,008	128,176	116,752
Purchases of property and equipment	(859)	(9,782)	(2,916)	(14,492)
Acquisitions, net of cash acquired	—	(7)	—	(9,994)
Purchases of intangible assets	—	(568)	—	(568)
Capitalized internal-use software development costs	(69)	(172)	(209)	(194)
Changes in restricted cash and deposits	109	2	103	3
Net cash used in investing activities	(58,887)	(8,597)	(58,805)	(76,408)
Cash flows from financing activities				
Proceeds from early exercise of common stock options	—	2	—	10
Proceeds from exercise of common stock options	3,183	1,608	4,528	2,770
Restricted stock units acquired to settle employee tax				
withholding liability	(11)	(2)	(12)	(6)
Excess tax benefits from employee stock plans	8,079	3,982	10,940	7,151
Net cash provided by financing activities	11,251	5,590	15,456	9,925

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Effect of exchange rate changes on cash and cash equivalents	313	40	429	33
Net change in cash and cash equivalents	(35,577)	12,215	78,186	(9,477)
Cash and cash equivalents at beginning of period	245,942	107,561	132,179	129,253
Cash and cash equivalents at end of period	\$210,365	\$119,776	\$210,365	\$119,776
Supplemental disclosures of other cash flow information:				
Cash paid for income taxes, net of refunds	\$9,316	\$13,350	\$12,281	\$15,992
Non-cash investing and financing activities:				
Changes in accounts payable and accrued liabilities related to				
property and equipment purchases	\$(98)	\$133	\$(787)	\$2,615
Vesting of early exercised stock options	\$10	\$18	\$26	\$35

See Notes to Condensed Consolidated Financial Statements.

VEEVA SYSTEMS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Business and Significant Accounting Policies

Description of Business

Veeva is a leading provider of industry cloud software and data solutions for life sciences companies. We were founded in 2007 on the premise that industry-specific cloud solutions could best address the operating challenges and regulatory requirements of the global life sciences industry. Our solutions are designed to meet the unique needs of life sciences companies regardless of size and to address their most strategic business functions. From research and development to commercialization, our solutions are designed to help our customers bring products to market faster and more efficiently, market and sell more effectively and maintain compliance with government regulations. We provide multichannel customer relationship management, regulated content and information management, master data management and data and data services that meet the specialized functional and compliance needs of life sciences companies. Recently, we announced that we will begin selling certain of our regulated content and information management applications to companies in regulated industries adjacent to life sciences. Our fiscal year end is January 31.

Principles of Consolidation and Basis of Presentation

These unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting and include the accounts of our wholly owned subsidiaries after elimination of intercompany accounts and transactions. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in Veeva's Annual Report on Form 10-K for the fiscal year ended January 31, 2016, filed on March 31, 2016. There have been no changes to our significant accounting policies described in the annual report that have had a material impact on our condensed consolidated financial statements and related notes.

The consolidated balance sheet as of January 31, 2016 included herein was derived from the audited financial statements as of that date. These unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations, our comprehensive income and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full fiscal year ending January 31, 2017 or any other period.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires us to make estimates, judgments and assumptions that affect the condensed consolidated financial statements and the notes thereto. These estimates are based on information available as of the date of the condensed consolidated financial statements. On a regular basis, management evaluates these estimates and assumptions. Significant items subject to such estimates and assumptions include, but are not limited to:

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- the best estimate of selling price of the deliverables included in multiple-deliverable revenue arrangements;
- the collectibility of our accounts receivable;
- the fair value of assets acquired and liabilities assumed for business combinations;
- the valuation of short-term investments and the determination of other-than-temporary impairments;
- the realizability of deferred income tax assets and liabilities;
- the fair value of our stock-based awards and related forfeiture rates; and
- the capitalization and estimated useful life of internal-use software development costs.

As future events cannot be determined with precision, actual results could differ significantly from those estimates.

Revenue Recognition

We derive our revenues primarily from subscription services fees and professional services fees. Subscription services revenues consist of fees from customers accessing our cloud-based software solutions and subscription or license fees for our data solutions. In addition, our acquired Zinc Ahead business had a limited number of perpetual license agreements with accompanying maintenance and hosting fees. We have included such on-going maintenance and hosting fees in our subscription services revenues. Professional services and other revenues consist primarily of fees from implementation services, configuration, data services, training and managed services related to our solutions. We commence revenue recognition when all of the following conditions are satisfied:

- there is persuasive evidence of an arrangement;
- the service has been or is being provided to the customer;
- the collection of the fees is reasonably assured; and
- the amount of fees to be paid by the customer is fixed or determinable.

Our subscription services arrangements are generally non-cancelable and do not provide for refunds to customers in the event of cancellations.

Subscription Services Revenues

Subscription services revenues are recognized ratably over the order term beginning when the solution has been provisioned to the customer. Our subscription arrangements are considered service contracts, and the customer does not have the right to take possession of the software. On-going maintenance and hosting fees for Zinc Ahead solutions are also recognized ratably over the accompanying maintenance and hosting term.

Professional Services and Other Revenues

The majority of our professional services arrangements are recognized on a time and materials basis. Professional services revenues recognized on a time and materials basis are measured monthly based on time incurred and contractually agreed upon rates. Certain professional services revenues are based on fixed fee arrangements and revenues are recognized based on the proportional performance method. In some cases, the terms of our time and materials and fixed fee arrangements may require that we defer the recognition of revenue until contractual conditions are met. Data services and training revenues are generally recognized as the services are performed.

Multiple Element Arrangements

We apply the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2009-13, Multiple—Deliverable Revenue Arrangements, to allocate revenues based on relative best estimated selling price to each unit of accounting in multiple element arrangements, which generally include subscriptions and professional services. Best estimated selling price of each unit of accounting included in a multiple element arrangement is based upon management's estimate of the selling price of deliverables when vendor specific objective evidence or third-party evidence of selling price is not available.

We enter into arrangements with multiple deliverables that generally include our subscription offerings and professional services. For these arrangements we must: (i) determine whether each deliverable has stand-alone value; (ii) determine the estimated selling price of each element using the selling price hierarchy of vendor specific objective evidence (VSOE) of fair value, third-party evidence (TPE) or best estimated selling price (BESP), as applicable; and (iii) allocate the total price among the various deliverables based on the relative selling price method.

In determining whether professional services and other revenues have stand-alone value, we consider the following factors for each consulting agreement: availability of the consulting services from other vendors, the nature of the consulting services and whether the professional services are required in order for the customer to use the subscription services. If stand-alone value cannot be established for a delivered item in a multiple-element arrangement, the delivered item is accounted for as a combined unit of accounting with the undelivered item(s).

We have established stand-alone value with respect to all of our offerings except professional services for the acquired Zinc Ahead business. As a result, we account for multiple element arrangements that include Zinc Ahead professional services as a combined unit of accounting and recognize the revenues from such professional services ratably over the term of the associated subscription services.

We have determined that we are not able to establish VSOE of fair value or TPE of selling price for any of our deliverables, and accordingly we use BESP for each deliverable in the arrangement. The objective of BESP is to estimate the price at which we would transact a sale of the service deliverables if the services were sold on a stand-alone basis. Revenue allocated to each deliverable is recognized when the basic revenue recognition criteria are met for each deliverable.

We determine BESP for our subscription services included in a multiple element arrangement by considering multiple factors including, but not limited to, stated subscription renewal rates offered to the customer to renew the service and other major groupings such as customer type and geography.

BESP for professional services considers the discount of actual professional services sold compared to list price, the experience level of the individual performing the service and the estimated location of the resources performing the services for professional services.

We allocate consideration proportionately based on established BESP and then recognize the allocated revenue over the respective delivery periods for each element.

Deferred Revenue

Deferred revenue includes amounts billed to customers for which the revenue recognition criteria have not been met. Deferred revenue primarily consists of billings or payments received in advance of revenue recognition from our subscription services, and to a lesser extent, professional services and other revenues described above, and is recognized as the revenue recognition criteria are met. We generally invoice our customers in annual, quarterly or monthly installments for the subscription services. Accordingly, the deferred revenue balance does not generally represent the total contract value of a subscription arrangement. Deferred revenue that will be recognized during the succeeding 12-month period is recorded as current deferred revenue and the remaining portion is recorded as noncurrent, which is in other long-term liabilities on the consolidated balance sheet.

Certain Risks and Concentrations of Credit Risk

Our revenues are derived from subscription services, professional services and other services delivered primarily to the life sciences industry. We operate in markets that are highly competitive and rapidly changing. Significant technological changes, shifting customer needs, the emergence of competitive products or services with new capabilities and other factors could negatively impact our operating results.

Our financial instruments that potentially subject us to concentration of credit risk consist primarily of cash and cash equivalents, short-term investments and trade accounts receivable. Our cash equivalents and short-term investments are held in safekeeping by large, credit-worthy financial institutions. We have established guidelines relative to credit ratings, diversification and maturities that seek to maintain safety and liquidity. Deposits in these financial institutions may significantly exceed federally insured limits.

We do not require collateral from our customers and generally require payment within 30 to 60 days of billing. We periodically evaluate the collectibility of our accounts receivable and provide an allowance for doubtful accounts as necessary, based on historical experience. Historically, such losses have not been material.

The following customers individually exceeded 10% of total accounts receivable as of the dates shown:

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	July	January
	31,	31,
	2016	2016
Customer 1 *		16%
Customer 2 *		15
Customer 3	12%	*
Customer 4	12	*

*Does not exceed 10%.

No single customer represented over 10% of total revenues in the condensed consolidated financial statements for the three and six months ended July 31, 2016 and 2015.

Recent Accounting Pronouncements

Stock-Based Compensation

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-09, "Compensation-Stock Compensation: Improvements to Employee Share-Based Payment". The guidance simplifies the accounting for share-based transactions, including the income tax consequences, classification of awards as either equity or liabilities on the balance sheet, and classification of employee taxes paid on statement of cash flows when an employer withholds shares for tax-withholding purposes. The new standard is effective for interim and annual periods beginning after December 15, 2016, and early adoption is permitted. We have elected not to early adopt. We are evaluating the impact of adopting this new accounting standard on our consolidated financial statements.

Leases

In February 2016, the FASB issued ASU 2016-02, "Leases". ASU 2016-02 requires that lease arrangements longer than twelve months result in an entity recognizing an asset and liability. The updated guidance is effective for interim and annual periods beginning after December 15, 2018, and early adoption is permitted. We are evaluating the impact of this new accounting standard on our consolidated financial statements and have not determined whether we will early adopt.

Financial Instruments

In January 2016, the FASB issued ASU 2016-1, "Financial Instruments." This guidance outlines the classification and measurement of financial instruments. The requirement to disclose the methods and significant assumptions used to estimate fair value is removed. In addition, financial assets and financial liabilities are to be presented separately in the notes to the financial statements, grouped by measurement category and form of financial asset. This standard will be effective for our fiscal year beginning in February 1, 2017, and early adoption is permitted. We do not expect this standard to have a material impact on our consolidated financial statements.

Business Combinations

In September 2015, the FASB issued ASU 2015-16, "Simplifying the Accounting for Measurement-Period Adjustments." This guidance requires the acquirer to recognize adjustments to provisional amounts identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings for changes in depreciation or amortization, or other income effects (if any) as a result of the change to the provisional amounts, calculated as if the accounting had been completed as of the acquisition date, must be recorded in the reporting period in which the adjustment amounts are determined rather than retrospectively. This standard will be applied prospectively to adjustments to provisional amounts that occur after the effective date. The Company adopted this standard on a prospective basis for our fiscal year beginning in February 1, 2016. This standard did not have a material impact on our consolidated financial statements.

Cloud Computing Arrangements

In April 2015, the FASB issued ASU 2015-05, "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." This guidance is intended to help entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement, primarily to determine whether the arrangement includes a sale or license of software. If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If the arrangement does not

include a software license, the customer should account for a cloud computing arrangement as a service contract. The Company adopted this standard on a prospective basis for our fiscal year beginning February 1, 2016. This standard did not have a material impact on our consolidated financial statements.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers." This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model requires revenue to be recognized when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. ASU 2014-09 supersedes the existing revenue recognition guidance in "Revenue Recognition (Topic 605)." This update should be applied retrospectively either to each prior reporting period presented in the financial statements, or only to the most current reporting period presented in the financial statements with a cumulative effect adjustment recorded in the retained earnings. In August 2015, the FASB issued ASU 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date." This Update defers the effective date of ASU 2014-09 for all entities by one year, although companies still have the option to begin applying the new guidance as of the original effective date. In accordance with the deferral, this guidance will be effective for our fiscal year beginning February 1, 2018. In May 2016, the FASB issued ASU 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients," which clarifies implementation guidance in ASU 2014-09 on assessing collectability, noncash consideration, presentation of sales tax and completed contracts and contract modifications at transition. We are evaluating the effect that these new accounting standards will have on our consolidated financial statements and related disclosures and have not selected a transition method yet. We have elected not to early adopt.

Note 2. Acquisitions

Our acquisitions are accounted for as business combinations. In accordance with authoritative guidance on business combination accounting, the assets and liabilities of the acquired companies were recorded as of the acquisition date, at their respective fair values, and are included within our condensed consolidated financial statements. The results of operations related to each company acquired have been included in our condensed consolidated statements of operations from the date of acquisitions. All acquisition-related transaction costs are expensed and reflected in general and administrative expenses on our condensed consolidated statements of comprehensive income for the periods presented.

Goodwill represents the excess of the purchase price over the fair value of the underlying net tangible and intangible assets and represents the future economic benefits of the customer relationships and data technology contributions in support of our data-related offerings. Goodwill is not deductible for U.S. tax purposes.

The fair values assigned to assets acquired and liabilities assumed are based on management's best estimates and assumptions as of the reporting date and are considered preliminary pending finalization of valuation analyses pertaining to intangible assets acquired, liabilities assumed and tax liabilities assumed including calculation of deferred tax assets and liabilities. Changes to amounts recorded as assets or liabilities may result in corresponding adjustments to goodwill during the measurement period (up to one year from the acquisition date).

Zinc Ahead

On September 29, 2015, we completed our acquisition of Mineral Newco Ltd., the ultimate parent company of Zinc Ahead Ltd, a company organized under the laws of the United Kingdom that is the ultimate parent company of Zinc Ahead Holdings Ltd, Zinc Ahead Ltd, Zinc Ahead Inc., Zinc Ahead PTY LTD and Zinc Ahead (Japan) KK (collectively, "Zinc Ahead"), in an all-cash transaction. Through a share purchase agreement our indirect subsidiary,

Veeva U.K. Holdings Limited, acquired all of the share capital of Zinc Ahead. Under the acquisition method of accounting, the total purchase price was allocated to Zinc Ahead's net tangible and intangible assets based upon their estimated fair values as of September 29, 2015.

The total closing consideration for the purchase was approximately \$119.9 million in cash. In addition, the agreement, as revised, calls for an amount payable over three years at a rate of one-third per year to employee shareholders and option holders of Zinc Ahead who remain employed with us. These payments have been accounted for as deferred compensation in the amount of \$4.8 million as of July 31, 2016 and will be recognized over the service period. Zinc Ahead was a provider of commercial content management solutions. We expect this acquisition to support the continued growth of our commercial content management solutions. Over time, we will seek to convert the end users of the Zinc Ahead solutions to our Veeva Vault PromoMats application. We had incurred \$2.2 million in acquisition-related transaction costs which are reflected in general and administrative expenses on our condensed consolidated statements of comprehensive income.

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

	Useful Lives of Intangible Assets	Fair Value
Purchase price		
Cash		\$ 119,935
Allocation of purchase price		
Cash		\$3,107
Accounts receivable		4,600
Other current and non-current assets		5,140
Deferred tax liabilities, net		(12,316)
Other current and non-current liabilities		(8,730)
Net liabilities		\$(8,199)
Customer contracts and relationships	10 years	\$31,823
Software	4.5 years	10,063
Brand	3.5 years	1,141
Purchased intangible assets		\$43,027
Goodwill		\$85,107
Total purchase price		\$ 119,935

We did not record any in-process research and development in connection with the Zinc Ahead acquisition.

The following unaudited pro forma information for the three months ended July 31, 2015, presents the combined results of operations for the periods presented as if the acquisition had been completed on February 1, 2015, the beginning of the comparable prior annual reporting period. The unaudited pro forma results include the amortization associated with preliminary estimates for the acquired intangible assets, changes to interest income for cash used in the acquisition, and exclude acquisition-related transaction costs and the associated tax impact on these unaudited pro forma adjustments.

The unaudited pro forma results do not reflect any cost saving synergies from operating efficiencies or the effect of the incremental costs incurred in integrating the two companies. Accordingly, these unaudited pro forma results are presented for informational purpose only and are not necessarily indicative of what the actual results of operations of the combined company would have been if the acquisition had occurred at the beginning of the period presented, nor are they indicative of future results of operations:

Periods Ended July 31, 2015

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(In thousands, except per share amounts, unaudited, pro forma)	Three Months	Six Months
Pro forma revenues	\$104,646	\$201,177
Pro forma net income	\$10,792	\$20,708
Pro forma net income per share attributable to Class A and Class B common stockholders:		
Basic	\$0.08	\$0.16
Diluted	\$0.07	\$0.14

Note 3. Short-Term Investments

At July 31, 2016, short-term investments consisted of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Asset-backed securities	\$ 16,660	\$ 35	\$ —	\$ 16,695
Commercial paper	16,062	—	—	16,062
Corporate notes and bonds	74,196	72	(23)	74,245
U.S. agency obligations	101,803	64	(12)	101,855
U.S. treasury securities	60,289	45	(1)	60,333
Total available-for-sale securities	\$ 269,010	\$ 216	\$ (36)	\$ 269,190

At January 31, 2016, short-term investments consisted of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Asset-backed securities	\$ 5,456	\$ —	\$ (2)	\$ 5,454
Commercial paper	5,970	—	—	5,970
Corporate notes and bonds	38,341	26	(40)	38,327
U.S. agency obligations	124,626	14	(54)	124,586
U.S. treasury securities	39,720	4	(37)	39,687
Total available-for-sale securities	\$ 214,113	\$ 44	\$ (133)	\$ 214,024

The following table summarizes the estimated fair value of our short-term investments, designated as available-for-sale and classified by the contractual maturity date of the securities as of the dates shown (in thousands):

	July 31, 2016	January 31, 2016
Due in one year or less	\$ 185,713	\$ 151,214
Due in greater than one year	83,477	62,810
Total	\$ 269,190	\$ 214,024

We have certain available-for-sale securities in a gross unrealized loss position, all of which have been in such position for less than 12 months. We review our debt securities classified as short-term investments on a regular basis to evaluate whether or not any security has experienced an other-than-temporary decline in fair value. We consider factors such as the length of time and extent to which the market value has been less than the cost, the financial position and near-term prospects of the issuer and our intent to sell, or whether it is more likely than not we will be required to sell the investment before recovery of the investment's amortized-cost basis. If we determine that an other-than-temporary decline exists in one of these securities, the respective investment would be written down to fair value. For debt securities, the portion of the write-down related to credit loss would be recognized to other income, net in our condensed consolidated statements of comprehensive income. Any portion not related to credit loss would be included in accumulated other comprehensive income (loss). There were no impairments considered other-than-temporary as of July 31, 2016 and January 31, 2016.

The following table shows the fair values and the gross unrealized losses of these available-for-sale securities aggregated by investment category as of July 31, 2016 (in thousands):

	Fair Value	Gross Unrealized Losses
Asset-backed securities	\$46	\$ —
Corporate notes and bonds	19,792	(23)
U.S. agency obligations	12,430	(12)
U.S. treasury securities	5,017	(1)

The following table shows the fair values and the gross unrealized losses of these available-for-sale securities aggregated by investment category as of January 31, 2016 (in thousands):

	Fair Value	Gross Unrealized Losses
Asset-backed securities	\$2,249	\$ (2)
Corporate notes and bonds	14,296	(40)
U.S. agency obligations	82,806	(54)
U.S. treasury securities	33,486	(37)

Note 4. Property and Equipment, Net

Property and equipment, net, consists of the following as of the dates shown (in thousands):

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	July 31, 2016	January 31, 2016
Land	\$3,040	\$3,040
Building	20,984	20,984
Land improvements and building improvements	14,230	14,106
Equipment and computers	6,649	5,910
Furniture and fixtures	6,879	6,453
Leasehold improvements	1,732	1,323
Construction in progress	239	—
	53,753	51,816
Less accumulated depreciation	(6,558)	(4,347)
Total property and equipment, net	\$47,195	\$47,469

Total depreciation expense was \$1.2 million and \$2.4 million for the three and six months ended July 31, 2016, respectively, and \$0.4 million and \$0.8 million for the three and six months ended July 31, 2015, respectively. Land is not depreciated.

Note 5. Capitalized Internal-Use Software

Capitalized internal-use software, net, consisted of the following as of the dates shown (in thousands):

	July 31, 2016	January 31, 2016
Capitalized internal-use software development costs	\$4,046	\$3,801
Less accumulated amortization	(3,184)	(2,822)
Capitalized internal-use software development costs, net	\$862	\$979

During the six months ended July 31, 2016, we capitalized \$0.2 million of internal-use software development costs. During the six months ended July 31, 2015, we capitalized \$0.2 million of internal-use software development costs.

Capitalized internal-use software amortization expense was \$0.2 million and \$0.4 million for the three and six months ended July 31, 2016, respectively, and \$0.2 million and \$0.4 million for the three and six months ended July 31, 2015, respectively.

Note 6. Intangible Assets

The following schedule presents the details of intangible assets as of July 31, 2016 (dollar amounts in thousands):

	July 31, 2016			Remaining Useful Life (in years)
	Gross Carrying Amount	Accumulated Amortization	Net	
Existing technology	\$3,880	\$ (2,345)	\$1,535	2.1
Database	4,939	(2,697)	2,242	2.7
Customer contracts and relationships	33,643	(3,460)	30,183	9.0
Software	10,867	(2,309)	8,558	3.7
Brand	1,141	(273)	868	2.7
	\$54,470	\$ (11,084)	\$43,386	

The following schedule presents the details of intangible assets as of January 31, 2016 (dollar amounts in thousands):

January 31, 2015

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	Gross			Remaining
	Carrying	Accumulated	Net	Useful
	Amount	Amortization		Life
				(in years)
Existing technology	\$3,880	\$ (1,957)	\$1,923	2.6
Database	4,939	(2,103)	2,836	3.0
Customer contracts and relationships	33,643	(1,693)	31,950	9.4
Software	10,867	(1,106)	9,761	4.2
Brand	1,141	(111)	1,030	3.2
	\$54,470	\$ (6,970)	\$47,500	

Amortization expense associated with intangible assets was \$2.1 million and \$4.1 million for the three and six months ended July 31, 2016, respectively, and \$0.7 million and \$1.1 million for the three and six months ended July 31, 2015, respectively.

The estimated amortization expense for intangible assets, for the next five years and thereafter is as follows (in thousands):

Period	Estimated Amortization Expense
Fiscal 2017	\$ 4,112
Fiscal 2018	7,791
Fiscal 2019	6,963
Fiscal 2020	6,062
Fiscal 2021	3,628
Thereafter	14,830
Total	\$ 43,386

Note 7. Accrued Expenses

Accrued expenses consisted of the following as of the dates shown (in thousands):

	July 31, 2016	January 31, 2016
Accrued commissions	\$1,908	\$2,798
Accrued bonus	1,806	2,957
Deferred compensation associated with Zinc Ahead	2,504	1,120
Accrued other compensation and benefits	6,164	5,576
Total accrued compensation and benefits	\$12,382	\$12,451
Accrued fees payable to salesforce.com	4,339	4,222
Accrued third-party professional services subcontractors' fees	591	1,152
Sales taxes payable	928	1,597
Other accrued expenses	3,436	4,088
Total accrued expenses and other current liabilities	\$9,294	\$11,059

Note 8. Fair Value Measurements

The carrying amounts of accounts receivable and other current assets, accounts payable and accrued liabilities approximate fair value due to their short-term nature.

Financial assets and financial liabilities recorded at fair value in the condensed consolidated financial statements are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, which are directly related to the amount of subjectivity associated with the inputs to the valuation of these

assets or liabilities are as follows:

Level 1—Observable inputs, such as quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, 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—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Financial assets and financial liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires management to make judgments and considers factors specific to the asset or liability.

The following table presents the fair value hierarchy for financial assets measured at fair value on a recurring basis as of July 31, 2016 (in thousands):

	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$22,969	\$—	\$ —	\$22,969
Commercial paper	—	10,447	—	10,447
Corporate notes and bonds	—	—	—	—
U.S. agency obligations	—	23,620	—	23,620
Short-term investments				
Asset-backed securities	—	16,695	—	16,695
Commercial paper	—	16,062	—	16,062
Corporate notes and bonds	—	74,245	—	74,245
U.S. agency obligations	—	101,855	—	101,855
U.S. treasury securities	—	60,333	—	60,333
Total	\$22,969	\$303,257	\$ —	\$326,226

The following table presents the fair value hierarchy for financial assets measured at fair value on a recurring basis as of January 31, 2016 (in thousands):

	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	\$28,087	\$—	\$ —	\$28,087
Corporate notes and bonds	—	11,396	—	11,396
U.S. agency obligations	—	3,002	—	3,002
Short-term investments				
Asset-backed securities	—	5,454	—	5,454
Commercial paper	—	5,970	—	5,970
Corporate notes and bonds	—	38,327	—	38,327
U.S. agency obligations	—	124,586	—	124,586
U.S. treasury securities	—	39,687	—	39,687
Total	\$28,087	\$228,422	\$ —	\$256,509

We determine the fair value of our security holdings based on pricing from our service provider and market prices from industry-standard independent data providers. The valuation techniques used to measure the fair value of financial instruments having Level 2 inputs were derived from non-binding consensus prices that are corroborated by observable market data or quoted market prices for similar instruments. Such market prices may be quoted prices in active markets for identical assets (Level 1 inputs) or pricing determined using inputs other than quoted prices that are observable either directly or indirectly (Level 2 inputs). We perform procedures to ensure that appropriate fair values are recorded such as comparing prices obtained from other sources.

Note 9. Income Taxes

For the three months ended July 31, 2016 and 2015, our effective tax rates were 42.3% and 38.8%, respectively. During the three months ended July 31, 2016 as compared to the prior year period, our effective tax rate increased primarily due to the establishment of a valuation allowance against certain deferred tax assets on loss carry-forwards that would likely not be realized by the Mederi AG entity. These deferred tax assets associated with the Mederi AG entity were recorded as part of our acquisition of the Qforma CrowdLink business in March 2015. The effective tax rate increase was partially offset by the benefit of the reenactment of the U.S. research and development tax credit.

For the six months ended July 31, 2016 and 2015, our effective tax rates were 40.8% and 39.5%, respectively. During the six months ended July 31, 2016 as compared to the prior year period, our effective tax rate increased primarily due to the establishment of a valuation allowance against certain deferred tax assets on loss carry-forwards that would likely not be realized by the Mederi AG entity. These deferred tax assets associated with the Mederi AG entity were recorded as part of our acquisition of the Qforma CrowdLink business in March 2015. The effective tax rate increase was partially offset by the benefit of the reenactment of the U.S. research and development tax credit.

Note 10. Stockholders' Equity
Stock Option Activity

A summary of stock option activity for the six months ended July 31, 2016 is as follows:

	Number of shares	Weighted average exercise price	Weighted average remaining contractual term (in years)	Aggregate intrinsic value
Options outstanding at January 31, 2016	18,549,702	\$ 5.01	6.8	\$359,306,108
Options granted	1,075,000	25.41		
Options exercised	(2,006,882)	2.27		
Options forfeited/cancelled	(212,452)	4.40		
Options outstanding at July 31, 2016	17,405,368	\$ 6.60	6.7	\$546,431,136
Options vested and exercisable at July 31, 2016	16,731,371	\$ 6.54	6.7	\$526,238,982
Options vested and exercisable at July 31, 2016 and expected to vest thereafter	5,333,997	\$ 5.17	6.1	\$175,053,298

During the three months ended July 31, 2016, we did not grant any stock options. The weighted average grant-date fair value of options granted was \$11.99 for the six months ended July 31, 2016 and \$12.40 and \$12.36 for the three and six months ended July 31, 2015, respectively.

As of July 31, 2016, there was \$37.0 million in unrecognized compensation cost, net of estimated forfeitures, related to unvested stock options granted under the 2007 Plan, 2012 Equity Incentive Plan and 2013 Equity Incentive Plan (2013 EIP). This cost is expected to be recognized over a weighted average period of 3.7 years.

As of July 31, 2016, we had authorized and unissued shares of common stock sufficient to satisfy exercises of stock options.

The total intrinsic value of options exercised was approximately \$42.6 million and \$57.9 million for the three and six months ended July 31, 2016.

Restricted Stock Units

A summary of restricted stock unit (RSU) activity for the six months ended July 31, 2016 is as follows:

	Unreleased Restricted Stock Units	Weighted average grant date fair value
Balance at January 31, 2016	2,219,425	\$ 26.80

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RSUs granted	1,876,140	26.85
RSUs vested	(420,845)	26.57
RSUs forfeited/cancelled	(202,939)	26.23
Balance at July 31, 2016	3,471,781	\$ 26.89

During the three and six months ended July 31, 2016, we issued 414,035 and 1,876,140 RSUs under the 2013 EIP with a weighted-average grant date fair value of \$31.82 and \$26.85, respectively.

As of July 31, 2016, there was a total of \$88.5 million in unrecognized compensation cost, net of estimated forfeitures, related to unvested RSUs. This cost is expected to be recognized over a weighted-average period of approximately 3.2 years.

Stock-Based Compensation

Compensation expense related to share-based transactions, including employee, consultant, and non-employee director stock option awards, is measured and recognized in the condensed consolidated financial statements based on fair value. The fair value of each option award is estimated on the grant date using the Black-Scholes option-pricing model. The stock-based compensation expense, net of forfeitures, is recognized using a straight-line basis over the requisite service periods of the awards, which is generally four to nine years. For restricted stock awards, fair value is based on the closing price of our common stock on the grant date.

Our option-pricing model requires the input of subjective assumptions, including the fair value of the underlying common stock, the expected term of the option, the expected volatility of the price of our common stock, risk-free interest rates, and the expected dividend yield of our common stock. The assumptions used in our option-pricing model represent management's best estimates. These estimates involve inherent uncertainties and the application of management's judgment. If factors change and different assumptions are used, our stock-based compensation expense could be materially different in the future.

The following table presents the weighted-average assumptions used to estimate the grant date fair value of options granted during the periods presented:

	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Volatility	—	45% – 46%	45% – 46%	45% – 46%
Expected term (in years)	—	5.50 – 6.32	5.50 – 6.31	5.50 – 6.32
Risk-free interest rate	—	1.69% – 1.84%	1.48% – 1.67%	1.69% – 1.84%
Dividend yield	—	0%	0%	0%

For the three and six months ended July 31, 2016 and 2015, we capitalized an immaterial amount of stock-based compensation as part of our internal-use software capitalization.

Early Exercise of Employee Options

We historically have allowed for the early exercise of options granted under the 2007 Stock Plan (2007 Plan) prior to vesting. Historically, all such early exercises have been through cash payment. The unvested shares are subject to our repurchase right at the original purchase price. The proceeds initially are recorded as an accrued liability from the early exercise of stock options, and reclassified to common stock as our repurchase right lapses. At July 31, 2016, the amount of unvested shares and the aggregate price for those shares that were subject to repurchase were immaterial. At January 31, 2016, there were 56,666 unvested shares which were subject to repurchase at an aggregate price of an

immaterial amount.

Note 11. Net Income per Share Attributable to Common Stockholders

We compute net income per share of Class A and Class B common stock using the two-class method required for participating securities. Prior to the date of our IPO in October 2013, we considered all series of our convertible preferred stock to be participating securities due to their non-cumulative dividend rights. Immediately prior to the completion of our IPO, all outstanding shares of convertible preferred stock converted to Class B common stock. Additionally, we consider unvested shares issued upon the early exercise of options to be participating securities as the holders of these shares have a non-forfeitable right to dividends in the event of our declaration of a dividend for common shares.

Under the two-class method, net income attributable to common stockholders is determined by allocating undistributed earnings, calculated as net income, less earnings attributable to participating securities.

The net income per share attributable to common stockholders is allocated based on the contractual participation rights of the Class A common stock and Class B common stock as if the income for the year has been distributed. As the liquidation and dividend rights are identical, the net loss attributable to common stockholders is allocated on a proportionate basis.

Basic net income per share of common stock is computed by dividing the net income attributable to common stockholders by the weighted-average number of shares of common stock outstanding during the period. All participating securities are excluded from the basic weighted-average shares of common stock outstanding. Unvested shares of common stock resulting from the early exercises of stock options are excluded from the calculation of the weighted-average shares of common stock until they vest as they are subject to repurchase until they are vested. The unvested shares of common stock resulting from early exercises of stock options accounted for all of our participating securities.

Diluted net income per share attributable to common stockholders is computed by dividing net income attributable to common stockholders by the weighted-average shares outstanding, including potentially dilutive shares of common equivalents outstanding during the period. The dilutive effect of potential shares of common stock are determined using the treasury stock method.

Undistributed net income for a given period is apportioned to participating securities based on the weighted-average shares of each class of common stock outstanding during the applicable period as a percentage of the total weighted-average shares outstanding during the same period.

For purposes of the diluted net income per share attributable to common stockholders calculation, unvested shares of common stock resulting from the early exercises of stock options and unvested options to purchase common stock are considered to be potentially dilutive shares of common stock. In addition, the computation of the fully diluted net income per share of Class A common stock assumes the conversion from Class B common stock, while the fully diluted net income per share of Class B common stock does not assume the conversion of those shares.

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The numerators and denominators of the basic and diluted EPS computations for our common stock are calculated as follows (in thousands, except per share data):

	Three Months Ended July 31,				Six Months Ended July 31,			
	2016	2015		2016	2015		2016	2015
	Class A	Class B	Class A	Class B	Class A	Class B	Class A	Class B
Basic								
Numerator								
Net income	\$9,381	\$3,577	\$7,450	\$5,956	\$17,787	\$7,680	\$14,292	\$12,096
Undistributed earnings allocated to								
participating securities	(1)	—	(9)	(7)	(1)	(1)	(17)	(14)
Net income attributable to common								
stockholders, basic	\$9,380	\$3,577	\$7,441	\$5,949	\$17,786	\$7,679	\$14,275	\$12,082
Denominator								
Weighted average shares used in								
computing net income per								
share attributable to common								
stockholders, basic	97,823	37,303	73,246	58,553	93,961	40,570	71,197	60,258
Net income per share attributable to common								
stockholders, basic	\$0.10	\$0.10	\$0.10	\$0.10	\$0.19	\$0.19	\$0.20	\$0.20
Diluted								
Numerator								
Net income attributable to common								
stockholders, basic	\$9,380	\$3,577	\$7,441	\$5,949	\$17,786	\$7,679	\$14,275	\$12,082
Reallocation as a result of conversion of								
Class B to Class A								
common stock:								
Net income attributable to common	3,577	—	5,949	—	7,679	—	12,082	—

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stockholders, basic								
Reallocation of net income to Class B								
common stock	—	767	—	671	—	1,474	—	1,322
Net income attributable to common								
stockholders, diluted	\$12,957	\$4,344	\$13,390	\$6,620	\$25,465	\$9,153	\$26,357	\$13,404
Denominator								
Number of shares used for basic EPS								
computation	97,823	37,303	73,246	58,553	93,961	40,570	71,197	60,258
Conversion of Class B to Class A common								
stock	37,303	—	58,553	—	40,570	—	60,258	—
Effect of potentially dilutive common								
shares	12,029	12,029	13,072	13,072	12,159	12,159	13,415	13,415
Weighted average shares used in								
computing net income per share attributable to common								
stockholders, diluted	147,155	49,332	144,871	71,625	146,690	52,729	144,870	73,673
Net income per share attributable to								
common stockholders, diluted	\$0.09	\$0.09	\$0.09	\$0.09	\$0.17	\$0.17	\$0.18	\$0.18

Potential common share equivalents excluded where the inclusion would be anti-dilutive are as follows:

	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Options and awards to purchase shares not included in the computation of diluted net income per share because their inclusion would be anti-dilutive	2,031,160	1,278,843	1,757,681	833,425

Note 12. Commitments and Contingencies

Litigation

Liabilities for loss contingencies arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment or remediation can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred.

From time to time, we may be involved in legal proceedings and subject to claims incident to the ordinary course of business. Although the results of such legal proceedings and claims cannot be predicted with certainty, we believe we are not currently a party to any legal proceedings, the outcome of which, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, cash flows or financial position. Regardless of the outcome, such proceedings can have an adverse impact on us because of defense and settlement costs, diversion of resources and other factors, and there can be no assurances that favorable outcomes will be obtained.

Value-Added Reseller Agreement

We have a value-added reseller agreement with salesforce.com, inc. for our use of the Salesforce Platform in combination with our developed technology to deliver certain of our multichannel customer relationship management applications, including hosting infrastructure and data center operations provided by salesforce.com. The agreement, as amended, requires that we meet minimum order commitments of \$500 million over the term of the agreement, which ends on September 1, 2025, including “true-up” payments if the orders we place with salesforce.com have not equaled or exceeded the following aggregate amounts within the timeframes indicated: (i) \$250 million for the period from March 1, 2014 to September 1, 2020 and (ii) the full amount of \$500 million by September 1, 2025. As of July 31, 2016, we remained obligated to pay fees of at least \$382.3 million prior to September 1, 2025 in connection with this agreement.

Service Outage

In May 2016, salesforce.com suffered a significant service outage with respect to a group of servers that hosts the Veeva CRM solution for 38 of our Veeva CRM customers. The outage resulted in unplanned system unavailability of up to 21 hours for the associated Veeva customers. Customers are allowed to claim service level credits under their contracts with us, and as of July 31, 2016, an immaterial amount has been claimed. We do not expect the impact to be material for any future period.

Note 13. Information about Geographic Areas

We track and allocate revenues by the principal geographic region of our customers’ end users rather than by individual country, which makes it impractical to disclose revenues for the United States or other specific foreign countries. Revenues by geographic area, as measured by the estimated location of the end users for subscription services revenues and the estimated location of the resources performing the services for professional services, were as follows for the periods shown below (in thousands):

	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
Revenues by geography				
North America	\$71,540	\$53,518	\$136,979	\$103,571
Europe and other	39,120	26,427	73,934	50,558
Asia Pacific	20,687	18,162	40,198	33,901
Total revenues	\$131,347	\$98,107	\$251,111	\$188,030

Long-lived assets by geographic area are as follows as of the periods shown below (in thousands):

	July 31, 2016	January 31, 2016
Long-lived assets by geography		
North America	\$44,555	\$45,163
Europe and other	1,772	1,827
Asia Pacific	868	479
Total long-lived assets	\$47,195	\$47,469

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

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our condensed consolidated financial statements and notes thereto appearing elsewhere in this report. In addition to historical condensed consolidated financial information, the following discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results could differ materially from those anticipated by these forward-looking statements as a result of many factors. We discuss factors that we believe could cause or contribute to these differences below and elsewhere in this report, including those set forth under "Risk Factors" and "Special Note Regarding Forward-Looking Statements."

Overview

Veeva is a leading provider of industry cloud software and data solutions for life sciences companies. We were founded in 2007 on the premise that industry-specific cloud solutions could best address the operating challenges and regulatory requirements of the global life sciences industry. Our solutions are designed to meet the unique needs of life sciences companies regardless of size and to address their most strategic business functions. From research and development to commercialization, our solutions are designed to help our customers bring products to market faster and more efficiently, market and sell more effectively and maintain compliance with government regulations.

Veeva CRM was our first commercially available solution and has made up the vast majority of our revenue historically. In our fiscal year ended January 31, 2016, we derived approximately 79% of our subscription services revenues and 74% of our total revenues from our core sales automation solution, Veeva CRM, and our newer multichannel customer relationship management applications that complement Veeva CRM. The contribution of subscription services revenues and total revenues associated with Veeva Vault, Veeva Network master data management solutions and Veeva's data offerings is expected to increase as a percentage of subscription services revenues and total revenue going forward. Additionally, we recently announced that we will begin selling certain of our Veeva Vault applications to companies in regulated industries adjacent to life sciences. However, we have less experience selling Veeva Vault, Veeva Network master data management solutions, Veeva's data offerings and our newer multichannel customer relationship management applications that complement Veeva CRM. Although the Veeva Vault solution, in particular, has begun to achieve market acceptance, to the extent that these more recently introduced solutions do not continue to achieve significant market acceptance, our business and results of operations may be adversely affected.

For our fiscal years ended January 31, 2016, 2015 and 2014, our total revenues were \$409.2 million, \$313.2 million and \$210.2 million, respectively, representing year-over-year growth in total revenues of 31% and 49% for our two most recent fiscal years. For our fiscal years ended January 31, 2016, 2015 and 2014, our subscription services revenues were \$316.3 million, \$233.1 million and \$146.6 million, respectively, representing year-over-year growth in subscription services revenues of 36% and 59% for our two most recent fiscal years. The growth rate of our total revenues and subscription services revenues may slightly decline in future periods. We generated net income of \$54.5 million, \$40.4 million and \$23.6 million for our fiscal years ended January 31, 2016, 2015 and 2014, respectively. As of January 31, 2016, 2015 and 2014, we served 400, 276 and 198 customers, respectively. With respect to our major product lines, our customer totals for each product line as of January 31, 2016, were 212 for Veeva CRM, 219 for Veeva Vault, 35 for Veeva Network Customer Master, and 62 for Veeva OpenData data and data services. A single customer may be counted in more than one product line if the customer has purchased multiple major product lines. Many of our Veeva Vault applications are used by smaller, earlier stage pre-commercial companies. Thus, the potential number of Veeva Vault customers is significantly higher than the potential number of customers that use our commercial solutions.

For the six months ended July 31, 2016 and 2015, our total revenues were \$251.1 million and \$188.0 million, respectively, representing period-over-period growth in total revenues of 34%. For the six months ended July 31, 2016

and 2015, our subscription services revenues were \$201.2 million and \$144.2 million, respectively, representing period-over-period growth in subscription services revenues of 40%. We generated net income of \$25.5 million and \$26.4 million for the six months ended July 31, 2016 and 2015, respectively.

Additionally, in September 2015, we completed our acquisition of the companies referred to as “Zinc Ahead” in an all-cash transaction. We are incorporating functionality from the Zinc Ahead products into our Veeva Vault PromoMats application and are migrating the Zinc Ahead customers to the Vault PromoMats application over time. While we expect this acquisition to support the continued growth of our commercial content management solutions, we may encounter difficulties integrating the Zinc Ahead business and we may not retain existing Zinc Ahead customers and key Zinc Ahead employees to the extent we expect, which could adversely affect our business.

Key Factors Affecting Our Performance

Investment in Growth. We have invested and intend to continue to invest aggressively in expanding the breadth and depth of our Industry Cloud for life sciences. We expect to continue to invest in research and development to expand existing solutions and build new solutions, sales and marketing to promote our solutions to new and existing customers and in existing and expanded geographies and industries, professional services to ensure the success of our customers' implementations of our solutions and other operational and administrative functions to support our expected growth. We anticipate that our headcount will increase as a result of these investments. We expect our total operating expenses will continue to increase over time, which, in some cases, could have a negative impact on our operating margin.

Adoption of Our Solutions by Existing and New Customers. Most of our customers initially deploy our solutions to a limited number of end users within a division or geography and may only initially deploy a limited set of our available solutions. Our future growth is dependent upon our existing customers' continued success and renewals of subscriptions to our solutions, expanded deployment of our solutions within their organizations, and the purchase of subscriptions to additional solutions. Our growth is also dependent on the adoption of our solutions by new customers.

Subscription Services Revenue Retention Rate. A key factor to our success is the renewal and expansion of our existing subscription agreements with our customers. We calculate our annual subscription services revenue retention rate for a particular fiscal year by dividing (i) annualized subscription revenue as of the last day of that fiscal year from those customers that were also customers as of the last day of the prior fiscal year by (ii) the annualized subscription revenue from all customers as of the last day of the prior fiscal year. Annualized subscription revenue is calculated by multiplying the daily subscription revenue recognized on the last day of the fiscal year by 365. This calculation includes the impact on our revenues from customer non-renewals, expanded deployment of our solutions within their organizations, deployments of additional solutions or discontinued use of solutions by our customers, and price changes for our solutions. Historically, the impact of price changes on our subscription services revenue retention rate has been minimal. For our fiscal years ended January 31, 2016, 2015 and 2014, our subscription services revenue retention rate was 125%, 138% and 166%, respectively.

Mix of Subscription and Professional Services Revenues. We believe our investments in professional services have driven customer success and facilitated the further adoption of our solutions by our customers. During the initial period of deployment by a customer, we generally provide a greater amount of configuration, implementation and training than later in the deployment. At the same time, many of our customers have historically purchased subscriptions for a limited set of their total potential end users or less than full adoption during their initial deployments. As a result of these factors, the proportion of total revenues for a customer associated with professional services is relatively high during the initial deployment period. Over time, as the need for professional services associated with user deployments decreases and the number of end users increases (as is often the case), we have observed and continue to expect the mix of total revenues to shift more toward subscription services revenues. As a result, we expect the proportion of our total revenues from subscription services to increase over time.

Components of Results of Operations

Revenues

We derive our revenues primarily from subscription services fees and professional services fees. Subscription services revenues consist of fees from customers accessing our cloud-based software solutions and subscription or license fees for our data solutions. In addition, Zinc Ahead had a limited number of perpetual license agreements with accompanying maintenance and hosting fees. We have included such on-going maintenance and hosting fees in our subscription services revenues. Professional services and other revenues consist primarily of fees from

implementation services, configuration, data services, training and managed services related to our solutions. For the six months ended July 31, 2016, subscription services revenues constituted 80% of total revenues and professional services and other revenues constituted 20% of total revenues.

We enter into master subscription agreements with our customers and count each distinct master subscription agreement that has not terminated or expired and that has orders for which we have recognized revenue in a quarter as a distinct customer for purposes of determining our total number of current customers as of the end of a quarter. We generally enter into a single master subscription agreement with each customer, although in some instances, affiliated legal entities within the same corporate family may enter into a separate master subscription agreement. Divisions, subsidiaries and operating units of our customers often place distinct orders for our subscription services under the same master subscription agreement, and we do not count such distinct orders as new customers for purposes of determining our total customer count. With respect to data services customers that have not purchased one of our software solutions, we count as a distinct customer the party to each agreement that has a known and recurring payment obligation. For purposes of determining our total customer count, we count each entity that uses a legacy Zinc Ahead product as a distinct customer if such entity is not otherwise a customer of ours.

New subscription orders typically have a one-year term and automatically renew unless notice of cancellation is provided in advance. If a customer adds end users or solutions to an existing order, such additional orders will generally be coterminus with the anniversary date of the initial order, and as a result, orders for additional end users or solutions will commonly have an initial term of less than one year. Subscription orders are generally billed at the beginning of the subscription commencement date in annual or quarterly increments. Because the term of orders for additional end users or solutions is commonly less than one year and payment terms may also be quarterly, the annualized value of such orders that we enter into with our customers will not be completely reflected in deferred revenue at any single point in time. We have also agreed from time to time and may agree in the future to allow customers to change the renewal dates of their orders to, for example, align more closely with a customer's annual budget process or to align with the renewal dates of other orders placed by other entities within the same corporate control group, or to change payment terms from annual to quarterly, or vice versa. Such changes typically result in an order of less than one year as necessary to align all orders to the desired renewal date and, thus, may result in a lesser increase to deferred revenue than if the adjustment had not occurred. Additionally, if a coterminus order of less than one year renews in the same fiscal year in which it was originally signed and has annual billing terms, the order will generate more deferred revenue in that fiscal year than the annual contract value of that order. Accordingly, we do not believe that change in deferred revenue or calculated billings, a metric commonly cited by financial analysts that is the sum of the change in deferred revenue plus revenue, are accurate indicators of future revenues for any given period of time. More recently and with respect to solutions other than our core sales automation solution, we have begun to enter into orders with terms of up to five years. Such multi-year orders are billed in annual or quarterly increments.

Subscription services revenues are recognized ratably over the order term beginning when the solution has been provisioned to the customer. Our subscription services agreements are generally non-cancelable during the term, although customers typically have the right to terminate their agreements for cause in the event of material breach. Subscription services revenues are affected primarily by the number of customers, the number of end users (or other subscription usage metric) at each customer that uses our solutions and the number of solutions subscribed to by each customer.

We utilize our own professional services personnel and, in certain cases, third-party subcontractors to perform our professional services engagements with customers. Our professional services engagements are primarily billed on a time and materials basis and revenues are typically recognized as the services are rendered. Certain professional services revenues are based on fixed fee arrangements and revenues are recognized based on the proportional performance method. In some cases, the terms of our time and materials and fixed fee arrangements may require that we defer the recognition of revenue until contractual conditions are met. In those circumstances, revenue recognition may be sporadic, based upon the achievement of such contractual conditions. Professional services revenues are affected primarily by our customers' demands for implementation services, configuration, data services, training and managed services in connection with our solutions. With respect to our acquired Zinc Ahead business, we have not established stand-alone value for professional services, and, therefore, we account for multiple element arrangements as a combined unit of accounting. As a result, professional services revenues for our Zinc Ahead business, when delivered as part of a multiple-element arrangement, are generally recognized ratably over the term of the associated subscription services.

Cost of Revenues

Cost of subscription services revenues for all of our solutions consists of expenses related to third-party data centers, personnel related costs associated with hosting our subscription services and providing support, including our data stewards, operating lease expense associated with computer equipment and software and allocated overhead, amortization expense associated with capitalized internal-use software related to our subscription services and amortization expense associated with purchased intangibles related to our subscription services. Cost of subscription services revenues for Veeva CRM and certain of our multichannel customer relationship management applications

also include fees paid to salesforce.com, inc. for our use of the Salesforce1 Platform and the associated hosting infrastructure and data center operations that are provided by salesforce.com. We intend to continue to invest additional resources in our subscription services to enhance our product offerings and increase our delivery capacity. For example, we may add or expand third-party data center capacity in the future and continue to make investments in the availability and security of our solutions. The timing of when we incur these additional expenses will affect our cost of revenues in absolute dollars in the affected periods.

Cost of professional services and other revenues consists primarily of employee-related expenses associated with providing these services, including salaries, benefits and stock-based compensation expense, the cost of third-party subcontractors, travel costs and allocated overhead. The cost of providing professional services is significantly higher as a percentage of the related revenues than for our subscription services due to the direct labor costs and costs of third-party subcontractors.

Operating Expenses

We accumulate certain costs such as building depreciation, office rent, utilities and other facilities costs and allocate them across the various departments based on headcount. We refer to these costs as “allocated overhead.”

Research and Development. Research and development expenses consist primarily of employee-related expenses, third-party consulting fees and allocated overhead, offset by any internal-use software development costs capitalized during the same period. We continue to focus our research and development efforts on adding new features and applications, increasing the functionality and enhancing the ease of use of our cloud-based applications.

Sales and Marketing. Sales and marketing expenses consist primarily of employee-related expenses, sales commissions, marketing program costs, amortization expense associated with purchased intangibles related to our customer contracts, customer relationships and brand, travel-related expenses and allocated overhead. Sales commissions and other program spend costs are expensed as incurred. Consequently, the recognition of this expense on our income statement generally precedes the recognition of the related revenue.

General and Administrative. General and administrative expenses consist of employee-related expenses for our executive, finance and accounting, legal, employee success, management information systems personnel and other administrative employees. In addition, general and administrative expenses include fees related to third-party legal counsel, fees related to third-part accounting, tax and audit services, acquisition-related transaction costs, other corporate expenses and allocated overhead.

Other Expense, Net

Other income, net consists primarily of transaction gains or losses on foreign currency, net of interest income and amortization of investments.

Provision for Income Taxes

Provision for income taxes consists of federal and state income taxes in the United States and income taxes in certain foreign jurisdictions. See note 9 of the notes to our condensed consolidated financial statements.

Results of Operations

The following tables set forth selected condensed consolidated statements of operations data and such data as a percentage of total revenues for each of the periods indicated:

	Three Months Ended		Six Months Ended	
	July 31, 2016	2015	July 31, 2016	2015
(in thousands)				
Consolidated Statements of Income Data:				
Revenues:				
Subscription services	\$105,211	\$75,280	\$201,243	\$144,174
Professional services and other	26,136	22,827	49,868	43,856
Total revenues	131,347	98,107	251,111	188,030
Cost of revenues⁽¹⁾:				
Cost of subscription services	23,108	16,819	44,853	32,692
Cost of professional services and other	19,087	16,654	38,433	32,766
Total cost of revenues	42,195	33,473	83,286	65,458
Gross profit	89,152	64,634	167,825	122,572
Operating expenses⁽¹⁾:				
Research and development	23,563	15,255	45,636	28,212
Sales and marketing	28,908	18,057	55,631	33,553
General and administrative	12,859	8,969	24,930	17,529
Total operating expenses	65,330	42,281	126,197	79,294
Operating income	23,822	22,353	41,628	43,278
Other income (expense), net	(1,362)	(445)	1,385	318
Income before income taxes	22,460	21,908	43,013	43,596
Provision for income taxes	9,502	8,502	17,546	17,208
Net income	\$12,958	\$13,406	\$25,467	\$26,388

(1) Includes stock-based compensation as follows:

Cost of revenues:				
Cost of subscription services	\$288	\$136	\$497	\$247
Cost of professional services and other	1,507	973	2,685	1,715
Research and development	2,812	1,643	5,206	3,026
Sales and marketing	3,342	1,755	5,797	2,875
General and administrative	2,065	1,104	3,972	2,547
Total stock-based compensation	\$10,014	\$5,611	\$18,157	\$10,410

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	Three Months Ended		Six Months Ended	
	July 31,		July 31,	
	2016	2015	2016	2015
Consolidated Statements of Income Data:				
Revenues:				
Subscription services	80.1 %	76.7 %	80.1 %	76.7 %
Professional services and other	19.9	23.3	19.9	23.3
Total revenues	100.0	100.0	100.0	100.0
Cost of revenues:				
Cost of subscription services	17.6	17.1	17.9	17.4
Cost of professional services and other	14.5	17.0	15.3	17.4
Total cost of revenues	32.1	34.1	33.2	34.8
Gross profit	67.9	65.9	66.8	65.2
Operating expenses:				
Research and development	17.9	15.5	18.2	15.0
Sales and marketing	22.0	18.4	22.2	17.9
General and administrative	9.8	9.1	9.9	9.3
Total operating expenses	49.7	43.0	50.3	42.2
Operating income	18.1	22.9	16.5	23.0
Other income (expense), net	(1.0)	(0.5)	0.6	0.2
Income before income taxes	17.1	22.4	17.1	23.2
Provision for income taxes	7.2	8.7	7.0	9.2
Net income	9.9 %	13.7 %	10.1 %	14.0 %

Revenues

	Three Months Ended			Six Months Ended		
	July 31,			July 31,		
	2016	2015	% Change	2016	2015	% Change
Revenues:						
Subscription services	\$105,211	\$75,280	40 %	\$201,243	\$144,174	40 %
Professional services and other	26,136	22,827	14	49,868	43,856	14
Total revenues	\$131,347	\$98,107	34	\$251,111	\$188,030	34
Percentage of revenues:						
Subscription services	80 %	77 %		80 %	77 %	
Professional services and other	20	23		20	23	
Total revenues	100 %	100 %		100 %	100 %	

Total revenues for the three months ended July 31, 2016 increased \$33.2 million from the same period in the prior year, of which \$29.9 million was from growth in subscription services revenues. Four percent of the increase in subscription services revenues was attributable to orders from existing customers that were placed on or prior to July 31, 2015 and the renewal of such orders through July 31, 2016, net of attrition. Ninety-six percent of the increase in subscription services revenues was attributable to new orders placed after July 31, 2015, which includes orders from the acquired Zinc Ahead business. New orders from existing customers consisted of expanded use of our solutions within a given customer and the addition of solutions not previously utilized by a given customer. The geographic mix of subscription services revenues, as measured by the estimated location of the end users for subscription services, were 53% from North America, 30% from Europe and other and 17% from Asia in the three months ended July 31, 2016 as compared to subscription services revenues of 53% from North America, 27% from Europe and other and 20% from Asia in the three months ended July 31, 2015.

Professional services and other revenues for the three months ended July 31, 2016 increased \$3.3 million from the same period in the prior year. The increase in professional services revenues was due primarily to new customers requesting implementation and deployment related professional services and existing customers requesting professional services related to expanding deployments or the deployment of newly purchased solutions. The geographic mix of professional services and other revenues, as measured by the estimated location of the resources performing the services, were 60% from North America, 29% from Europe and other and 11% from Asia in the three months ended July 31, 2016 as compared to professional services and other revenues of 60% from North America, 28% from Europe and other and 12% from Asia in the three months ended July 31, 2015.

Subscription services revenues were 80% of total revenues for the three months ended July 31, 2016, compared to 77% of total revenues for the three months ended July 31, 2015, reflecting the faster growth rate of our subscription services revenues as compared to the growth rate of our professional services and other revenues as our customers expanded their use of our solutions across new divisions, new geographies and new products.

Total revenues for the six months ended July 31, 2016 increased \$63.1 million from the same period in the prior year, of which \$57.1 million was from growth in subscription services revenues. Seventeen percent of the increase in subscription services revenues was attributable to orders from existing customers that were placed on or prior to July 31, 2015 and the renewal of such orders through July 31, 2016, net of attrition. Eighty-three percent of the increase in subscription services revenues was attributable to new orders placed after July 31, 2015, which includes orders from the acquired Zinc Ahead business. New orders from existing customers consisted of expanded use of our solutions within a given customer and the addition of solutions not previously utilized by a given customer. The geographic mix of subscription services revenues, as measured by the estimated location of the end users for subscription services, were 53% from North America, 30% from Europe and other and 17% from Asia in the six months ended July 31, 2016 as compared to subscription services revenues of 53% from North America, 27% from Europe and other and 20% from Asia in the six months ended July 31, 2015.

Professional services and other revenues for the six months ended July 31, 2016 increased \$6.0 million from the same period in the prior year. The increase in professional services revenues was due primarily to new customers requesting implementation and deployment related professional services and existing customers requesting professional services related to expanding deployments or the deployment of newly purchased solutions. The geographic mix of professional services and other revenues, as measured by the estimated location of the resources performing the services, were 61% from North America, 28% from Europe and other and 11% from Asia in the six months ended July 31, 2016 as compared to professional services and other revenues of 62% from North America, 27% from Europe and other and 11% from Asia in the six months ended July 31, 2015.

Subscription services revenues were 80% of total revenues for the six months ended July 31, 2016, compared to 77% of total revenues for the six months ended July 31, 2015, reflecting the faster growth rate of our subscription services revenues as compared to the growth rate of our professional services and other revenues as our customers expanded their use of our solutions across new divisions, new geographies and new products.

Cost of Revenues and Gross Profit

Three Months Ended			Six Months Ended		
July 31, 2016	2015	% Change	July 31, 2016	2015	

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	(dollars in thousands)						% Change	
Cost of revenues:								
Cost of subscription services	\$23,108	\$16,819	37	%	\$44,853	\$32,692	37	%
Cost of professional services and other	19,087	16,654	15		38,433	32,766	17	
Total cost of revenues	\$42,195	\$33,473	26		\$83,286	\$65,458	27	
Gross margin percentage:								
Subscription services	78	%	78	%	78	%	77	%
Professional services and other	27		27		23		25	
Total gross margin percentage	68	%	66	%	67	%	65	%
Gross profit	\$89,152	\$64,634	38	%	\$167,825	\$122,572	37	%

Cost of revenues for the three months ended July 31, 2016 increased \$8.7 million from the same period in the prior year, of which \$6.3 million was related to cost of subscription services. The increase in cost of subscription services was primarily due to an increase in the number of end users of our subscription services, which drove an increase of \$1.7 million in fees paid to salesforce.com, a \$1.6 million increase in third-party data center costs, and an increase \$1.3 million in employee compensation-related costs (which includes the impact of an increase of \$0.2 million in stock-based compensation). The increase in employee compensation-related costs is primarily driven by an increase in headcount during the period, including headcount from the acquired Zinc Ahead business. We expect cost of subscription services revenues to increase in absolute dollars in the near term, as we renew existing orders and enter into new orders for our subscription services which may result in increased fees paid to salesforce.com and costs for additional third-party data center capacity. In addition, we expect cost of subscription services revenues to decrease as a percentage of subscription services revenues in the near term, as we receive a greater proportion of our subscription services revenues from our product offerings that have slightly higher gross margins, including our Veeva Vault applications.

Cost of professional services and other revenues for the three months ended July 31, 2016 increased \$2.4 million from the same period in the prior year, primarily due to a \$2.6 million increase in employee compensation-related costs (which includes the impact of an increase of \$0.5 million in stock-based compensation), which was partially offset by a \$0.4 million decrease in third-party subcontractor costs. The increase in employee compensation-related costs is primarily driven by the increase in headcount during the period, including headcount from the acquired Zinc Ahead business. We expect cost of professional services and other revenues to increase as we add personnel to our professional services organization worldwide.

Gross profit as a percentage of total revenues for the three months ended July 31, 2016 and 2015 was 68% and 66%, respectively. The increases compared to the prior periods is largely due to an increase in the proportion of total revenues attributable to subscription services revenues as compared to professional services and other revenues, which have higher gross margins, and the continued growth of Veeva Vault, Veeva Network master data management solutions, and our newer multichannel customer relationship management applications that compliment Veeva CRM, all of which have slightly higher subscription services gross margins than our core Veeva CRM application.

Cost of revenues for the six months ended July 31, 2016 increased \$17.8 million from the same period in the prior year, of which \$12.2 million was related to cost of subscription services. The increase in cost of subscription services was primarily due to an increase in the number of end users of our subscription services, which drove an increase of \$3.4 million in fees paid to salesforce.com, a \$2.9 million increase in third-party data center costs, a \$2.4 million increase in employee compensation-related costs (which includes the impact of an increase of \$0.3 million in stock-based compensation), and a \$1.2 million increase in amortization of purchased intangibles. The increase in employee compensation-related costs is primarily driven by the increase in headcount during the period, including headcount from the acquired Zinc Ahead business.

Cost of professional services and other revenues for the six months ended July 31, 2016 increased \$5.7 million from the same period in the prior year, primarily due to a \$5.8 million increase in employee compensation-related costs (which includes the impact of an increase of \$1.0 million in stock-based compensation), which was partially offset by a decrease of \$0.9 million in third-party subcontractor costs. The increase in employee compensation-related costs is primarily driven by the increase in headcount during the period, including headcount from the acquired Zinc Ahead business.

Gross profit as a percentage of total revenues for the six months ended July 31, 2016 and 2015 was 67% and 65%, respectively. The increases compared to the prior periods is largely due to an increase in the proportion of total revenues attributable to subscription services revenues as compared to professional services and other revenues, which have higher gross margins, and the continued growth of Veeva Vault, Veeva Network master data management

solutions, and our newer multichannel customer relationship management applications that compliment Veeva CRM, all of which have slightly higher subscription services gross margins than our core Veeva CRM application.

Operating Expenses and Operating Margin

Operating expenses include research and development, sales and marketing and general and administrative expenses. As we continue to invest in our growth through hiring, and as we realize the full impact of the additional headcount and operating expenses associated with the acquired Zinc Ahead business, we expect operating expenses to increase in absolute dollars and as a percentage of revenue to continue for the foreseeable future, which may result in a slight decrease in our operating margin.

Research and Development

	Three Months Ended			Six Months Ended			
	July 31,			July 31,			
	2016	2015	% Change	2016	2015	% Change	
	(dollars in thousands)						
Research and development	\$23,563	\$15,255	54	% \$45,636	\$28,212	62	%
Percentage of total revenues	18	% 16	%	18	% 15	%	

Research and development expenses for the three months ended July 31, 2016 increased \$8.3 million from the same period in the prior year, primarily due to an increase of \$7.2 million in employee compensation-related costs (which includes the impact of an increase of \$1.2 million in stock-based compensation) resulting from increased headcount during the period. The expansion of our headcount in this area is primarily to support the increasing number of products that are under development across our solution offerings, and to a lesser extent headcount from the acquired Zinc Ahead business. We also had an increase in facility related expenses of \$0.5 million primarily resulting from the move into our new corporate headquarters in August 2015.

Research and development expenses for the six months ended July 31, 2016 increased \$17.4 million from the same period in the prior year, primarily due to an increase of \$14.5 million in employee compensation-related costs (which includes the impact of an increase of \$2.2 million in stock-based compensation) resulting from increased headcount during the period. The expansion of our headcount in this area is to support the increasing number of products that are under development across our solution offerings, and to a lesser extent headcount from the acquired Zinc Ahead business. We also had an increase in facility related expenses of \$1.0 million primarily resulting from the move into our new corporate headquarters in August 2015. We expect research and development expenses to increase in absolute dollars in the near term, primarily due to higher headcount as we continue to add research and development personnel and invest in our solutions.

Sales and Marketing

	Three Months Ended			Six Months Ended			
	July 31,			July 31,			
	2016	2015	% Change	2016	2015	% Change	
	(dollars in thousands)						
Sales and marketing	\$28,908	\$18,057	60	% \$55,631	\$33,553	66	%
Percentage of total revenues	22	% 18	%	22	% 18	%	

Sales and marketing expenses for the three months ended July 31, 2016 increased \$10.9 million from the same period in the prior year, primarily due to an increase of \$8.2 million in employee compensation-related costs (which includes the impact of an increase of \$1.2 million in sales commissions and an increase of \$1.6 million in stock-based compensation), a \$0.9 million increase in amortization expense primarily associated with the Zinc Ahead purchased intangibles related to our to customer contracts, customer relationships and brand, and a \$0.8 million increase in marketing program costs. The increase in employee compensation-related costs is primarily driven by increase in headcount during the period, including to a lesser extent headcount from the acquired Zinc Ahead business.

Sales and marketing expenses for the six months ended July 31, 2016 increased \$22.1 million from the same period in the prior year, primarily due to an increase of \$16.7 million in employee compensation-related costs (which includes the impact of an increase of \$2.6 million in sales commissions and an increase of \$2.9 million in stock-based compensation), a \$1.8 million increase in amortization expense primarily associated with the Zinc Ahead purchased intangibles related to our to customer contracts, customer relationships and brand, a \$1.0 million increase in travel-related costs, and a \$0.8 million increase in marketing program costs. The increase in employee compensation-related costs is primarily driven by increase in headcount during the period, including to a lesser extent headcount from the acquired Zinc Ahead business.

We expect sales and marketing expenses to continue to grow in absolute dollars in the near term, primarily due to employee-related expenses as we increase our headcount to support our sales and marketing efforts associated with our newer solutions and our continued expansion of our international sales capacity across all our solutions.

General and Administrative

	Three Months Ended			Six Months Ended			
	July 31,			July 31,			
	2016	2015	% Change	2016	2015	% Change	
	(dollars in thousands)						
General and administrative	\$ 12,859	\$ 8,969	43	% \$ 24,930	\$ 17,529	42	%
Percentage of total revenues	10	% 9	%	10	% 9	%	

General and administrative expenses for the three months ended July 31, 2016 increased \$3.9 million from the same period in the prior year, primarily due to increases of \$2.5 million in employee compensation-related costs (which includes the impact of an increase of \$1.0 million in stock-based compensation) and a \$0.6 million increase in deferred compensation associated with the acquired Zinc Ahead business. The increase in employee compensation-related costs is primarily driven by increase in headcount during the period, including to a lesser extent headcount from the acquired Zinc Ahead business.

General and administrative expenses for the six months ended July 31, 2016 increased \$7.4 million from the same period in the prior year, primarily due to increases of \$4.3 million in employee compensation-related costs (which includes the impact of an increase of \$1.4 million in stock-based compensation), a \$1.9 million increase in deferred compensation associated with the acquired Zinc Ahead business, and a \$0.6 million in expense for software subscriptions for internal use. The increase in employee compensation-related costs is primarily driven by increase in headcount during the period, including to a lesser extent headcount from the acquired Zinc Ahead business.

We expect general and administrative expenses to continue to grow in absolute dollars in the near term, primarily due to higher headcount and additional expenses, such as fees related to third-party legal counsel and fees related to third-party accounting, tax and audit services, as we continue to invest in our business.

Other Income (Expense), Net

	Three Months Ended			Six Months Ended			
	July 31,			July 31,			
	2016	2015	% Change	2016	2015	% Change	
	(dollars in thousands)						
Other income (expense), net	\$(1,362)	\$(445)	206	% \$ 1,385	\$ 318	336	%

Other expense, net for the three months ended July 31, 2016 increased \$0.9 million from the prior year period, primarily due to a \$1.1 million foreign currency loss, offset by \$0.3 million decrease in investment amortization. We

continue to experience foreign currency fluctuations primarily due to the volatility in the value of the U.S. Dollar against the Euro and British Pound Sterling and the impact resulting from the periodic re-measurement of our foreign currency balances that are denominated in currencies other than the functional currency of the entities in which they are recorded. Our results of operations are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Euro, British Pound Sterling and Japanese Yen. We may continue to experience favorable or adverse foreign currency impacts due to any additional volatility in these currencies.

Other income, net for the six months ended July 31, 2016 increased \$1.1 million from the prior year period, primarily due to an increase of \$0.7 million in foreign currency gain and a decrease of \$0.7 million in investment amortization, partially offset by a \$0.2 million decrease in interest income. The lower investment amortization compared to the prior year period was primarily attributable to lower balances in our short-term investments.

Provision for Income Taxes

	Three Months Ended			Six Months Ended			
	July 31,			July 31,			
	2016	2015	% Change	2016	2015	% Change	
	(dollars in thousands)						
Income before income taxes	\$22,460	\$21,908	3	% \$43,013	\$43,596	-1	%
Provision for income taxes	9,502	8,502	12	17,546	17,208	2	
Effective tax rate	42.3	% 38.8	%	40.8	% 39.5	%	

Our effective tax rate in all periods is the result of the mix of income earned in various tax jurisdictions that incur a broad range of income tax rates. The provision for income taxes differs from the tax computed at the U.S. federal statutory income tax rate due primarily to earnings considered as indefinitely reinvested in foreign operations, state taxes, the permanent reenactment of the U.S. research and development tax credit which was signed into law in December 2015, equity compensation and the U.S. domestic production activity deduction. Future effective tax rates could be adversely affected if earnings are lower than anticipated in countries where we have lower statutory tax rates, by unfavorable changes in tax laws and regulations or by adverse rulings in tax related litigation, as may be applicable. Differing tax rates in various jurisdictions could harm our results of operations and financial condition by increasing our overall tax rate.

For the three months ended July 31, 2016 and 2015, our effective tax rates were 42.3% and 38.8%, respectively. During the three months ended July 31, 2016 as compared to the prior year period, our effective tax rate increased 3.5% primarily due to the establishment of a valuation allowance against certain deferred tax assets on loss carry-forwards that would likely not be realized by the Mederi AG entity. The effective tax rate increase was partially offset by the benefit of the reenactment of the U.S. research and development tax credit.

For the six months ended July 31, 2016 and 2015, our effective tax rates were 40.8% and 39.5%, respectively. During the six months ended July 31, 2016 as compared to the prior year period, our effective tax rate increased 1.3% primarily due to the establishment of a valuation allowance against certain deferred tax assets on loss carry-forwards that would likely not be realized by the Mederi AG entity. The effective tax rate increase was partially offset by the benefit of the reenactment of the U.S. research and development tax credit.

We regularly assess the likelihood that our deferred income tax assets will be realized based on the realization guidance available. To the extent that we believe any amounts are not more likely than not to be realized, we record a valuation allowance to reduce the deferred income tax assets. For the Mederi AG entity, which we acquired in March 2015 as part of our acquisition of the Qforma CrowdLink business, we determined that certain German deferred tax assets associated with loss carry-forwards would likely not be realized. Therefore, we recorded a valuation allowance against those deferred tax assets in the three and six months ended July 31, 2016. We regularly assess the need for the valuation allowance on our deferred tax assets, and to the extent that we determine that an adjustment is needed, such adjustment will be recorded.

Non-GAAP Financial Measures

Regulation S-K Item 10(e), "Use of Non-GAAP Financial Measures in Commission Filings," defines and prescribes the conditions for use of non-GAAP financial measures. Our measures of non-GAAP operating income, non-GAAP net income and non-GAAP diluted net income per share each meet the definition of a non-GAAP financial measure.

Non-GAAP operating income and non-GAAP net income

We use the non-GAAP measures of non-GAAP operating income and non-GAAP net income to provide an additional view of operational performance by excluding certain expenses and benefits that are not directly related to performance in any particular period. In addition to our GAAP measures, we use these non-GAAP measures interna