

**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 March 31, 2020.

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 001-37468

**AppFolio, Inc.**

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

**Delaware**

*(State of incorporation or organization)*

**26-0359894**

*(I.R.S. Employer Identification No.)*

**50 Castilian Drive**

**Santa Barbara, California**

*(Address of principal executive offices)*

**93117**

*(Zip Code)*

**(805) 364-6093**

*(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 Website, 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, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

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

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

<b><u>Title of each class</u></b>	<b><u>Trading Symbol</u></b>	<b><u>Name of each exchange on which registered</u></b>
Class A Common Stock, \$0.0001 par value	APPF	NASDAQ Global Market

As of April 27, 2020, the number of shares of the registrant's Class A common stock outstanding was 16,712,280 and the number of shares of the registrant's Class B common stock outstanding was 17,536,442.

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## CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2020 (this "Quarterly Report"), includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which statements are subject to considerable risks and uncertainties. Forward-looking statements include all statements that are not statements of historical facts and can be identified by words such as "anticipates," "believes," "seeks," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "could," "will," "would" or similar expressions and the negatives of those expressions. Forward-looking statements also include the assumptions underlying or relating to such statements. In particular, forward-looking statements contained in this Quarterly Report relate to, among other things:

- our future or assumed financial condition, results of operations and liquidity;
- business forecasts and plans;
- trends affecting our business and industry, and the economy as a whole;
- capital needs and financing plans;
- capital resource allocation plans;
- share repurchase plans;
- research and product development plans;
- future products and Value+ services;
- growth in the size of our business and number of customers;
- strategic plans and objectives;
- the impact of acquisitions and investments;
- changes in the competitive environment;
- the outcome of legal proceedings or regulatory matters; and
- the impact of, and our response to, the novel coronavirus ("COVID-19") pandemic.

We caution you that the foregoing list may not include all of the forward-looking statements made in this Quarterly Report.

Our forward-looking statements are based on our management's current beliefs, assumptions and expectations about future events and trends, which affect or may affect our business, strategy, operations, financial performance or liquidity. Although we believe these forward-looking statements are based upon reasonable assumptions, they are subject to numerous known and unknown risks and uncertainties and are made in light of information currently available to us. Our actual financial condition and results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those discussed in the sections entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Risk Factors" in this Quarterly Report and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019 (our "Annual Report"), as well as in the other reports we file with the Securities and Exchange Commission (the "SEC"). You should read this Quarterly Report, and the other documents we file with the SEC, with the understanding that our actual future results may be materially different from the results expressed or implied by these forward-looking statements.

Moreover, we operate in an evolving environment. New risks and uncertainties emerge from time to time and it is not possible for our management to predict all risks and uncertainties, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual future results to be materially different from those expressed or implied by any forward-looking statements.

Forward-looking statements speak only as of the date they were made, and, except to the extent required by law or the rules of the NASDAQ Global Market, we undertake no obligation to update or review any forward-looking statement because of new information, future events or other factors.

We qualify all of our forward-looking statements by these cautionary statements.

**PART I. FINANCIAL INFORMATION**
**Item 1. Condensed Consolidated Financial Statements**

**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**  
**(in thousands, except par values)**

	March 31, 2020	December 31, 2019
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 56,779	\$ 15,813
Investment securities—current	7,952	22,876
Accounts receivable, net	9,617	7,562
Prepaid expenses and other current assets	18,362	15,540
Total current assets	92,710	61,791
Investment securities—noncurrent	6,676	12,089
Property and equipment, net	22,536	14,744
Operating lease right-of-use assets	26,750	27,803
Capitalized software, net	32,587	30,023
Goodwill	58,425	58,425
Intangible assets, net	20,121	21,377
Deferred taxes	27,212	27,574
Other long-term assets	6,410	6,276
Total assets	\$ 293,427	\$ 260,102
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities		
Accounts payable	\$ 2,509	\$ 1,927
Accrued employee expenses	11,833	17,758
Accrued expenses	11,419	10,833
Deferred revenue	5,732	4,600
Other current liabilities	5,636	11,139
Term loan, net—current portion	1,520	1,208
Total current liabilities	38,649	47,465
Operating lease liabilities	34,143	33,312
Revolving facility	49,000	—
Term loan, net	46,760	47,375
Total liabilities	168,552	128,152
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, \$0.0001 par value, 25,000 shares authorized and no shares issued and outstanding at March 31, 2020 and December 31, 2019	—	—
Class A common stock, \$0.0001 par value, 250,000 shares authorized at March 31, 2020 and December 31, 2019; 17,089 and 16,923 shares issued at March 31, 2020 and December 31, 2019, respectively; 16,670 and 16,552 shares outstanding at March 31, 2020 and December 31, 2019, respectively	2	2
Class B common stock, \$0.0001 par value, 50,000 shares authorized at March 31, 2020 and December 31, 2019; 17,536 and 17,594 shares issued and outstanding at March 31, 2020 and December 31, 2019, respectively	2	2
Additional paid-in capital	156,513	161,509
Accumulated other comprehensive income	165	33
Treasury stock, at cost, 419 and 371 shares of Class A common stock at March 31, 2020 and December 31, 2019, respectively	(25,756)	(21,562)
Accumulated deficit	(6,051)	(8,034)
Total stockholders' equity	124,875	131,950
Total liabilities and stockholders' equity	\$ 293,427	\$ 260,102

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(UNAUDITED)**  
**(in thousands, except per share amounts)**

	Three Months Ended March 31,	
	2020	2019
Revenue	\$ 72,495	\$ 57,091
Costs and operating expenses:		
Cost of revenue (exclusive of depreciation and amortization)	28,961	24,181
Sales and marketing	14,506	11,219
Research and product development	11,212	8,481
General and administrative	8,572	8,192
Depreciation and amortization	6,414	5,076
Total costs and operating expenses	69,665	57,149
Income (loss) from operations	2,830	(58)
Other income (expense), net	22	(1)
Interest expense, net	(494)	(497)
Income (loss) before provision for (benefit from) income taxes	2,358	(556)
Provision for (benefit from) income taxes	375	(4,281)
Net income	\$ 1,983	\$ 3,725
Net income per common share:		
Basic	\$ 0.06	\$ 0.11
Diluted	\$ 0.06	\$ 0.11
Weighted average common shares outstanding:		
Basic	34,175	33,913
Diluted	35,681	35,342

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(UNAUDITED)**  
**(in thousands)**

	<b>Three Months Ended March 31,</b>	
	<b>2020</b>	<b>2019</b>
Net income	\$ 1,983	\$ 3,725
Other comprehensive income:		
Changes in unrealized gains on investment securities	132	129
Comprehensive income	<u>\$ 2,115</u>	<u>\$ 3,854</u>

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**(UNAUDITED)**  
**(in thousands)**

	Common Stock		Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income	Treasury Stock	Accumulated Deficit	Total
	Class A		Class B						
	Shares	Amount	Shares	Amount					
<b>Balance at December 31, 2019</b>	16,552	\$ 2	17,594	\$ 2	\$ 161,509	\$ 33	\$ (21,562)	\$ (8,034)	\$ 131,950
Exercise of stock options	17	—	—	—	97	—	—	—	97
Stock-based compensation	—	—	—	—	1,365	—	—	—	1,365
Vesting of restricted stock units, net of shares withheld for taxes	91	—	—	—	(6,458)	—	—	—	(6,458)
Conversion of Class B stock to Class A stock	58	—	(58)	—	—	—	—	—	—
Other comprehensive income	—	—	—	—	—	132	—	—	132
Repurchase of common stock	(48)	—	—	—	—	—	(4,194)	—	(4,194)
Net income	—	—	—	—	—	—	—	1,983	1,983
<b>Balance at March 31, 2020</b>	<u>16,670</u>	<u>\$ 2</u>	<u>17,536</u>	<u>\$ 2</u>	<u>\$ 156,513</u>	<u>\$ 165</u>	<u>\$ (25,756)</u>	<u>\$ (6,051)</u>	<u>\$ 124,875</u>

	Common Stock		Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Treasury Stock	Accumulated Deficit	Total
	Class A		Class B						
	Shares	Amount	Shares	Amount					
<b>Balance at December 31, 2018</b>	15,789	\$ 2	18,109	\$ 2	\$ 157,898	\$ (178)	\$ (21,562)	\$ (44,316)	\$ 91,846
Exercise of stock options	14	—	—	—	90	—	—	—	90
Stock-based compensation	—	—	—	—	1,831	—	—	—	1,831
Vesting of restricted stock units, net of shares withheld for taxes	58	—	—	—	(2,572)	—	—	—	(2,572)
Vesting of early exercised shares	—	—	—	—	6	—	—	—	6
Conversion of Class B stock to Class A stock	38	—	(38)	—	—	—	—	—	—
Other comprehensive income	—	—	—	—	—	129	—	—	129
Net income	—	—	—	—	—	—	—	3,725	3,725
<b>Balance at March 31, 2019</b>	<u>15,899</u>	<u>\$ 2</u>	<u>18,071</u>	<u>\$ 2</u>	<u>\$ 157,253</u>	<u>\$ (49)</u>	<u>\$ (21,562)</u>	<u>\$ (40,591)</u>	<u>\$ 95,055</u>

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.



**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**  
**(in thousands)**

	Three Months Ended March 31,	
	2020	2019
<b>Cash from operating activities</b>		
Net income	\$ 1,983	\$ 3,725
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,414	5,076
Amortization of operating lease right-of-use assets	1,053	942
Deferred income taxes	362	(4,281)
Stock-based compensation	959	1,552
Other	(38)	27
Changes in operating assets and liabilities:		
Accounts receivable	(1,616)	(2,051)
Prepaid expenses and other current assets	(2,822)	(3,577)
Other assets	(148)	660
Accounts payable	(362)	100
Accrued employee expenses	(5,427)	(2,867)
Accrued expenses	726	1,580
Deferred revenue	693	268
Operating lease liabilities	784	(735)
Other liabilities	522	(124)
Net cash provided by operating activities	3,083	295
<b>Cash from investing activities</b>		
Purchases of available-for-sale investments	(649)	—
Proceeds from sales of available-for-sale investments	13,942	1,750
Proceeds from maturities of available-for-sale investments	7,250	2,250
Purchases of property, equipment and intangible assets	(7,992)	(1,030)
Additions to capitalized software	(6,822)	(4,658)
Cash paid in business acquisition, net of cash acquired	—	(54,004)
Net cash provided by (used in) investing activities	5,729	(55,692)
<b>Cash from financing activities</b>		
Proceeds from stock option exercises	97	90
Tax withholding for net share settlement	(6,458)	(1,315)
Payment of contingent consideration	(5,977)	—
Proceeds from issuance of debt	49,437	597
Principal payments on debt	(749)	(909)
Payment of debt issuance costs	—	(360)
Purchase of treasury stock	(4,194)	—
Net cash provided by (used in) financing activities	32,156	(1,897)
Net increase (decrease) in cash, cash equivalents and restricted cash	40,968	(57,294)
<b>Cash, cash equivalents and restricted cash</b>		
Beginning of period	16,247	74,506
End of period	\$ 57,215	\$ 17,212

**APPFOLIO, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**  
**(in thousands)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2020</b>	<b>2019</b>
<b>Noncash investing and financing activities</b>		
Purchases of property and equipment included in accounts payable and accrued expenses	\$ 4,251	\$ 445
Additions of capitalized software included in accrued and accrued employee expenses	687	391
Stock-based compensation capitalized for software development	406	338
Tax withholding for net share settlement included in accrued employee expenses	—	1,258
Purchase consideration for acquisitions included in other current liabilities	—	6,000

The following table presents a reconciliation of cash, cash equivalents and restricted cash reported within our Condensed Consolidated Balance Sheets to the total of the same such amounts shown above (in thousands):

	<b>March 31,</b>	
	<b>2020</b>	<b>2019</b>
Cash and cash equivalents	\$ 56,779	\$ 16,783
Restricted cash included in other assets	436	429
<b>Total cash, cash equivalents and restricted cash</b>	<b>\$ 57,215</b>	<b>\$ 17,212</b>

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

APPFOLIO, INC.

NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS

**1. Nature of Business**

AppFolio, Inc.'s (the "Company," "we," "us" or "our") mission is to revolutionize vertical industry businesses by providing great software and services. Today we offer industry-specific, cloud-based business software solutions, services and data analytics to the real estate market, which represents over 90% of our revenue, and, to a lesser extent, to the legal market. Although specific functionality varies by product, our core solutions address common business operations and interactions of businesses in our targeted verticals. In addition to our core solutions, we offer a range of optional, but often business-critical, Value+ services. Our Value+ services are built to enhance, automate and streamline processes and support workflows essential to our customers' businesses.

Our real estate software solutions provide our property management customers with a system of record to automate essential business processes, a system of engagement to enhance business interactions between our customers and their clients and other stakeholders, and a system of intelligence to leverage data to predict and optimize business workflows that enable superior customer experiences and increase efficiency across our customers' businesses. We also provide software solutions to the legal market that enable law firms to administer their practice and manage their caseloads more efficiently by centralizing case details in a single system of record and system of engagement.

The significant majority of our customers in the real estate market use our property management solutions. Our property management customers include third-party property managers and owner-operators who manage single- and multi-family residences, community associations, commercial properties, and student housing, as well as mixed real estate portfolios. Our legal customers are typically small law firms that directly and indirectly account for less than 10% of our annual revenue.

**2. Summary of Significant Accounting Policies**

***Basis of Presentation and Significant Accounting Policies***

The accompanying unaudited Condensed Consolidated Financial Statements were prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information. Certain information and disclosures normally included in consolidated financial statements prepared in accordance with GAAP have been condensed or omitted. Accordingly, these Condensed Consolidated Financial Statements should be read in conjunction with our audited consolidated financial statements and the related notes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019 ("Annual Report"), filed with the Securities and Exchange Commission ("SEC") on March 2, 2020. The year-end condensed balance sheet was derived from our audited consolidated financial statements. Our unaudited interim Condensed Consolidated Financial Statements include, in the opinion of management, all adjustments, consisting of normal and recurring items, necessary for the fair statement of our Condensed Consolidated Financial Statements. The operating results for the three months ended March 31, 2020 are not necessarily indicative of the results expected for the full year ending December 31, 2020.

***Reclassifications***

We reclassified certain amounts in our Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Cash Flows within the cash from operating activities section in the prior year to conform to the current year's presentation.

***Changes in Accounting Policies***

Except as described below under *Recently Adopted Accounting Pronouncements*, there have been no significant changes in our accounting policies from those disclosed in our annual consolidated financial statements and the related notes included in our Annual Report.

***Use of Estimates***

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Assets and liabilities which are subject to judgment and use of estimates include the fair value of assets and liabilities assumed in business combinations, fair value of financial instruments, capitalized software costs, period of benefit associated with deferred costs, incremental borrowing rate used to measure operating lease liabilities, the recoverability of goodwill and long-lived assets, income taxes, useful lives associated with property and equipment and intangible assets, contingencies, and valuation and assumptions underlying stock-based compensation and other equity instruments.

In December 2019, a novel coronavirus disease ("COVID-19") was reported and has spread globally, including to every state in the United States. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic, and on March 13, 2020, the United States government declared a national emergency with respect to COVID-19. COVID-19 has created and may continue to create significant uncertainty in global financial markets, which may reduce demand for our core solutions and/or Value+ services, impact the productivity of our workforce, reduce our access to capital, and harm our business and results of operations.

In light of the currently unknown ultimate duration and severity of COVID-19, we face a greater degree of uncertainty than normal in making the judgments and estimates needed to apply our significant accounting policies. The Company assessed certain accounting matters that generally require consideration of forecasted financial information in context with the information reasonably available to the Company and the unknown future impacts COVID-19 as of March 31, 2020 and through the date of this report. The accounting matters assessed included, but were not limited to, the Company's allowance for doubtful accounts and credit losses, the carrying value of the goodwill and other long-lived assets, incentive-based compensation and income taxes.

As of the date of our Condensed Consolidated Financial Statements, we are not aware of any specific event or circumstance that would require us to update our estimates or judgments or to revise the carrying value of our assets or liabilities. However, these estimates and judgments may change as new events occur and additional information is obtained, which may result in changes being recognized in our consolidated financial statements in future periods. While we considered the effects of COVID-19 in our estimates and assumptions, due to the current level of uncertainty over the economic and operational impacts of COVID-19 on our business, there may be other judgments and assumptions that were not currently considered. Such judgments and assumptions could result in a meaningful impact on our financial statements in future periods. Actual results could differ from those estimates and any such differences may have a material impact on our financial statements.

### **Net Income per Common Share**

Net income per common share was the same for shares of our Class A and Class B common stock because they are entitled to the same liquidation and dividend rights and are therefore combined in the table below. The following table presents a reconciliation of the weighted average number of shares of our Class A and Class B common stock used to compute net income per common share (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2020</b>	<b>2019</b>
Weighted average common shares outstanding	34,180	33,918
Less: Weighted average unvested restricted shares subject to repurchase	5	5
Weighted average common shares outstanding; basic	<u>34,175</u>	<u>33,913</u>
Plus: Weighted average options, restricted stock units and restricted shares used to compute diluted net income per common share	1,506	1,429
Weighted average common shares outstanding; diluted	<u>35,681</u>	<u>35,342</u>

For the three months ended March 31, 2020 and 2019, an aggregate of 135,000 and 362,000 shares, respectively, underlying performance-based stock options ("PSOs") and performance-based restricted stock units ("PSUs"), were not included in the computations of diluted and anti-dilutive shares as they are considered contingently issuable upon the satisfaction of pre-defined performance measures and their respective performance measures have not been met.

Restricted stock units ("RSUs") with anti-dilutive effect were excluded from the calculation of weighted average number of shares used to compute diluted net income per common share and they were not material for the three months ended March 31, 2020 and 2019.

### **Recently Adopted Accounting Pronouncements**

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which amends the current accounting guidance and requires the measurement of all expected losses based on historical experience, current conditions and reasonable and supportable forecasts. This guidance amends the accounting for credit losses for available-for-sale investment securities and purchased financial assets with credit deterioration. The adoption of this guidance did not have a material impact on our financial condition, results of operations, cash flows or disclosures.

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*, a series of amendments which align the requirements for capitalizing implementation costs incurred in a hosting arrangement that

is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by these amendments. The adoption of this guidance did not have a material impact on our financial condition, results of operations, cash flows or disclosures.

#### ***Recent Accounting Pronouncements Not Yet Adopted***

In December 2019, the FASB issued ASU No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes* ("ASU 2019-12"). This amendment was issued to simplify the accounting for income taxes by removing certain exceptions for recognizing deferred taxes, performing intraperiod allocation, and calculating income taxes in interim periods. Further, ASU 2019-12 adds guidance to reduce complexity in certain areas, including recognizing deferred taxes for tax basis goodwill and allocating taxes to members of a consolidated group. ASU 2019-12 is effective for public business entities for fiscal years, and interim periods within those years, beginning after December 15, 2020. We do not expect the adoption of this guidance to have a material impact on our financial condition, results of operations, cash flows or disclosures.

In March 2020, the FASB issued ASU No. 2020-04, *Facilitation of the Effects of Reference rate Reform on Financial Reporting*. This guidance is intended to provide temporary optional expedients and exceptions to the GAAP guidance on contract modifications and hedge accounting to ease the financial reporting burdens related to the expected market transition from the London Interbank Offered Rate ("LIBOR") and other interbank offered rates to alternative reference rates. This guidance is effective beginning March 12, 2020, and the Company may elect to apply the amendments prospectively through December 31, 2022. We are currently evaluating the effect of the adoption of this guidance on our financial condition, results of operations, cash flows and disclosures.

### **3. Business Combinations**

#### ***Acquisition of Dynasty***

On January 7, 2019, we acquired 100% of the voting equity interest of Dynasty Marketplace, Inc. ("Dynasty") for \$60.2 million. Dynasty is a provider of advanced AI solutions for the real estate market that automate leasing communications, replace manual tasks and help customers grow their portfolios.

The transaction was accounted for using the acquisition method and, as a result, assets acquired and liabilities assumed were recorded at their estimated fair values as of the acquisition date. Determining the fair value of assets acquired and liabilities assumed requires management to make significant judgments and estimates, including the selection of valuation methodologies and comparable companies, estimates of future revenue and cash flows, discount rates, and the software decay rate and database ramp up rate. The following table summarizes the final purchase price allocation (in thousands), as well as the estimated useful lives of the acquired intangible assets over which they are amortized on a straight-line basis, as this approximates the pattern in which economic benefits will be consumed:

	Amount (in thousands)	Estimated Useful Life (in years)
Total current assets	\$ 305	
Identified intangible assets:		
Technology	5,730	4.0
Database	4,710	10.0
Customer relationships	1,110	5.0
Backlog	470	1.0
Trademark & trade name	1,390	10.0
Non-compete agreement	7,340	5.0
Total intangible assets subject to amortization	20,750	6.0
Goodwill	42,877	Indefinite
Other noncurrent assets	35	
Total assets acquired	63,967	
Accrued and other liabilities	48	
Deferred tax liability, net	3,711	
Total liabilities assumed	3,759	
Purchase consideration	\$ 60,208	

Goodwill is mainly attributable to synergies expected from the acquisition and assembled workforce and is non-deductible for U.S. federal income tax purposes.

We incurred a total of \$291,000 in transaction costs related to the acquisition and expensed all transaction costs incurred during the period in which such service was received.

### ***Pro Forma Results***

The following unaudited pro forma information has been prepared for illustrative purposes only, and assumes that the aforementioned Dynasty acquisition occurred on January 1, 2018, and includes pro forma adjustments related to the amortization of acquired intangible assets, elimination of historical interest and amortization expense, income taxes, compensation arrangements, and the transaction costs incurred. The unaudited pro forma results have been prepared based on estimates and assumptions, which we believe are reasonable; however, they are not necessarily indicative of the consolidated results of operations had the acquisitions occurred at the beginning of the periods presented, or of future results of operations. The unaudited pro forma results are as follows (in thousands):

	Three Months Ended March 31,	
	2020	2019
Revenue	\$ 72,495	\$ 57,126
Net income (loss)	1,983	(546)

#### 4. Investment Securities and Fair Value Measurements

##### Investment Securities

Investment securities classified as available-for-sale consisted of the following at March 31, 2020 and December 31, 2019 (in thousands):

	March 31, 2020			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	\$ 1,597	\$ 2	\$ —	\$ 1,599
Agency securities	2,649	40	—	2,689
Treasury securities	10,205	135	—	10,340
Total available-for-sale investment securities	\$ 14,451	\$ 177	\$ —	\$ 14,628

	December 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	\$ 9,597	\$ 18	\$ (1)	\$ 9,614
Agency securities	11,101	17	—	11,118
Treasury securities	14,222	12	(1)	14,233
Total available-for-sale investment securities	\$ 34,920	\$ 47	\$ (2)	\$ 34,965

For available-for-sale debt securities in an unrealized loss position, we first assess whether we intend to sell, or whether it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either of these criteria is met, the security's amortized cost basis is written down to fair value through income. For securities in an unrealized loss position that do not meet these criteria, we evaluate whether the decline in fair value has resulted from credit loss or other factors. If this assessment indicates a credit loss exists, the credit-related portion of the loss is recorded as an allowance for losses on the security. No allowance for credit losses for available-for-sale investment securities was recorded as of March 31, 2020.

At March 31, 2020 and December 31, 2019, the contractual maturities of our investments did not exceed 36 months. The fair values of available-for-sale investment securities, by remaining contractual maturity, are as follows (in thousands):

	March 31, 2020		December 31, 2019	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 7,897	\$ 7,952	\$ 22,846	\$ 22,876
Due after one year through three years	6,554	6,676	12,074	12,089
Total available-for-sale investment securities	\$ 14,451	\$ 14,628	\$ 34,920	\$ 34,965

During the three months ended March 31, 2020 and 2019, we had sales and maturities (which include calls) of investment securities, as follows (in thousands):

	Three Months Ended March 31, 2020			
	Gross Realized Gains	Gross Realized Losses	Gross Proceeds from Sales	Gross Proceeds from Maturities
Corporate bonds	\$ 5	\$ —	\$ 4,006	\$ 4,000
Agency securities	24	—	7,878	1,250
Treasury securities	4	—	2,058	2,000
Total	\$ 33	\$ —	\$ 13,942	\$ 7,250

	Three Months Ended March 31, 2019			
	Gross Realized Gains	Gross Realized Losses	Gross Proceeds from Sales	Gross Proceeds from Maturities
Corporate bonds	\$ —	\$ (1)	\$ 1,750	\$ 2,250

Interest income, net of the amortization and accretion of the premium and discount, was \$0.1 million and \$0.2 million for the three months ended March 31, 2020 and 2019, respectively.

### Fair Value Measurements

#### Recurring Fair Value Measurements

Financial assets and financial liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The following tables summarize our financial assets measured at fair value on a recurring basis as of March 31, 2020 and December 31, 2019 by level within the fair value hierarchy (in thousands):

	March 31, 2020			Total Fair Value
	Level 1	Level 2	Level 3	
Cash equivalents:				
Money market funds	\$ 28,548	\$ —	\$ —	\$ 28,548
Available-for-sale investment securities:				
Corporate bonds	—	1,599	—	1,599
Agency securities	—	2,689	—	2,689
Treasury securities	10,340	—	—	10,340
<b>Total</b>	<b>\$ 38,888</b>	<b>\$ 4,288</b>	<b>\$ —</b>	<b>\$ 43,176</b>

	December 31, 2019			Total Fair Value
	Level 1	Level 2	Level 3	
Cash equivalents:				
Money market funds	\$ 337	\$ —	\$ —	\$ 337
Available-for-sale investment securities:				
Corporate bonds	—	9,614	—	9,614
Agency securities	—	11,118	—	11,118
Treasury securities	14,233	—	—	14,233
<b>Total</b>	<b>\$ 14,570</b>	<b>\$ 20,732</b>	<b>\$ —</b>	<b>\$ 35,302</b>

The carrying amounts of cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the short maturity of these items.

The estimated fair value of the \$50.0 million term loan issued by Wells Fargo Bank, National Association ("Wells Fargo"), as administrative agent, and the lenders that are parties thereto ("Term Loan") and the \$50.0 million revolving credit facility made available to us by Wells Fargo and the lenders that are parties thereto ("Revolving Facility," and together with the Term Loan, the "Credit Facility"), approximate their carrying values due to the variable interest rates. We consider the fair value of the Term Loan and the Revolving Facility to be Level 2 measurements as these debt instruments are not actively traded. We carry the Term Loan at face value less the unamortized discount. Refer to Note 8, *Long-Term Debt*, of our Condensed Consolidated Financial Statements for more information about our Term Loan and Revolving Facility.

There were no changes to our valuation techniques used to measure financial asset and financial liability fair values on a recurring basis during the three months ended March 31, 2020. The valuation techniques for the financial assets in the tables above are as follows:



*Cash Equivalents*

As of March 31, 2020 and December 31, 2019, cash equivalents include cash invested in money market funds with a maturity of three months or less. Fair value is based on market prices for identical assets.

*Available-for-Sale Investment Securities*

Our Level 2 securities were priced by a pricing vendor. The pricing vendor utilizes the most recent observable market information in pricing these securities or, if specific prices are not available for these securities, other observable inputs like market transactions involving comparable securities are used.

*Non-Recurring Fair Value Measurements*

Certain assets, including goodwill, intangible assets and our note receivable with SecureDocs, Inc., are also subject to measurement at fair value on a non-recurring basis using Level 3 measurement, but only when they are deemed to be impaired. For the three months ended March 31, 2020 and 2019, no impairments were identified on those assets required to be measured at fair value on a non-recurring basis.

**5. Internal-Use Software Development Costs**

Internal-use software development costs as of March 31, 2020 and December 31, 2019 were as follows (in thousands):

	March 31, 2020	December 31, 2019
Internal use software development costs, gross	\$ 88,204	\$ 81,475
Less: Accumulated amortization	(55,617)	(51,452)
Internal use software development costs, net	<u>\$ 32,587</u>	<u>\$ 30,023</u>

Capitalized software development costs were \$6.7 million and \$5.0 million for the three months ended March 31, 2020 and 2019, respectively. Amortization expense with respect to software development costs totaled \$4.2 million and \$3.0 million for the three months ended March 31, 2020 and 2019, respectively.

Future amortization expense with respect to capitalized software development costs as of March 31, 2020 is estimated as follows (in thousands):

Years Ending December 31,	
2020	\$ 12,283
2021	12,980
2022	6,935
2023	389
Total amortization expense	<u>\$ 32,587</u>

## 6. Intangible Assets

Intangible assets consisted of the following as of March 31, 2020 and December 31, 2019 (in thousands, except years):

	March 31, 2020			Weighted Average Useful Life in Years
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	
Customer relationships	\$ 3,070	\$ (1,438)	\$ 1,632	5.0
Database	8,330	(1,162)	7,168	10.0
Technology	10,541	(6,466)	4,075	5.0
Trademarks and trade names	2,690	(1,036)	1,654	6.0
Partner relationships	680	(680)	—	3.0
Non-compete agreements	7,400	(1,854)	5,546	5.0
Domain names	301	(277)	24	5.0
Patents	252	(230)	22	5.0
	<u>\$ 33,264</u>	<u>\$ (13,143)</u>	<u>\$ 20,121</u>	6.6

	December 31, 2019			Weighted Average Useful Life in Years
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	
Customer relationships	\$ 3,070	\$ (1,296)	\$ 1,774	5.0
Database	8,330	(954)	7,376	10.0
Technology	10,541	(6,074)	4,467	5.0
Trademarks & trade names	2,690	(898)	1,792	6.0
Partner relationships	680	(680)	—	3.0
Non-compete agreements	7,400	(1,484)	5,916	5.0
Domain names	301	(276)	25	5.0
Patents	252	(225)	27	5.0
Backlog	470	(470)	—	1.0
	<u>\$ 33,734</u>	<u>\$ (12,357)</u>	<u>\$ 21,377</u>	6.2

Amortization expense with respect to intangible assets totaled \$1.3 million and \$1.4 million for the three months ended March 31, 2020 and 2019, respectively. Future amortization expense with respect to intangible assets is estimated as follows (in thousands):

Years Ending December 31,	
2020	\$ 3,623
2021	4,727
2022	4,665
2023	3,060
2024	1,197
Thereafter	2,849
Total amortization expense	<u>\$ 20,121</u>

## 7. Leases

We have operating leases for our corporate offices and data centers. Our leases have remaining lease terms ranging from one to twelve years, some of which include options to extend the leases by up to 10 years. These options to extend have not been recognized as part of our operating lease right-of-use assets and lease liabilities as it is not reasonably certain that we will exercise

these options. Our lease agreements do not contain any residual value guarantees or material restrictive covenants. We have lease agreements with lease and non-lease components, which we have elected to combine for all asset classes. The total lease cost associated with our operating leases for the three months ended March 31, 2020 and 2019 was \$1.4 million and \$1.2 million, respectively.

Lease-related assets and liabilities were as follows at March 31, 2020 and December 31, 2019 (in thousands):

	March 31, 2020	December 31, 2019
<b>Assets</b>		
Prepaid expenses and other current assets	\$ 3,118	\$ 3,908
Operating lease right-of-use assets	26,750	27,803
<b>Liabilities</b>		
Other current liabilities	\$ 2,779	\$ 2,826
Operating lease liabilities	34,143	33,312
Total lease liabilities	<u>\$ 36,922</u>	<u>\$ 36,138</u>

Future minimum lease payments under non-cancellable leases as of March 31, 2020 were as follows (in thousands):

Years ending December 31,		
2020 <sup>(1)</sup>		\$ 1,663
2021 <sup>(1)</sup>		2,383
2022		4,085
2023		3,977
2024		3,908
Thereafter		29,590
Total future minimum lease payments		45,606
Less: imputed interest		(11,802)
Total <sup>(2)</sup>		<u>\$ 33,804</u>

<sup>(1)</sup> Future minimum lease payments are presented net of tenant improvement allowances of \$2.8 million and \$2.3 million, respectively.

<sup>(2)</sup> Total future minimum lease payments include the current portion of lease liabilities recorded in *Prepaid expenses and other current assets* of \$3.1 million which relates to certain of our leases for which the lease incentives to be received exceed the minimum lease payments to be paid over the next twelve months.

## 8. Long-Term Debt

### *Credit Agreement*

On December 24, 2018, we entered into Amendment Number Two to the Credit Agreement (the "Second Amendment") with Wells Fargo, as administrative agent, and the lenders that are parties thereto (as amended, the "Credit Agreement"). Under the terms of the Second Amendment, the lenders issued the Term Loan to us and increased the amount available under the Revolving Facility to \$50.0 million. The maturity date of the Term Loan and Revolving Facility is December 24, 2023. In addition, pursuant to the Second Amendment, we are permitted to make certain restricted junior payments, including, without limitation, repurchases of our common stock, and to enter into acquisitions with no value limitation on such acquisitions, so long as we maintain specified liquidity requirements and maintain specified leverage ratios.

The Second Amendment also modified certain financial covenants by, among other things, requiring us to maintain (i) an EBITDA to interest expense ratio of not less than 3.0 to 1.0, and (ii) a funded indebtedness to EBITDA ratio of not more than 3.5 to 1.0 (the "Required Leverage Ratio") (decreasing by 0.25 per year until the Required Leverage Ratio is 2.5 to 1.0); provided, however, that we are not required to maintain the foregoing ratios if our liquidity (defined as the sum of the remaining borrowing capacity under the Credit Agreement and available cash) has equaled or exceeded the greater of \$20.0 million and 20% of the sum of the outstanding principal amount of the Term Loan and commitments under the Revolving Facility. If we enter into an Acquisition

with a purchase price greater than or equal to \$20.0 million, then the Required Leverage Ratio will be increased by 0.5 for the 12-month period immediately following the consummation of such Acquisition.

The Credit Agreement contains customary affirmative, negative and financial covenants. The affirmative covenants require us to, among other things, disclose financial and other information to the lenders, maintain our business and properties, and maintain adequate insurance. The negative covenants restrict us from, among other things, incurring additional indebtedness, prepaying certain types of indebtedness, encumbering or disposing of our assets, making fundamental changes to our corporate structure, and making certain dividends and distributions. At March 31, 2020, we were in compliance with the financial covenants under the Credit Agreement.

Under the terms of the Second Amendment, borrowings under the Credit Agreement will bear interest at a fluctuating rate per annum equal to, at our option, (i) the adjusted LIBOR or (ii) an alternate base rate, in each case plus the applicable interest rate margin. Borrowings will fluctuate between adjusted LIBOR plus 1.5% per annum and adjusted LIBOR plus 2.0% per annum (or between the alternate base rate plus 0.5% per annum and the alternate base rate plus 1.0% per annum), based upon our leverage ratio.

Fees payable on the unused portion of the Revolving Facility will be 25 basis points per annum, unless the average usage of the Revolving Facility is equal to or less than \$30.0 million for the applicable period, in which case the fees on the unused portion of the Revolving Facility will be 375 basis points per annum.

As of March 31, 2020 and December 31, 2019 we had \$1.0 million and \$50.0 million, respectively, of available credit under our Revolving Facility. Outstanding borrowings under the Revolving Facility were \$49.0 million at March 31, 2020 and there were no outstanding borrowings under the Revolving Facility at December 31, 2019.

### **Debt Financing Costs**

As a result of the Second Amendment, we incurred \$0.4 million in financing fees that were capitalized and will be amortized over the remaining life of the related debt, \$0.2 million of which was related to the Term Loan and \$0.2 million of which was related to the Revolving Facility. Pursuant to GAAP, the Second Amendment is accounted for as a debt modification. As a result, the unamortized deferred debt financing costs related to the Revolving Facility prior to the Second Amendment were added to the \$0.2 million of deferred debt financing costs related to the Second Amendment and will be amortized over the remaining life of the Revolving Facility.

Debt financing costs are deferred and amortized, using the straight-line method, which approximates the effective interest method, for costs related to the Term Loan and the straight-line method for costs related to the Revolving Facility over the term of the debt arrangement; such amortization is included in interest expense in our Condensed Consolidated Statements of Operations. Amortization of deferred debt financing costs was not material for the three months ended March 31, 2020 or 2019. At March 31, 2020 and December 31, 2019, the remaining unamortized deferred debt financing costs were \$0.4 million, of which \$0.2 million was offset against debt. At March 31, 2020 and December 31, 2019, \$0.2 million and \$0.3 million, respectively, of the remaining unamortized deferred debt financing costs were recorded in *Prepaid expenses and other current assets* and other assets on our Condensed Consolidated Balance Sheets, as they pertained to the Revolving Facility.

The following is a summary of our long-term debt at March 31, 2020 (in thousands):

	March 31, 2020	December 31, 2019
Principal amounts due under Term Loan	\$ 48,438	\$ 48,750
Unamortized debt financing costs	(158)	(167)
Long-term debt, net of unamortized debt financing costs	<u>\$ 48,280</u>	<u>\$ 48,583</u>

Scheduled principal payments for the Term Loan at March 31, 2020 are as follows (in thousands):

Years Ending December 31,	
2020	\$ 938
2021	2,500
2022	2,500
2023	42,500
Total principal payments	<u>\$ 48,438</u>

## **9. Commitments and Contingencies**

### ***Legal Liability to Landlord Insurance***

We have a wholly owned subsidiary, Terra Mar Insurance Company, Inc., which was established to provide our customers with the option to purchase legal liability to landlord insurance. If our customers choose to use this insurance service, they are issued an insurance policy underwritten by our third-party service provider. The policy has a limit of \$100,000 per incident for each insured residence. We have entered into a reinsurance agreement with our third-party service provider and, as a result, we assume a 100% quota share of the legal liability to landlord insurance provided to our customers through our third-party service provider. We accrue for reported claims, and include an estimate of losses incurred but not reported by our property manager customers, in cost of revenue because we bear the risk related to all such claims. Our liability for reported claims and incurred but not reported claims as of March 31, 2020 and December 31, 2019 was \$2.0 million and \$1.8 million, respectively, and is included in other current liabilities on our Condensed Consolidated Balance Sheets.

Included in prepaid expenses and other current assets as of March 31, 2020 and December 31, 2019, are \$1.6 million and \$1.3 million, respectively, of deposits held with a third party related to requirements to maintain collateral for this insurance service.

### ***Legal Proceedings***

In July 2019, we received a Request for Information from the Civil Rights Division (Housing and Civil Enforcement Section) of the U.S. Department of Justice ("DOJ") requesting certain information relating to our compliance with the Servicemembers Civil Relief Act in connection with our tenant screening Value+ service. We continue to fully cooperate with the DOJ, and do not presently have sufficient information to predict the outcome of, or any potential costs or penalties associated with, the DOJ investigation.

In December 2018, we received a Civil Investigative Demand from the Federal Trade Commission ("FTC") requesting certain information relating to our compliance with the Fair Credit Reporting Act (the "FCRA") in connection with our tenant screening Value+ service. On April 30, 2020, the FTC staff informed us of its belief that there is a reasonable basis for asserting claims against us for our alleged failure to comply with certain sections of the FCRA that could result in monetary penalty and/or injunctive relief. We disagree with the stated belief of the FTC and will vigorously defend our position. We expect to continue to have discussions with the FTC with the goal of quickly resolving the matter. We are unable to predict the outcome of, or any potential costs or penalties associated with this matter at this time, although it is possible any costs or penalties could be material.

In addition, from time to time, we are involved in various other investigatory inquiries or legal proceedings arising from or related to matters incident to the ordinary course of our business activities, including actions with respect to intellectual property, employment, regulatory and contractual issues. Although the results of such investigatory inquiries and legal proceedings cannot be predicted with certainty, we believe that we are not currently a party to any investigatory inquiries or legal proceedings which, if determined adversely to us, would, individually or taken together, have a material adverse effect on our business, operating results, financial condition or cash flows.

### ***Indemnification***

In the ordinary course of business, we may provide indemnification of varying scope and terms to customers, vendors, investors, directors and officers with respect to certain matters, including, but not limited to, losses arising out of our breach of applicable agreements, services to be provided by us, or intellectual property infringement claims made by third parties. These indemnification provisions may survive termination of the underlying agreement and the maximum potential amount of future payments we could be required to make may not be subject to maximum loss clauses and may therefore be indeterminable. We have never paid a material claim, nor have any legal claims been brought against us in connection with these indemnification arrangements. As of March 31, 2020 and December 31, 2019, we had not accrued a liability for these indemnification obligations because we determined that the likelihood of incurring any payment obligation in connection with these indemnification arrangements is not probable or reasonably possible, and the amount or range of amounts of any such liability is not reasonably estimable.

## **10. Share Repurchase Program**

On February 20, 2019, our Board of Directors authorized a \$100.0 million share repurchase program (the "Program") relating to our outstanding shares of Class A common stock. Under the Program, share repurchases may be made from time to time, as directed by a Committee consisting of three Directors, in open market purchases or privately negotiated transactions at a repurchase price that the members of the Committee unanimously believe is below intrinsic value conservatively determined. The

Program does not obligate us to repurchase any specific dollar amount or number of shares, there is no expiration date for the Program, and it may be modified, suspended or terminated at any time and for any reason.

During the three months ended March 31, 2020, we repurchased a total of 48,002 shares of our Class A common stock through open market repurchases, and recorded a \$4.2 million reduction to stockholders' equity, which includes broker commissions. We did not repurchase any shares of our Class A common stock under the Program during the three months ended March 31, 2019.

## 11. Stock-Based Compensation

### Stock Options

A summary of activity in connection with our stock options for the three months ended March 31, 2020, is as follows (number of shares in thousands):

	Number of Shares	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Life in Years
Options outstanding at December 31, 2019	1,342	\$ 11.84	5.9
Options granted	—	—	
Options exercised	(17)	5.77	
Options cancelled/forfeited	(55)	23.80	
Options outstanding at March 31, 2020	<u>1,270</u>	<u>\$ 11.39</u>	<u>5.6</u>

During the three months ended March 31, 2020, 77,000 PSOs vested based on the achievement of 95% of the pre-established free cash flow performance target for the year ended December 31, 2019 and 40,000 PSOs vested based on the achievement of 115% of the pre-established gross margin target for the year ended December 31, 2019.

Our stock-based compensation expense for stock options for the three months ended March 31, 2020 was not material and for the three months ended March 31, 2019 was \$0.2 million. At March 31, 2020, the total estimated remaining stock-based compensation expense for unvested stock options was not material.

The fair value of stock options is estimated on their date of grant using the Black-Scholes option-pricing model. No stock options were granted during the three months ended March 31, 2020 or 2019.

### Restricted Stock Units

A summary of activity in connection with our RSUs for the three months ended March 31, 2020, is as follows (number of shares in thousands):

	Number of Shares	Weighted Average Grant Date Fair Value per Share
Unvested at December 31, 2019	646	\$ 52.42
Granted	103	109.60
Vested	(146)	21.92
Forfeited	(10)	50.19
Unvested at March 31, 2020	<u>593</u>	<u>\$ 69.93</u>

During the three months ended March 31, 2020, we granted 100,000 RSUs that are subject to time-based vesting in equal annual installments over four years, and 3,000 PSUs that are subject to vesting based on the achievement of a pre-established consolidated net revenue growth target for the year ending December 31, 2022, assuming continued employment throughout the performance period. The number of PSUs granted, as included in the above table, assumes achievement of the performance metric at 100% of the performance target. The actual number of shares to be issued at the end of the performance period will range from 0% to 100% of the initial target awards. Achievement of the performance metric between 100% and 150% of the performance target will result in a performance based cash bonus payment between 100% and 165% of the initial target awards.

During the three months ended March 31, 2020, 84,000 PSUs vested and 4,000 PSUs were cancelled based on the achievement of 95% of the pre-established free cash flow performance target for the year ended December 31, 2019.

Included in the unvested RSUs as of March 31, 2020 are 37,000 and 95,000 PSUs granted in 2019 and 2018, respectively. Of these PSUs, 54,000 are subject to vesting based on the achievement of a pre-established consolidated net revenue growth target for the year ending December 31, 2020, 49,000 are subject to vesting based on the achievement of a pre-established consolidated net revenue growth target for the year ending December 31, 2021, and 29,000 are subject to vesting based on the achievement of a pre-established consolidated net revenue growth target for the year ending December 31, 2022. The number of PSUs granted assumes achievement of the performance metric at 100% of the performance target. The actual number of shares to be issued at the end of the performance period will range from 0% to 100% of the initial target awards. Achievement of the performance metric between 100% and 150% of the performance target will result in a performance based cash bonus payment between 100% and 165% of the initial target awards.

We recognize expense for the PSUs based on the grant date fair value of the PSUs that we determine are probable of vesting. Adjustments to compensation expense are made each period based on changes in our estimate of the number of PSUs that are probable of vesting. Our stock-based compensation expense for the RSUs and PSUs for the three months ended March 31, 2020 and 2019 was \$1.2 million and \$1.6 million, respectively.

As of March 31, 2020, the total estimated remaining stock-based compensation expense for the RSUs and PSUs was \$26.1 million, which is expected to be recognized over a weighted average period of 2.5 years.

### Restricted Stock Awards

A summary of activity in connection with our restricted stock awards for the three months ended March 31, 2020 is as follows (number of shares in thousands):

	Number of Shares	Weighted Average Grant Date Fair Value per Share
Unvested at December 31, 2019	5	\$ 105.88
Granted	—	—
Vested	—	—
Forfeited	—	—
Unvested at March 31, 2020	5	\$ 105.88

We have the right to repurchase any unvested restricted stock awards subject to certain conditions. Restricted stock awards vest over a one-year period. We recognized stock-based compensation expense for restricted stock awards of \$0.1 million for each of the three months ended March 31, 2020 and 2019.

As of March 31, 2020, the total estimated remaining stock-based compensation expense for unvested restricted stock awards with a repurchase right was \$0.2 million, which is expected to be recognized over a weighted average period of 0.5 years.

## 12. Income Taxes

We calculate our provision for income taxes on a quarterly basis by applying an estimated annual effective tax rate to income from operations and by calculating the tax effect of discrete items recognized during the quarter.

For the three months ended March 31, 2020, we recorded income tax expense of \$0.4 million. The income tax expense recorded and the difference between the U.S. federal statutory rate of 21% was primarily due to the tax impact associated with stock-based compensation expense and research and development credits.

For the three months ended March 31, 2019, we recorded an income tax benefit of \$4.3 million. The tax benefit recorded is primarily due to changes in the deferred tax asset valuation allowance resulting from \$4.1 million of deferred tax liabilities acquired through the Dynasty acquisition. The acquired deferred tax liabilities are expected to provide a source of income to support realizability of our existing deferred tax assets.

There were no material changes to the Company's unrecognized tax benefits during the three months ended March 31, 2020 and the Company does not expect to have any significant changes to unrecognized tax benefits through the end of the fiscal year.

## 13. Revenue and Other Information

The following table presents our revenue categories for the three months ended March 31, 2020 and 2019 (in thousands):

	Three Months Ended March 31,	
	2020	2019
Core solutions	\$ 24,902	\$ 20,822
Value+ services	44,138	33,698
Other	3,455	2,571
Total revenue	\$ 72,495	\$ 57,091

During the three months ended March 31, 2020 and 2019, we recognized \$2.3 million and \$1.7 million of revenue, respectively, that were included in the deferred revenue balances at December 31, 2019 and 2018, respectively.

Our revenue is generated primarily from customers in the United States. All of our property and equipment is located in the United States.

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

*The following discussion and analysis of our financial condition and results of operations should be read together with our Condensed Consolidated Financial Statements and the related notes included elsewhere in this Quarterly Report and in our Annual Report. This discussion and analysis contains forward-looking statements that are based on our current expectations and reflect our plans, estimates and anticipated future financial performance. These statements involve numerous risks and uncertainties, including those related to the anticipated impact on our business from, and our response to, the COVID-19 pandemic. Our actual results may differ materially from those expressed or implied by these forward-looking statements as a result of many factors, including those set forth in the section entitled "Risk Factors" in this Quarterly Report and in our Annual Report, as well as our other public filings with the SEC. Please also refer to the section of this Quarterly Report entitled "Cautionary Note Regarding Forward-Looking Statements" for additional information.*

### Overview

Our mission is to revolutionize vertical industry businesses by providing great software and services. Today we offer industry-specific, cloud-based business software solutions, services and data analytics to the real estate market, which represents over 90% of our revenue, and, to a lesser extent, to the legal market. Although specific functionality varies by product, our core solutions address common business operations and interactions of businesses in our targeted verticals. In addition to our core solutions, we offer a range of optional, but often business-critical, Value+ services. Our Value+ services are built to enhance, automate and streamline processes and support workflows essential to our customers' businesses.

Our real estate software solutions provide our property management customers (including third-party property managers and owner-operators who manage single- and multi-family residences, community associations, commercial properties, and student housing, as well as mixed real estate portfolios) with a system of record to automate essential business processes, a system of engagement to enhance business interactions between our customers and their clients and other stakeholders, and a system of intelligence designed to leverage data to predict and optimize business workflows in order to enable superior customer experiences and increase efficiency across our customers' businesses. Our mobile-optimized software solutions are designed for use across multiple devices and operating systems. Our software solutions are all offered as a service for our customers and hosted using a modern cloud-based architecture. This architecture leads to rich data sets that have a consistent schema across our customer base and enables us to deploy data-powered products and services for our customers. We also provide software solutions to the legal market that enable law firms to administer their practice and manage their caseloads more efficiently by centralizing case details in a single system of record and system of engagement.

We have focused on growing our revenue by increasing the size of our customer base in the markets we serve, increasing the number of units under management, introducing new or expanded Value+ services, retaining customers, and increasing the adoption and utilization of our Value+ services by new and existing customers. We evaluate the success of our business during the periods presented based on factors such as the development and launch of new and innovative core functionality and Value+ services, enhancements to user experience, customer satisfaction, growth in our revenue and customer base, fluctuations in costs and operating expenses as a percentage of revenue, operating loss or income and cash flows from operating activities.



To date, we have experienced rapid revenue growth due to our investments in research and product development, sales and marketing, customer service and support, and infrastructure. We intend to continue to invest in growth across our organization as we expand in our current and adjacent markets and into new verticals. Over the long-term, these investments to grow our business are expected to continue to increase our costs and operating expenses on an absolute basis. Many of these investments will occur in advance of our realization of revenue or any other benefit, which will make it difficult to determine if we are allocating our resources effectively and efficiently. We expect our operating margins will improve over the long term, but this trend may be interrupted from time to time as a result of accelerated investment opportunities occurring in advance of realization of revenue.

We have managed, and plan to continue to manage, our business towards the achievement of long-term growth that we believe will positively impact long-term stockholder value, and not towards the realization of short-term financial or business metrics, or short-term stockholder value. We have invested, and intend to continue to invest, in our business to capitalize on our market opportunity. Accordingly, if opportunities arise that might cause us to sacrifice our performance with respect to short-term financial or business metrics, but that we believe are in the best interests of our stockholders in the long term, we will take those opportunities.

At March 31, 2020, we had approximately 1,300 employees, and we consider our relationship with them to be very good. We also hire temporary employees and consultants, and feel similarly about our relationships with them. None of our employees is represented by a labor union or covered by a collective bargaining agreement.

### Real Estate Overview

In 2008, we entered the real estate market with our first product, AppFolio Property Manager ("APM"), a property management solution designed to address the unique operational and business requirements of property management companies. Recognizing that our customers and their stakeholders would benefit from additional business critical services, we launched a series of Value+ services beginning in 2009. Our first Value+ service assisted our customers in the marketing of their rental properties by offering property level website design and hosting services. One year later, we commenced the roll out of our electronic payment services, thereby facilitating the payment of rent via ACH by tenants. In 2011, we launched tenant screening services, further assisting our customers with the leasing process. In 2012, we introduced our legal liability to landlord insurance program, which protects property owners and managers from certain defined losses. We expanded our electronic payment services in 2013 by allowing residents to pay rent by ECP and credit or debit card. In 2014, we launched a tenant-facing contact center solution to assist our property managers with resolving incoming maintenance requests. In 2015, we expanded the marketing services offered to our property management customers with a premium leads service built on technology acquired with our acquisition of RentLinx and expanded our electronic payment services to facilitate payments made between our customers and property owners and vendors. In 2016, we introduced a tenant debt collection Value+ service to assist our property managers with running a more efficient business. We expanded our insurance services in 2017 to enable tenants to purchase renters insurance from within APM, protecting both our property management customers and their tenants. In 2018, we acquired substantially all of the assets of WegoWise, Inc. ("WegoWise"), a provider of cloud-based utility analytics software solutions, and began offering AppFolio Utility Management as a Value+ service to our property management customers in mid-2019. That same year, we released AppFolio Property Manager PLUS ("APM PLUS"), a new tier of APM designed for larger businesses with more complex needs. APM PLUS builds upon the core functionality of APM and also offers data analytics, configurable workflows, and revenue management and optimization functionality for our customers. In January 2019, we acquired Dynasty, a provider of advanced artificial intelligence ("AI") solutions for the real estate market, and began offering an AI Leasing Assistant, which we refer to as "Lisa", as a Value+ service to our property management customers in mid-2019. In April 2019, we launched AppFolio Investment Management, which enables real estate investment managers to better manage their investor relationships by increasing transparency and streamlining certain business processes.

Over 90% of our annual revenue is derived directly and indirectly from the software solutions, services and data analytics we offer to the real estate market. The significant majority of our customers in the real estate market use our property management solutions. We define our property management customer base as the number of customers subscribing to our property management core solutions. Customer count and property management units under management are presented in the table below:

	Quarter Ended				
	March 31,	December 31,	September 30,	June 30,	March 31,
	2020	2019			
Property manager customers	14,729	14,385	14,034	13,737	13,409
Property manager units under management (in millions)	4.80	4.64	4.41	4.23	4.08

### Legal Overview

We entered the legal market with the acquisition of MyCase in 2012. In 2013, we introduced website design and hosting services, our first Value+ service for our legal market customers, designed to assist smaller law firms and solo practitioners with the marketing of their practices, electronic storage of case information and communications. In 2016, we launched electronic payments services for the legal market, which streamlined the billing and receivables process through MyCase.

Our legal customers directly and indirectly account for less than 10% of our annual revenue. We define our legal customer base as the number of customers subscribing to MyCase core solutions, exclusive of free trial periods. Legal customer count is summarized in the table below:

	Quarter Ended				
	March 31,	December 31,	September 30,	June 30,	March 31,
	2020	2019			
Law firm customers	11,115	10,971	10,781	10,631	10,485

### Trends and Uncertainties Related to the COVID-19 Pandemic

In December 2019, a novel coronavirus disease, referred to as COVID-19, was reported and has spread globally, including to every state in the United States. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic, and on March 13, 2020, the United States government declared a national emergency with respect to COVID-19.

In response to the COVID-19 pandemic, many state, local, and foreign governments have put in place, and others in the future may put in place, travel restrictions, quarantines, shelter-in-place orders, and similar government orders and restrictions, in an attempt to control the spread of the disease. Such restrictions or orders, or the perception that such restrictions or orders could be implemented, have resulted in business closures, work stoppages, slowdowns and delays, work-from-home policies, and the cancellation or postponement of events.

Beginning in March 2020, in an effort to protect our employees and comply with applicable government orders, we restricted non-essential employee travel and transitioned our employees to a remote work environment. Although we have not experienced a material impact from shifting our employees to a remote work environment, which we primarily attribute to the professionalism of our workforce and our extensive use of technology throughout our business, if the COVID-19 pandemic requires remote working conditions for a prolonged period of time, it could negatively impact the productivity of our workforce.

We began fiscal year 2020 with healthy demand for our products and services, many of which are designed to enable our customers to manage their businesses virtually. During the three months ended March 31, 2020, we did experience some variability in demand for certain Value+ services after certain government restrictions were put in place. We expect demand variability for our products and services could continue as a result of the COVID-19 pandemic, although it is presently unclear whether the cumulative impacts will be positive or negative. We continue to stay close with and listen to our customers to best ensure that we are responding to their needs in the current environment with innovative solutions that will not only be beneficial now but over the long term as well.

We continue to monitor developments related to COVID-19 and remain flexible in our response to the challenges presented by the pandemic. To mitigate the adverse impact COVID-19 may have on our business and operations, we have implemented a number of measures to protect the health and safety of our employees, as well as to strengthen our financial position. These efforts include increasing our cash position and eliminating, reducing, or deferring non-essential expenditures, as well as complying with local and state government recommendations to protect our workforce.

Our reported results for the three month period ended March 31, 2020 may not be reflective of current market conditions, or of our results for any future periods, which may be negatively impacted by the COVID-19 pandemic to a greater extent than the reported period. The impact of the COVID-19 pandemic may also exacerbate other risks discussed in this Quarterly Report. Refer to Item 1A. "Risk Factors" in this Quarterly Report on Form 10-Q for a complete description of the material risks that the Company currently faces.

### Key Components of Results of Operations

#### Revenue

We charge our customers on a subscription basis for our core solutions and certain of our Value+ services. Our subscription fees are designed to scale to the size of our customers' businesses. We recognize subscription revenue over time on a straight-line basis over the contract term beginning on the date that our service is made available to the customer. We generally invoice our customers for subscription services in monthly or annual installments, typically in advance of the subscription period. Revenue

from subscription services is impacted by a number of factors, including the change in the number and type of our customers, the size and needs of our customers' businesses, our customer renewal rates, pricing for our solutions, and the level of adoption of our Value+ subscription services by new and existing customers.

We also charge our customers usage-based fees for using certain Value+ services. Certain of the usage-based fees are paid by either our customers or clients of our customers. Usage-based fees are charged on a flat fee per transaction basis with no minimum usage commitments. We recognize revenue for usage-based services in the period the service is rendered. We generally invoice our customers for usage-based services on a monthly basis for services rendered in the preceding month. Revenue from usage-based services is impacted by a number of factors, including the number of new and existing customers that adopt and utilize our Value+ services, the size and needs of our customers, and our customer renewal rates.

We experience limited seasonality in our Value+ services revenue, primarily with respect to certain leasing-related services we provide to our property management customers, including our tenant screening services and new tenant applications which impact electronic payment services revenue. Our property management customers historically have processed fewer applications for new tenants during the fourth quarter. As a result of this seasonal decline in activity, we have typically experienced overall slower sequential revenue growth or a sequential decline in revenue in the fourth quarter of each of our most recent fiscal years. We expect this seasonality to continue in the foreseeable future.

We offer assistance to our customers with on-boarding to our core solutions, as well as website design services. We generally invoice our customers for these other services in advance of the services being completed. We recognize revenue for these other services upon completion of the related service. We generate revenue from RentLinx, WegoWise, and Dynasty stand-alone customers by providing services outside of our property management core solution platform. Revenue derived from customers using these services is recorded in Other revenue.

### ***Costs and Operating Expenses***

***Cost of Revenue.*** Cost of revenue consists of fees paid to third-party service providers associated with delivering certain of our Value+ services (including legal fees and costs associated with the delivery and provision of those services, as well as loss reserves and other costs associated with our legal liability to landlord insurance services), personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on customer service and the support of our operations, platform infrastructure costs (such as data center operations and hosting-related costs), payment processing fees and allocated shared and other costs. Cost of revenue excludes depreciation of property and equipment, and amortization of capitalized software development costs and intangible assets. We intend to continue to invest in customer service and support, and the expansion of our technology infrastructure as we grow the number of our customers, enter new markets, and offer additional Value+ services. These investments could impact cost of revenue both in absolute dollars and as an overall percentage of revenue.

***Sales and Marketing.*** Sales and marketing expense consists of personnel-related costs (including salaries, sales commissions, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on sales and marketing, costs associated with sales and marketing activities, and allocated shared costs. Marketing activities include advertising, online lead generation, lead nurturing, customer and industry events, and the creation of industry-related content and collateral. Sales commissions and other incremental costs to acquire customers and grow adoption and utilization of our Value+ services by our new and existing customers are deferred and then amortized on a straight-line basis over a period of benefit, that we have determined to be three years. We focus our sales and marketing efforts on generating awareness of our software solutions, creating sales leads, establishing and promoting our brands, and cultivating an educated community of successful and vocal customers. We intend to continue to invest in sales and marketing to increase our customer base in new and existing markets, and increase the adoption and utilization of Value+ services by our new and existing customers.

***Research and Product Development.*** Research and product development expense consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on research and product development, fees for third-party development resources, and allocated shared costs. Our research and product development efforts are focused on enhancing functionality and the ease of use of our existing software solutions by adding new core functionality, Value+ services and other improvements, as well as developing new products and services for new and existing markets. We capitalize our software development costs which meet the criteria for capitalization. Amortization of capitalized software development costs is included in depreciation and amortization expense. We intend to continue to invest in research and product development as we continue to introduce new core functionality, roll out new Value+ services, develop new products and services, and expand into adjacent markets, and new verticals.

***General and Administrative.*** General and administrative expense consists of personnel-related costs (including salaries, a majority of total incentive-based compensation, benefits, and stock-based compensation) for employees in our executive, finance, information technology, human resources, corporate development, legal, and administrative organizations. In addition, general

and administrative expense includes fees for third-party professional services (including audit, legal, tax, and consulting services), transaction costs related to business combinations, other corporate expenses, and allocated shared costs. We intend to continue to incur incremental general and administrative costs associated with supporting the growth of our business.

*Depreciation and Amortization.* Depreciation and amortization expense includes depreciation of property and equipment, amortization of capitalized software development costs, and amortization of intangible assets. We depreciate or amortize property and equipment, software development costs, and intangible assets over their expected useful lives on a straight-line basis, which approximates the pattern in which the economic benefits of the assets are consumed. As we continue to invest in our research and product development organization and the development or acquisition of new technology, we expect to have increased capitalized software development costs and incremental amortization. Further, we may incur additional amortization expense to the extent we enter into additional arrangements to acquire or invest in new technologies or markets adjacent to those we serve today or entirely new verticals. Finally, as we expand our facilities footprint and increase our base of employees, we expect to have increased property and equipment expenditures and incremental depreciation expense.

*Interest Expense, Net.* Interest expense includes interest paid on outstanding borrowings under our Credit Agreement with Wells Fargo Bank, National Association ("Wells Fargo"), as administrative agent, and the lenders that are parties thereto (the "Credit Agreement"). Interest income includes interest earned on investment securities, amortization and accretion of the premium and discounts paid from the purchase of investment securities, and interest earned on notes receivable and on cash deposited in our bank accounts.

*Provision for (Benefit from) Income Taxes.* Provision for (benefit from) income taxes consists of federal and state income taxes in the United States.

## Results of Operations

The following table sets forth our results of operations for the periods presented in dollars (in thousands) and as a percentage of revenue:

	Three Months Ended March 31,			
	2020		2019	
	Amount	%	Amount	%
<b>Consolidated Statements of Operations Data:</b>				
Revenue	\$ 72,495	100.0 %	\$ 57,091	100.0 %
Costs and operating expenses:				
Cost of revenue (exclusive of depreciation and amortization) <sup>(1)</sup>	28,961	39.9	24,181	42.4
Sales and marketing <sup>(1)</sup>	14,506	20.0	11,219	19.7
Research and product development <sup>(1)</sup>	11,212	15.5	8,481	14.9
General and administrative <sup>(1)</sup>	8,572	11.8	8,192	14.3
Depreciation and amortization	6,414	8.8	5,076	8.9
Total costs and operating expenses	69,665	96.1	57,149	100.1
Income (loss) from operations	2,830	3.9	(58)	(0.1)
Other income (expense), net	22	—	(1)	—
Interest expense, net	(494)	(0.7)	(497)	(0.9)
Income (loss) before provision for (benefit from) income taxes	2,358	3.3	(556)	(1.0)
Provision for (benefit from) income taxes	375	0.5	(4,281)	(7.5)
Net income	<u>\$ 1,983</u>	2.7 %	<u>\$ 3,725</u>	6.5 %

<sup>(1)</sup> Includes stock-based compensation expense as follows (in thousands):

	Three Months Ended March 31,	
	2020	2019
Stock-based compensation expense included in costs and operating expenses:		
Cost of revenue (exclusive of depreciation and amortization)	\$ 126	\$ 324
Sales and marketing	225	248
Research and product development	294	308
General and administrative	314	672
Total stock-based compensation expense	<u>\$ 959</u>	<u>\$ 1,552</u>

## Comparison of the Three Months Ended March 31, 2020 and 2019

### Revenue

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Core solutions	\$ 24,902	\$ 20,822	\$ 4,080	20%
Value+ services	44,138	33,698	10,440	31%
Other	3,455	2,571	884	34%
Total revenue	\$ 72,495	\$ 57,091	\$ 15,404	27%

For the three months ended March 31, 2020 and 2019, we derived over 90% of our revenue directly and indirectly from the software solutions, services and data analytics we offer to our real estate market customers. The significant majority of our customers in the real estate market use our property management solutions.

Total revenue was \$72.5 million for the three months ended March 31, 2020 compared to \$57.1 million for the three months ended March 31, 2019, an increase of \$15.4 million, or 27%. Core solutions revenue was \$24.9 million for the three months ended March 31, 2020 compared to \$20.8 million for the three months ended March 31, 2019, an increase of \$4.1 million, or 20%. Value+ services revenue was \$44.1 million for the three months ended March 31, 2020 compared to \$33.7 million for the three months ended March 31, 2019, an increase of \$10.4 million, or 31%. Other revenue was \$3.5 million for the three months ended March 31, 2020, compared to \$2.6 million for the three months ended March 31, 2019, an increase of \$0.9 million or 34%.

The majority of our revenue is derived from our property management core solutions and Value+ services utilized by property managers, residents, applicants and owners. The increase in core solutions and Value+ services revenue was mainly attributed to a growing base of property management customers. During this period, we experienced an 18% year over year increase in the number of property management units under management resulting from a 10% year over year increase in the number of property management customers. In addition, our property managers, residents, applicants and owners increased their usage of our Value+ services. A significant majority of our Value+ services revenue comes directly and indirectly from our customers' use of our electronic payment services, tenant screening services, and insurance services. During the period, we also introduced new Value+ services and expanded the functionality of others, which resulted in incremental revenue. The increase in Other revenue was primarily attributed to revenue generated from our real estate-related acquisitions and from an increase in fees associated with our property management customers upgrading to a new website hosting platform.

### Cost of Revenue (Exclusive of Depreciation and Amortization)

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Cost of revenue (exclusive of depreciation and amortization)	\$ 28,961	\$ 24,181	\$ 4,780	20%
Percentage of revenue	39.9%	42.4%		

Cost of revenue (exclusive of depreciation and amortization) was \$29.0 million for the three months ended March 31, 2020 compared to \$24.2 million for the three months ended March 31, 2019, an increase of \$4.8 million, or 20%. This increase in cost of revenue (exclusive of depreciation and amortization) was primarily attributed to the 27% increase in revenue over the same period.

Expenditures to third-party service providers, related to the delivery of our Value+ services, increased \$3.5 million directly associated with the increased adoption and utilization of our Value+ services, as evidenced by the 31% increase in Value+ services revenue. Our third-party service provider expenses include costs associated with the delivery and provision of Value+ services, as well as loss reserves, legal fees and other costs associated with our insurance services. This increase was primarily due to a \$1.7 million increase in personnel-related costs necessary to support growth and key investments in the business, partially offset by a \$0.5 million decrease in estimated incentive-based employee bonuses and stock-based compensation costs due to the potential impact of the COVID-19 pandemic. Allocated and other costs increased by \$0.7 million primarily driven by an increase in facilities, platform infrastructure, payment processing and other costs incurred in support of our overall growth, as well as costs associated with the delivery and provision of our Value+ services.

As a percentage of revenue, cost of revenue (exclusive of depreciation and amortization) fluctuates primarily based on the mix and prices of Value+ services utilized during the period, and investments made in advance of expected revenue generation. For the three months ended March 31, 2020 cost of revenue (exclusive of depreciation and amortization), as a percentage of revenue, was 39.9% compared to 42.4% for the three months ended March 31, 2019. This improvement in cost as a percentage of revenue was primarily driven by our ability to increase revenue with a more moderate increase in personnel-related costs.

### Sales and Marketing

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Sales and marketing	\$ 14,506	\$ 11,219	\$ 3,287	29%
Percentage of revenue	20.0%	19.7%		

Sales and marketing expense was \$14.5 million for the three months ended March 31, 2020 compared to \$11.2 million for the three months ended March 31, 2019, an increase of \$3.3 million, or 29%. This increase was primarily due to a \$2.9 million increase in personnel-related costs necessary to support growth and key investments in the business, partially offset by a \$0.4 million decrease in estimated incentive-based employee bonuses and stock-based compensation costs due to the potential impact of the COVID-19 pandemic. Advertising and promotion costs increased by \$0.5 million related to our new and expanded service offerings. In addition, there was an increase in allocated and other costs of \$0.3 million driven by an increase in IT and other costs incurred in support of our overall growth in personnel.

As a percentage of revenue, sales and marketing expense increased to 20.0% from 19.7% for the three months ended March 31, 2020 compared to the three months ended March 31, 2019. This increase was primarily driven by personnel-related investments made in advance of expected revenue generation associated with growth initiatives in the business.

### Research and Product Development

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Research and product development	\$ 11,212	\$ 8,481	\$ 2,731	32%
Percentage of revenue	15.5%	14.9%		

Research and product development expense was \$11.2 million for the three months ended March 31, 2020 compared to \$8.5 million for the three months ended March 31, 2019, an increase of \$2.7 million, or 32%. This increase was the result of an increase in personnel-related costs, net of capitalized software development costs, of \$2.9 million due to investments in headcount growth within our research and product development organization, partially offset by a \$0.6 million decrease in estimated incentive-based employee bonuses and stock-based compensation costs due to the potential impact of the COVID-19 pandemic. There was also an increase in allocated and other costs of \$0.4 million driven by an increase in facilities, IT and other costs incurred in support of our overall growth in personnel.

### General and Administrative

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
General and administrative	\$ 8,572	\$ 8,192	\$ 380	5%
Percentage of revenue	11.8%	14.3%		

General and administrative expense was \$8.6 million for the three months ended March 31, 2020 compared to \$8.2 million for the three months ended March 31, 2019, a net increase of \$0.4 million, or 5%. This increase was primarily due to a \$1.8 million increase in personnel-related costs necessary to support growth and key investments in the business, partially offset by a \$1.1 million decrease in estimated incentive-based employee bonuses and stock-based compensation costs due to the potential impact

of the COVID-19 pandemic. There was also a decrease in allocated and other costs of \$0.4 million primarily due to a decrease in third-party professional services costs.

We expect stock-based compensation expense will continue to decrease for certain executives with our adoption of a Long-Term Cash Bonus Plan in 2018. No accrual has yet been made under this plan as a result of the high degree of uncertainty regarding potential future payments under the plan.

### **Depreciation and Amortization**

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Depreciation and amortization	\$ 6,414	\$ 5,076	\$ 1,338	26%
Percentage of revenue	8.8%	8.9%		

Depreciation and amortization expense was \$6.4 million for the three months ended March 31, 2020 compared to \$5.1 million for the three months ended March 31, 2019, an increase of \$1.3 million, or 26%. This increase was primarily due to increased amortization expense associated with higher accumulated capitalized software development balances.

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

	Three Months Ended March 31,		Change	
	2020	2019	Amount	%
	(dollars in thousands)			
Provision for (benefit from) income taxes	\$ 375	\$ (4,281)	\$ 4,656	(109)%
Percentage of revenue	0.5%	(7.5)%		

We calculate our provision for income taxes on a quarterly basis by applying an estimated annual effective tax rate to income from operations and by calculating the tax effect of discrete items recognized during the quarter.

For the three months ended March 31, 2020, we recorded income tax expense of \$0.4 million. The income tax expense recorded and the difference between the U.S. federal statutory rate of 21% was primarily due to the tax impact associated with stock-based compensation expense and research and development credits.

For the three months ended March 31, 2019, we recorded an income tax benefit of \$4.3 million. The tax benefit recorded is primarily due to changes in the deferred tax asset valuation allowance resulting from \$4.1 million of deferred tax liabilities acquired through the Dynasty acquisition. The acquired deferred tax liabilities are expected to provide a source of income to support realizability of our existing deferred tax assets.

## **Liquidity and Capital Resources**

### **Cash and Cash Equivalents**

As of March 31, 2020, our principal sources of liquidity were cash and cash equivalents and investment securities, which had an aggregate balance of \$71.4 million. Our available cash is subject to our ongoing compliance with the financial covenants set forth in the Credit Agreement. For additional information regarding the Credit Agreement, refer to Note 8, *Long-Term Debt*, of our Condensed Consolidated Financial Statements.



### **Working Capital**

As of March 31, 2020, we had working capital of \$54.1 million, compared to working capital of \$14.3 million as of December 31, 2019. The increase in our working capital was primarily due to an increase in cash and cash equivalents as a result of our borrowing under the Revolving Facility, a decrease in accrued employee expenses and a decrease in other current liabilities due to the payment of contingent consideration related to the Dynasty acquisition. The increase in our working capital was partially offset by a decrease in investment securities-current and increases in deferred revenue, accrued expenses and accounts payable.

### **Revolving Facility**

As of March 31, 2020, we had a \$50.0 million revolving credit facility (the "Revolving Facility") under the terms of the Credit Agreement. During the three months ended March 31, 2020, we borrowed \$49.0 million under our Revolving Facility to provide additional liquidity in light of the uncertainty caused by the COVID-19 pandemic. For additional information regarding the Credit Agreement, refer to Note 8, *Long-Term Debt*, of our Condensed Consolidated Financial Statements.

### **Liquidity Requirements**

We believe that our existing cash and cash equivalents, investment securities, and cash generated from operating activities will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months.

### **Capital Requirements**

Our future capital requirements will depend on many factors, including continued market acceptance of our software solutions, change in the number of our customers, adoption and utilization of our Value+ services by new and existing customers, the timing and extent of the introduction of new core functionality, products and Value+ services, the timing and extent of our expansion into adjacent or new markets, and the timing and extent of our investments across our organization. In addition, we have in the past entered into, and may in the future enter into, arrangements to acquire or invest in new technologies or markets adjacent to those we serve today or entirely new verticals. Furthermore, our Board of Directors has authorized our management to repurchase up to \$100.0 million of shares of our Class A common stock from time to time. For additional information regarding our share repurchase program, refer to Note 10, *Share Repurchase Program* of our Condensed Consolidated Financial Statements.

### **Cash Flows**

The following table summarizes our cash flows for the periods indicated (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2020</b>	<b>2019</b>
Net cash provided by operating activities	\$ 3,083	\$ 295
Net cash provided by (used in) investing activities	5,729	(55,692)
Net cash provided by (used in) financing activities	32,156	(1,897)
Net increase (decrease) in cash, cash equivalents and restricted cash	<u>\$ 40,968</u>	<u>\$ (57,294)</u>

### **Cash Provided by Operating Activities**

Our primary source of operating cash inflows is cash collected from our customers in connection with their use of our core solutions and Value+ services. Our primary uses of cash from operating activities are for personnel-related expenditures and third-party costs incurred to support the delivery of our software solutions.

For the three months ended March 31, 2020, net cash provided by operating activities was \$3.1 million resulting from net income of \$2.0 million, adjusted by non-cash charges of \$8.8 million and a net decrease in our operating assets and liabilities of \$7.7 million. The non-cash charges primarily consist of \$6.4 million of depreciation and amortization costs, \$1.1 million of amortization of operating lease right-of-use ("ROU") assets, stock-based compensation expense of \$1.0 million, and a decrease in deferred taxes of \$0.4 million. The net decrease in our operating assets and liabilities was mostly attributable to a \$5.4 million decrease in accrued employee expenses primarily due to the payout of accrued employee bonuses and commissions, an increase of \$2.8 million in prepaid expenses and other current assets, and a \$1.6 million increase in accounts receivable primarily driven by growth of our Value+ services. These decreases were partially offset by a \$0.8 million increase in operating lease liabilities, a \$0.7 million increase in accrued expenses and a \$0.7 million increase in deferred revenue.

For the three months ended March 31, 2019, cash provided by operating activities was \$0.3 million resulting from net income of \$3.7 million, adjusted by non-cash charges of \$3.3 million and a net decrease in our operating assets and liabilities of \$6.7 million. The non-cash charges primarily consist of \$5.1 million of depreciation and amortization costs, a tax benefit of \$4.3

million related to changes in the deferred tax asset valuation allowance resulting from deferred tax liabilities acquired through the Dynasty acquisition, \$1.6 million of stock-based compensation, and \$0.9 million of amortization of ROU assets. The net decrease in our operating assets and liabilities was mostly attributable to an increase of \$3.6 million in prepaid expenses and other current assets, a \$2.9 million decrease in accrued employee expenses due to the payout of accrued employee bonuses and commissions, and a \$2.1 million increase in accounts receivable primarily driven by growth in our Value+ services. These decreases were partially offset by a \$1.6 million increase in accrued expenses, a \$0.7 million decrease in other assets, and a \$0.3 million increase in deferred revenue.

#### ***Cash Provided by (Used in) Investing Activities***

Cash provided by (used in) investing activities is generally comprised of purchases, maturities and sales of investment securities, purchases of property and equipment, additions to capitalized software development, and cash paid for business acquisitions.

For the three months ended March 31, 2020, investing activities provided \$5.7 million in cash primarily due to sales and maturities of investment securities of \$13.9 million and \$7.3 million, respectively. These sources of cash were partially offset by capital expenditures of \$8.0 million to purchase property and equipment for the continued growth and expansion of our business, capitalized software development costs of \$6.8 million for the continued investment in our software development, and purchases of investment securities of \$0.6 million.

For the three months ended March 31, 2019, investing activities used \$55.7 million in cash primarily due to \$54.0 million used to acquire Dynasty, as well as capitalized software development costs of \$4.7 million for the continued investment in our software development, and capital expenditures of \$1.0 million to purchase property and equipment for the continued growth and expansion of our business. These uses were partially offset by sales and maturities of investment securities of \$1.8 million and \$2.3 million, respectively.

#### ***Cash Provided by (Used in) Financing Activities***

Cash provided by (used in) financing activities is generally comprised of proceeds from the exercise of stock options, net share settlements for employee tax withholdings associated with the vesting of RSUs, the payment of contingent consideration under acquisition arrangements, activities associated with our Revolving Facility and a \$50.0 million term loan issued by Wells Fargo, as administrative agent, and the lenders that are parties thereto (the "Term Loan," and together with the Revolving Facility, the "Credit Facility"), and activities related to the repurchase of our Class A common stock.

For the three months ended March 31, 2020, financing activities provided \$32.2 million in cash primarily as a result of proceeds from the Revolving Facility of \$49.4 million, partially offset by net share settlements for employee tax withholdings associated with the vesting of RSUs of \$6.5 million, payment of contingent consideration related to the Dynasty acquisition of \$6.0 million, and the repurchase of outstanding shares of Class A common stock in the amount of \$4.2 million.

For the three months ended March 31, 2019, financing activities used \$1.9 million in cash primarily as a result of net share settlements for employee tax withholdings associated with the vesting of RSUs of \$1.3 million, as well as principal payments on debt of \$0.9 million and payments of debt issuance costs of \$0.4 million, partially offset by proceeds from issuance of debt of \$0.6 million.

#### **Contractual Obligations and Other Commitments**

There have been no material changes to our contractual obligations and other commitments as disclosed in our Annual Report.

#### **Off-Balance Sheet Arrangements**

As of March 31, 2020, we did not have any off-balance sheet arrangements.

#### **Critical Accounting Policies and Estimates**

Our Condensed Consolidated Financial Statements and the related notes are prepared in accordance with accounting principles generally accepted in the United States. The preparation of our Condensed Consolidated Financial Statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting period.

COVID-19 has created and may continue to create significant uncertainty in global financial markets, which may reduce demand for our core solutions and/or Value+ services, impact the productivity of our workforce, reduce our access to capital, and harm our business and results of operations. As of the date of our Condensed Consolidated Financial Statements, we are not aware of any specific event or circumstance that would require us to update our estimates or judgments, or to revise the carrying value of our assets or liabilities. However, these estimates may change as new events occur and additional information is obtained, which may result in changes being recognized in our consolidated financial statements in future periods. While we considered the effects of COVID-19 in our estimates and assumptions, due to the current level of uncertainty over the economic and operational impacts of COVID-19 on our business, there may be other judgments and assumptions that were not currently considered. Such judgments and assumptions could result in a meaningful impact to our financial statements in future periods. Actual results could differ from those estimates and any such differences may have a material impact on our financial statements.

There have been no changes to our critical accounting policies and estimates described in our Annual Report that have had a material impact on our Condensed Consolidated Financial Statements and related notes.

### **Recent Accounting Pronouncements**

For information regarding recent accounting pronouncements, refer to Note 2, *Summary of Significant Accounting Policies*, of our Condensed Consolidated Financial Statements.

### **Item 3. Qualitative and Quantitative Disclosure about Market Risk**

#### ***Interest Rate Risk***

##### *Short-Term Investments*

At March 31, 2020, we had cash and cash equivalents of \$56.8 million consisting of bank deposits and money market funds and \$14.6 million of investment securities consisting of corporate bonds, United States government agency securities and treasury securities. The primary objective of our investment policy is to invest in securities to support our liquidity and capital needs. We have not purchased investments for trading or speculative purposes and have not used any derivative financial instruments to manage our interest rate risk exposure.

Our investment securities are exposed to market risk due to interest rate fluctuations. While fluctuations in interest rates do not impact our interest income from our investment securities as all of these securities have fixed interest rates, changes in interest rates may impact the fair value of the investment securities. Since our investment securities are held as available for sale, all changes in fair value impact our other comprehensive income unless an investment security is considered impaired in which case changes in fair value are reported in other expense. At March 31, 2020 a hypothetical 100 basis point change in interest rates would not have resulted in a material change in the fair value of our investment securities. This estimate is based on a sensitivity model which measured an instant change in interest rates by 100 basis points at March 31, 2020.

##### *Credit Facility*

We are exposed to interest rate risk as a result of our Credit Facility. Outstanding borrowings under the Credit Facility accrue interest as described in Note 8, *Long-Term Debt* of our Condensed Consolidated Financial Statements. Our borrowings under the Credit Facility are subject to interest rate fluctuations, which could have a material impact on our cash flows and results of operations depending on the magnitude of the fluctuations and the outstanding borrowings. In order to determine the potential impact of changes in interest rates on our cash flows and result of operations, we performed a sensitivity analysis. A hypothetical 100 basis point increase in interest rates during the period ended March 31, 2020 would not have had a material impact on our cash flows or results of operations.

#### ***Inflation Risk***

We have not been exposed to, nor do we anticipate being exposed to, material risks due to changes in inflation rates.

## **Item 4. Controls and Procedures**

### ***Evaluation of Disclosure Controls and Procedures***

Our management, with the supervision and participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to provide reasonable assurance that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and other procedures designed to provide reasonable assurance that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Based on our management’s evaluation, our principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this Quarterly Report, our disclosure controls and procedures were effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

### ***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Quarterly Report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We have not experienced any material changes to our internal controls over financial reporting despite the fact that all non-essential employees are working remotely due to the COVID-19 pandemic. We are continually monitoring the impact of COVID-19 on the operating effectiveness of our internal control over financial reporting.

### ***Inherent Limitations on Effectiveness of Disclosure Controls***

In designing and evaluating our disclosure controls and procedures, our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable and not absolute assurance of achieving the desired control objectives. In reaching a reasonable level of assurance, management necessarily is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. In addition, the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Control systems can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

From time to time, we are involved in various legal proceedings arising from or related to claims incident to the ordinary course of our business activities, including without limitation, actions involving intellectual property, employment and contractual matters. Although the results of such legal proceedings and claims cannot be predicted with certainty, we believe that we are not currently a party to any legal proceedings which, if determined adversely to us, would, individually or taken together, have a material adverse effect on our business, operating results, financial condition or cash flows. However, regardless of the merit of any claims raised or the ultimate outcome, legal proceedings may generally have an adverse impact on us as a result of defense and settlement costs, diversion of management resources, and other factors.

For additional information regarding legal proceedings, refer to Note 9, Commitments and Contingencies, of our Condensed Consolidated Financial Statements.

### Item 1A. Risk Factors

An investment in our Class A common stock involves risks. You should consider carefully the risks described below, together with all of the other information included in this Quarterly Report, as well as in our other filings with the SEC, in evaluating our business. If any of the following risks actually occur, our business, financial condition, operating results and future prospects could be materially and adversely affected. In that case, the trading price of our Class A common stock may decline and you might lose all or part of your investment. The risks described below are not the only ones we face. Additional risks that we currently do not know about or that we currently believe to be immaterial may also impair our business, financial condition, operating results and prospects.

Please be advised that certain of the risks and uncertainties described below contain “forward-looking statements.” See the section of this Quarterly Report entitled “*Cautionary Note Regarding Forward-Looking Statements*” for additional information.

#### Risks Related to Our Business and Our Industry

***Health epidemics, including the COVID-19 pandemic, have had, and could in the future have, a material adverse impact on our operations, the operations of our customers and other business partners, and the markets and communities in which we and our customers and partners operate.***

In December 2019, a novel coronavirus disease, referred to as COVID-19, was reported and has spread globally, including to every state in the United States. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic, and on March 13, 2020, the United States government declared a national emergency with respect to COVID-19.

The COVID-19 pandemic has had, and another public health crisis or epidemic in the future could have, repercussions across local, regional and global economies and financial markets. The outbreak of COVID-19 in many countries, including the United States, has adversely impacted global economic activity and has contributed to volatility in and negative pressure on financial markets. In response to the COVID-19 pandemic, many state, local, and foreign governments have put in place, and others in the future may put in place, travel restrictions, quarantines, shelter-in-place orders, and similar government orders and restrictions, in an attempt to control the spread of the disease. Such restrictions or orders, or the perception that such restrictions or orders could be implemented, have resulted in business closures, work stoppages, slowdowns and delays, work-from-home policies, and cancellation or postponement of events, among other effects that could negatively impact our operations, as well as the operations of our customers and business partners.

Beginning in March 2020, we restricted non-essential employee travel and transitioned our employees to a remote work environment. Although we have not experienced a material impact from shifting our employees to a remote work environment, there is no guarantee that our employees will be as effective while working remotely due to a number of factors, including the inability of team members to communicate as effectively in a remote environment, the reality that employees may have additional personal needs to attend to (such as looking after children as a result of school closures or family members who become sick), and employees may become sick themselves and unable to work. If the COVID-19 pandemic requires remote working conditions for a prolonged period of time, it could have an adverse impact on the productivity of our employees, which would harm our business and impede our ability to achieve our strategic plan. In addition, in an effort to manage the financial uncertainty involved with the COVID-19 pandemic, we have delayed the hiring of certain non-essential employees.

The COVID-19 pandemic has resulted in a rapid rise in unemployment and a sudden decrease in global economic activity, and many businesses have experienced, or are anticipating that they may experience, a significant negative impact on their operating results. While we did not experience a significant impact on the demand for our core products and Value+ services during the period ended March 31, 2020, we anticipate greater demand impacts in future periods, although the timing and magnitude of these impacts is difficult to estimate. In addition, our inability to meet in-person with current or prospective customers, or the cancellation or postponement of Company-sponsored events or third-party events at which our products are featured, could have a negative impact on our customer engagement efforts, which could further impact demand in future periods.

Furthermore, the demand for our products and services, as well as our operating results, could be adversely impacted due to number of other factors, including the following:

- new customers delaying decisions to adopt our core products, or expand the use of our Value+ services, as they seek to reduce or delay spending in response to the impacts of COVID-19 on their own businesses;
- a complete or partial closure of, or other operational issues at, properties owned by our customers resulting from government restrictions or orders;
- a deterioration in our ability, or the ability of our customers, to operate in affected geographic areas;
- bankruptcies or other financial difficulties facing our customers, which could cause them to delay making payments to us, or result in them terminating or reducing their use of our core products or Value+ services;
- the inability of tenants to meet their obligations to our customers, resulting in tenant evictions or the sale of properties;
- the failure of key business partners to provide services needed for our efficient operations, including with respect to electronic payments and tenant screening;
- a decrease in the reliability or availability of our core products or Value+ services, as a result of service interruptions caused by the remote work environment; and
- a decrease in the availability or utility of our customer service organization caused by the remote work environment.

Any of the factors described above, or any number of other risks related to the COVID-19 pandemic, could disrupt our business, which could have a material adverse impact on our business, operations and financial results. The global impact of COVID-19 continues to rapidly evolve, and it is not currently possible to ascertain all of the current or future impacts to our business. The ultimate impact of the COVID-19 pandemic, or a similar public health crisis in the future, on our business is highly uncertain and subject to change. Further, we expect any further spread of the COVID-19 pandemic, or even the threat or perception that this could occur, could further exacerbate any negative impacts on our business, financial condition and operating results.

***We manage our business towards the achievement of long-term growth, which may not be consistent with the short-term expectations of some investors.***

We plan to continue to manage our business towards the achievement of long-term growth that we believe will positively impact long-term stockholder value, and not towards the realization of short-term financial or business metrics, or short-term stockholder value. If opportunities arise that might cause us to sacrifice our performance with respect to short-term financial or business metrics, but that we believe are in the best interests of our stockholders, we will take those opportunities.

We focus on growing our customer base by developing and launching new and innovative core functionality and/or Value+ services to address our customers' evolving business needs, developing and/or acquiring new products for adjacent markets and additional verticals consistent with our strategic plan, and improving the experience of our users across our targeted verticals. We prioritize product innovation and user experience over short-term financial or business metrics. We will make product decisions that may reduce our short-term operating results if we believe that these decisions are consistent with our strategic objective to achieve long-term growth. These decisions may not be consistent with the short-term expectations of some investors, and may cause significant fluctuations in our operating results and our stock price from period to period. In addition, notwithstanding our intention to make strategic decisions that positively impact long-term stockholder value, the decisions we make may not produce the long-term benefits we expect.

Our executive officers, directors and principal stockholders control a majority of the combined voting power of our outstanding capital stock. As a result, they are able to exercise significant influence and control over the establishment and

implementation of our future business plans and strategic objectives, as well as control all matters submitted to our stockholders for approval. These persons may manage our business in ways with which you disagree and which may be adverse to your interests.

***If we fail to manage our growth effectively, it could adversely affect our operating results and preclude us from achieving our strategic objectives.***

We have experienced significant growth since our formation in 2006, and we anticipate that we will continue to experience growth and expansion of our operations, although the rate of growth may be negatively impacted by the COVID-19 pandemic. This growth in the size, complexity and diversity of our business has placed, and we expect it will continue to place, a significant strain on our management, administrative, operational and financial resources, as well as our company culture. Our future success will depend, in part, on our ability to manage this growth effectively, which we expect to be more challenging in the current environment as we seek to respond to the uncertainty and disruption caused by the COVID-19 pandemic.

To manage the expected growth of our operations, we will need to continue to develop and improve our operational and financial controls and our reporting systems and procedures, attract and retain highly qualified and motivated personnel across our organization, and nurture and build on our company culture. Failure to effectively manage growth could adversely impact our business, including by resulting in errors or delays in deploying new core functionality to our customers, delays or difficulties in introducing new Value+ services or other products, declines in the quality or responsiveness of our customer service organization, exposure to legal, regulatory and operational risks inherent in our business and resulting from any new products or services we provide to our customers or to our customers' customers, increases in costs and operating expenses, and other operational difficulties. If any of these risks actually occur, it could adversely affect our operating results, and preclude us from achieving our strategic objectives.

***We have a limited operating history and limited experience selling our solutions. We expect to make substantial investments across our organization to grow our business and, as a result, we expect our financial results may fluctuate significantly from period to period and we may not sustain profitability.***

We were formed in 2006 and in 2008 entered the real estate vertical with our first product, APM, to serve property managers. We expanded our real estate offerings with the launch of APM PLUS in late 2018 and AppFolio Investment Management in April 2019. In 2012, we entered the legal vertical through the acquisition of MyCase, which represents less than 10% of our total revenue for the three months ended March 31, 2020. As a result, we have a limited operating history and limited experience selling our software solutions in two dynamic vertical markets. These and other factors, including the significant disruption and uncertainty caused by the COVID-19 pandemic, combine to make it difficult for us to accurately forecast our future operating results, which in turn makes it difficult for us to prepare accurate budgets and implement strategic plans. We expect this uncertainty will continue to exist in our business for the foreseeable future, and the future impacts of the COVID-19 pandemic may be significantly worse than we currently expect.

We have made substantial investments across our organization to develop our software solutions and capitalize on our market opportunity. In order to implement our business strategy, we intend to continue to make substantial investments in, among other things:

- our research and product development organization to enhance the ease of use and functionality of our software solutions by adding new core functionality, Value+ services and/or other improvements to address the evolving needs of our customers, as well as to develop new products for adjacent markets and new verticals consistent with our strategic plan;
- our continued efforts to identify acquisition targets that enhance the depth or functionality of our software solutions or Value+ services, or that enable our expansion into adjacent markets or new vertical markets consistent with our strategic plan;
- our customer service organization to deepen our relationships with our customers, assist our customers in achieving success through the use of our software solutions, and promote customer retention;
- our sales and marketing organization, including expansion of our direct sales organization and marketing programs, to increase the size of our customer base, increase adoption and utilization of new and existing Value+ services by our new and existing customers, and enter adjacent markets and new verticals consistent with our strategic plan;

- maintaining and expanding our technology infrastructure and operational support to promote the security and availability of our software solutions, and support our growth;
- our general and administrative functions, to support our growth and assist us in maintaining compliance with legal, regulatory and other compliance-related obligations; and
- the expansion of our existing facilities, including leasing and building out additional office space, to support our growth and strategic development.

As a result of our continuing investments to grow our business in these and other areas, we expect our expenses to increase significantly, and we may not be consistently profitable. Even if we are successful in growing our customer base and increasing revenue from new and existing customers, we may not be able to generate additional revenue in an amount that is sufficient to cover our expenses. We may incur significant losses in a particular period for a number of reasons, and may experience significant fluctuations in our operating results from period to period. We cannot assure you that we will continue to achieve profitability in the near term or that we will sustain profitability on a sequential quarterly basis or over any particular period of time. Any additional operating losses will have a negative impact on our stockholders' equity.

***Our quarterly results may fluctuate significantly and period-to-period comparisons of our results may not be meaningful.***

Our quarterly results, including the levels of our revenue, costs, operating expenses, and operating margins, may fluctuate significantly in the future, and period-to-period comparisons of our results may not be meaningful. Accordingly, the results of any one quarter should not be relied upon as an indication of our future performance. In addition, our quarterly results may not fully reflect the underlying performance of our business. Factors that may cause fluctuations in our quarterly results include, but are not limited to:

- our ability to retain our existing customers, and to expand adoption and utilization of our core solutions and Value+ services by our existing customers;
- our ability to attract new customers, the type of customers we are able to attract, the size and needs of their businesses, and the cost of acquiring these customers;
- the mix of our core solutions and Value+ services sold during the period;
- the timing and impact of security breaches, service outages or other performance issues with our technology infrastructure and software solutions;
- variations in the timing of sales of our core solutions and Value+ services as a result of trends impacting the verticals in which we sell our software solutions;
- the timing and market acceptance of new core functionality, Value+ services and other products introduced by us and our competitors;
- changes in our pricing policies or those of our competitors;
- the timing of our recognition of revenue;
- the amount and timing of costs and operating expenses related to the maintenance and expansion of our business, infrastructure and operations;
- the amount and timing of costs and operating expenses associated with assessing or entering adjacent markets or new verticals;
- the amount and timing of costs and operating expenses related to the development or acquisition of businesses, services, technologies or intellectual property rights, and potential future charges for impairment of goodwill from these acquisitions;
- the timing and costs associated with legal proceedings, enforcement actions, regulatory inquiries or similar matters;
- changes in the competitive dynamics of our industry, including consolidation among competitors, strategic partners or customers;
- loss of our executive officers or other key employees;



- industry conditions and trends that are specific to the verticals in which we sell or intend to sell our software solutions; and
- general economic and market conditions, including the impacts and disruptions caused by the COVID-19 pandemic, which could increase the negative impacts to our business of any of the factors discussed above.

Our focus on managing our business towards the achievement of long-term growth, rather than the realization of short-term financial or business metrics, may also serve to exacerbate the fluctuations in our quarterly results, which could result in downward pressure on the market price of our Class A common stock. In addition, fluctuations in quarterly results may negatively impact the value of our Class A common stock, regardless of whether they impact or reflect the overall performance of our business. Furthermore, if our quarterly results fall below the expectations of investors or any securities analysts who follow our stock, or below any financial guidance we may provide, the price of our Class A common stock could decline substantially.

***We may require additional capital to support our operations or the growth of our business, and we cannot be certain that this capital will be available on favorable terms, or at all, which may adversely affect our business and financial condition.***

We may need additional capital to grow our business and meet our strategic objectives. Our ability to obtain additional capital, if and when required, will depend on numerous factors, including investor and lender demand, our compliance with debt obligations, our historical and forecasted financial and operating performance, our liquidity position, the overall condition of the capital markets, and the global economy as a whole. The capital markets have been negatively impacted by the COVID-19 pandemic, and the impacts may continue for the foreseeable future. We cannot guarantee that additional financing will be available to us on favorable terms when required, or at all. In addition, if we raise additional funds through the issuance of equity securities, those securities may have powers, preferences or rights senior to the rights of our Class A common stock, and our existing stockholders may experience immediate dilution. If we raise additional funds through the issuance of debt securities, we may incur interest expense or other costs to service the indebtedness, we may be required to encumber certain assets, and we may become subject to restrictions on our ability to conduct business, any of which could negatively impact our operating results. Furthermore, if we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support the growth of our business and the achievement of our strategic objectives could be significantly impaired and our operating results may be harmed.

***Our estimates of market opportunity are subject to significant uncertainty and, even if the markets in which we compete meet or exceed our size estimates, we could fail to increase our revenue or market share.***

Market opportunity estimates are subject to significant uncertainty and are based on assumptions and estimates, including our internal analysis and industry experience. Assessing the market for industry-specific, cloud-based business management software is particularly difficult due to a number of factors, including limited available information and rapid evolution of the market. Further, market opportunity estimates sometimes change based on relevant macro-trends and market conditions, or evolving assessment methodologies. We determine the level of our investment in various aspects of the business, in part, based on our market opportunity estimates. If we had made different assumptions, our estimates of market opportunity, and/or our related investment determinations, could be materially different. The disruptions and impacts caused by the COVID-19 pandemic may ultimately require us to reduce, potentially by a significant margin, our estimates of the market opportunities in certain markets or industry verticals, which could negatively impact our prospects for long-term growth.

In addition, even if the markets in which we compete meet or exceed our size estimates, our software solutions could fail to gain market acceptance and our business may not grow in line with our forecasts, or at all, which would have a material adverse impact on our financial condition and operating results.

***We have acquired, and may in the future acquire, other companies or technologies, which could divert our management's attention, result in additional dilution to our stockholders and otherwise disrupt our operations.***

We have acquired, and may in the future acquire, other companies or technologies to complement or expand our software solutions, optimize our technical capabilities, enhance our ability to compete in our targeted verticals, provide an opportunity to expand into an adjacent market or new vertical, or otherwise offer growth or strategic opportunities. For example, in our real estate vertical, we acquired substantially all of the assets of WegoWise in 2018 and completed the acquisition of Dynasty in 2019. The pursuit of acquisitions may divert the attention of management and cause us to incur various expenses in identifying, investigating and pursuing suitable acquisitions, whether or not they are consummated.

We have limited experience acquiring other businesses. We may not be able to integrate acquired assets, technologies, personnel and operations successfully or achieve the anticipated synergies or other benefits from the acquired business due to a number of risks associated with acquisitions, including:

- the aggregate cost, whether in the form of cash or equity securities, to acquire the business;
- difficulties integrating the assets, technologies, personnel or operations of the acquired business in a cost-effective manner;
- difficulties and additional expenses associated with supporting legacy products and services of the acquired business;
- difficulties converting the customers of the acquired business to our software solutions and contract terms;
- diversion of management's attention from our business to address acquisition and integration challenges, as well as post-acquisition disputes;
- adverse effects on our existing business relationships with customers and strategic partners as a result of the acquisition;
- cultural challenges associated with integrating employees from the acquired organization into our company;
- the loss of key employees;
- use of resources that are needed in other parts of our business;
- costs associated with and exposure to new or enhanced legal, regulatory or other compliance-based and/or operational risks implicit in the acquired business;
- use of substantial portions of our available cash resources to consummate the acquisition or pay acquisition-related expenses; and
- unanticipated costs or liabilities associated with the acquisition.

If an acquisition fails to meet our expectations in terms of its contribution to our overall business strategy or operating results, or if the costs of acquiring or integrating the acquired business exceed our estimates, our business, operating results and financial condition may suffer. In addition, acquisitions could result in the issuance of equity securities, which would result in immediate dilution to our stockholders or, the incurrence of debt, which could impose debt service obligations and restrictions on our ability to operate our business. Furthermore, a significant portion of the purchase price of companies we may acquire could be allocated to goodwill and other intangible assets, which must be assessed for impairment. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could adversely affect our operating results.

***Security vulnerabilities in our software solutions or a breach of our security controls could result in the loss, theft, misuse, unauthorized disclosure, or unauthorized access to customer or employee data, or other confidential and sensitive information, which could harm our relationships with customers or employees, expose us to litigation or regulatory proceedings, or harm our reputation, any of which could negatively impact our business and operating results.***

Our business involves the storage and transmission of a significant amount of confidential and sensitive information, including the personal information of our employees and other individuals, customer data, and our proprietary financial, operational and strategic information. In providing our software solutions, we store and transmit large amounts of our customers' data, including sensitive and proprietary data and personal information collected by or on behalf of our customers. Our software solutions are typically the system of record, system of engagement and, increasingly, the system of intelligence for all or a portion of our customers' businesses, and the data processed through our software solutions is critical to their businesses. Cyber attacks and other malicious Internet-based activities continue on a regular basis. Like many other businesses, we have experienced, and are continually at risk of being subject to, attacks and data security incidents. As our business grows, the number of users of our software solutions, as well as the amount of information we collect and store, is increasing, and our brands are becoming more widely recognized. We believe these factors combine to make us an even greater target for this type of malicious activity. Although we take data security seriously, there can be no assurance that the security measures we employ will prevent malicious or unauthorized access to our systems and information. Techniques used to sabotage, or to obtain unauthorized access to, systems or networks change frequently and may not be recognized until launched against a target. Furthermore, no security program can eliminate entirely the risk of non-malicious human error, such as an employee or contractor's failure to follow one or more security protocols. Therefore,

despite our significant efforts to keep our systems and networks protected and up to date, we may be unable to anticipate cyber attacks, detect security incidents or react to them in a timely manner, or implement adequate preventive measures, any of which may expose us to a risk of loss, litigation and potential liability. In addition, some of our third-party service providers also collect and/or store our sensitive information and our customers' data on our behalf, and these service providers are subject to similar threats of cyber attacks and other malicious Internet-based activities.

If our security measures, or the security measures of our third-party service providers, are breached as a result of wrongdoing or malicious activity on the part of our employees, our partners' employees, our customers' employees, or any third party, or as a result of any human error or neglect, product defect or otherwise, and this results in the loss, theft, misuse, unauthorized disclosure, or unauthorized access to customer data or other sensitive information, we could incur liability to our customers and to individuals or organizations whose information was being stored by us or our customers, as well as fines from payment processing networks and regulatory action by governmental bodies. If we experience a widespread security breach, we cannot be certain that our insurance coverage will be sufficient to compensate us for liabilities actually incurred or that insurance will continue to be available to us on reasonable terms, or at all. In addition, any security breaches could result in reputational damage, adversely affect our ability to attract new customers and cause existing customers to reduce or discontinue the use of our software solutions, any of which could harm our business and operating results. Furthermore, the perception by our current or potential customers that our software solutions could be vulnerable to exploitation or that our security measures are inadequate, even in the absence of a particular problem or threat, could reduce market acceptance of our software solutions and cause us to lose customers. The legal and regulatory environment around data security and governance is significantly evolving, and both regulators and consumers are increasingly taking action on data-related matters, which may contribute to increased reputational, economic and other harm in the event of a data security incident.

***Service outages due to malicious activities or performance problems associated with our technology infrastructure could harm our reputation, adversely affect our ability to attract new customers and cause us to lose existing customers.***

We have experienced significant growth in the number of users and the amount of data that our technology infrastructure supports, and we expect this growth to continue. We seek to maintain sufficient excess capacity in our technology infrastructure to meet the needs of all of our customers, including facilitating the expansion of existing customer deployments and the provisioning of new customer deployments. In addition, we need to properly manage our technology infrastructure in order to support version control, changes in hardware and software parameters, and the evolution of our software solutions.

We have experienced, and may in the future experience, website disruptions, service outages and other performance problems with our technology infrastructure. These problems may be caused by a variety of factors, including infrastructure changes, power or network outages, fire, flood or other natural disasters affecting our data centers, human or software errors, viruses, security breaches, fraud or other malicious activity, spikes in customer usage and distributed denial of service attacks. In some instances, we may not be able to identify the cause or causes of these service outages and performance problems within an acceptable period of time. If our technology infrastructure fails to keep pace with the increased number of users and amount of data, or if we are unable to avoid service outages and performance problems, or to resolve them quickly, this could adversely affect our ability to attract new customers, result in the loss of existing customers and harm our reputation, any or all of which could adversely affect our business and operating results.

***Errors, defects or other disruptions in our software solutions could harm our reputation, cause us to lose customers, and result in significant expenditures to correct the problem.***

Our customers use our software solutions to manage critical aspects of their businesses, and any errors, defects or other disruptions in the performance of our software solutions, including with respect to third party partners upon which certain of our software solutions are dependent, may result in loss of or damage to our customers' data and disruption to our customers' businesses, which could harm our reputation. We provide continuous updates to our software solutions and, while our software updates undergo extensive testing prior to their release, these updates may contain undetected errors when first introduced. In the past, we have discovered errors, failures, vulnerabilities and bugs in our software updates after they have been released, and similar problems may arise in the future. Real or perceived errors, failures, vulnerabilities or bugs in our software solutions could result in negative publicity, reputational harm, loss of customers, delay in market acceptance of our software solutions, loss of competitive position, withholding or delay of payment to us, claims by customers for losses sustained by them and potential litigation or regulatory action. In any such event, we may be required to expend additional resources in order to help correct the problem or, in order to address customer service or reputational concerns, we may choose to expend additional resources to take corrective action even where not required. The costs incurred in correcting any material errors, defects or other disruptions could be substantial and there may not be any corresponding increase in revenue to offset these costs. In addition, we may not carry insurance sufficient to compensate us for any losses that may result from claims arising from errors, defects or other disruptions in our software solutions.

***Government regulation is evolving and unfavorable changes could adversely affect our operating results, subject us to litigation or governmental investigation, or otherwise harm our business.***

We are subject to general business regulations and laws, as well as regulations and laws specifically governing the highly regulated real estate and legal markets, electronic payment, background screening and insurance services markets, the Internet itself, the use of mobile devices to conduct business and communicate, and many other products and services we provide. Existing and future laws and regulations may impede our growth. These regulations and laws may cover privacy, data protection, artificial intelligence and related technologies, pricing, content, intellectual property, mobile communications, electronic contracts and other communications, competition, consumer protection, employment, trade and protectionist measures, web services, the provision of online payment and tenant screening services, information reporting requirements, unencumbered Internet access to our products or services, and the design and operation of websites. It is not clear how existing laws governing issues such as property ownership, management, rental and investment, data protection, and personal privacy apply to the Internet, digital content, web services, and artificial intelligence technologies and services. Unfavorable regulations, laws, and administrative or judicial decisions interpreting or applying those laws and regulations could diminish the demand for, or availability of, our products and services, subject us to litigation or governmental investigation and increase our cost of doing business, any of which may adversely affect our operating results.

***Privacy and data security laws and regulations could impose additional costs on us and reduce the demand for our software solutions.***

We store and transmit personal information relating to our employees and other individuals, and our customers use our technology platform to store and transmit a significant amount of personal information relating to their clients, vendors, employees and other industry participants. Privacy and data security have become significant issues in the United States and in other jurisdictions where we may operate or offer our software solutions. The regulatory framework relating to privacy and data security worldwide is rapidly evolving, and is likely to remain uncertain for the foreseeable future. Federal, state and foreign government bodies and agencies have in the past adopted, and may in the future adopt, laws and regulations regarding the collection, use, processing, storage and disclosure of personal or identifying information obtained from customers and other individuals. For instance, the California Consumer Privacy Act, which went into effect on January 1, 2020, creates new data privacy and security rights for California residents. Similarly, there are a number of existing and proposed laws and regulations in the European Union and the United States at both the federal and state level, as well as other jurisdictions that could impose new obligations in areas affecting our business. These new obligations could increase the cost and complexity of delivering our services, and divert our managements' attention from pursuing strategic objectives.

In addition to government regulation, privacy advocates and industry groups may propose various self-regulatory standards that may legally or contractually apply to our business. Because the interpretation and application of many privacy and data security laws, regulations and applicable industry standards are uncertain, it is possible that these laws, regulations and standards may be interpreted and applied in a manner inconsistent with our existing privacy and data management practices. As new laws, regulations and industry standards take effect, and as we expand into new jurisdictions, adjacent markets or verticals consistent with our strategic plan, we will need to understand and comply with various new requirements, which may result in significant additional costs.

To the extent applicable to our business or the businesses of our customers, these laws, regulations and industry standards could have negative effects on our business, including by increasing our costs and operating expenses, and/or delaying or impeding our deployment of new or existing core functionality or Value+ services. Compliance with these laws, regulations and industry standards requires significant management time and attention, and failure to comply could result in negative publicity, subject us to fines or penalties, expose us to litigation, or result in demands that we modify or cease existing business practices. In addition, the costs of compliance with, and other burdens imposed by, such laws, regulations and industry standards may adversely affect our customers' ability or desire to collect, use, process and store personal information using our software solutions, which could reduce overall demand for them. Even the perception of privacy and data security concerns, whether or not valid, may inhibit market acceptance of our software solutions. Furthermore, privacy and data security concerns may cause our customers' clients, vendors, employees and other industry participants to resist providing the personal information necessary to allow our customers to use our applications effectively. Any of these outcomes could adversely affect our business and operating results.

***We face a number of risks in our electronic payment services business that could adversely affect our business or operating results.***

In our electronic payments services business, we facilitate the processing of both inbound and outbound payments for our customers. These payments are settled through our sponsoring clearing bank, card payment processors, and other third-party

electronic payment services providers that we may contract with from time to time. Our electronic payment services subject us to a number of risks, including, but not limited to:

- liability for customer costs related to disputed or fraudulent transactions if those costs exceed the amount of the customer reserves we have, if any, during the clearing period or after payments have been settled to our customers;
- electronic processing limits on the amounts that any single electronic payment services provider, or collectively all of our electronic payment services providers, will underwrite;
- our reliance on sponsoring clearing banks, card payment processors and other electronic payment providers to process electronic transactions;
- failure by us, our electronic payment services providers or our customers to adhere to applicable laws, regulations and standards that apply to the provision of electronic payment services;
- continually evolving laws and regulations governing money transmission and anti-money laundering, the application or interpretation of which is not clear in some jurisdictions;
- incidences of fraud in our electronic payment services ecosystem, security breaches, errors, defects, failures, vulnerabilities or bugs in our electronic payment services business, or our failure to comply with required external audit standards; and
- our inability to increase our fees as the business evolves in a sufficient amount to maintain our existing margins.

If any of these risks related to our electronic payment services were to materialize, our business or operating results could be negatively affected. Although we attempt to structure and adapt our electronic payment services to comply with complex and evolving laws, regulations and standards, our underwriting efforts do not guarantee compliance. In the event that we are found to be in violation of our legal, regulatory or contractual requirements, we may be subject to monetary fines or penalties, cease and desist orders, mandatory product changes, or other liabilities that could have an adverse effect on our operating results.

Additionally, with respect to the processing of electronic payment transactions by our third-party electronic payment services providers, we are exposed to financial risk. Electronic payment transactions between our customer and another user may be returned for various reasons such as insufficient funds, fraud or stop payment orders. If we or our electronic payment services provider is unable to collect such amounts from the customer's account (such as if the customer is illegitimate, or if the customer refuses or is unable to reimburse us for the amounts charged back), we bear the ultimate risk of loss for the transaction amount. While we have not experienced material losses resulting from amounts charged back in the past, there can be no assurance that we will not experience these types of losses in the future.

In addition, there is an overarching risk stemming from the potential widespread adoption of quickly evolving financial technology products, including, for example, blockchain or other distributed ledger technologies, that could materially impact the manner in which payments are processed, the mix of payment methodologies conventionally utilized by payors and payees, and the regulatory framework applicable to such payments. The adoption of disruptive financial technologies could significantly reduce the volume of our electronic payment services business or change the transaction costs associated with or potential revenue derived from those payments, thereby reducing our revenue and increasing our associated expenses, which could materially impact our business, financial condition, and operating results.

***Evolution and expansion of our electronic payment services may subject us to additional risks and regulatory requirements.***

The evolution and expansion of our electronic payment services may subject us to additional risks and regulatory requirements, including, without limitation, laws and regulations governing money transmission and anti-money laundering. These requirements vary throughout the markets in which we operate, and several jurisdictions lack clarity with respect to the application and interpretation of these rules. Our efforts to comply with these rules could require significant management time and effort, as well as significant expenditures, and will not guarantee our compliance with all regulatory requirements, especially given that the applicable regulatory frameworks are constantly changing and subject to evolving interpretation. While we maintain a compliance program focused on applicable laws and regulations throughout our applicable industries, there is no guarantee that we will not be subject to fines, penalties or other regulatory actions in one or more jurisdictions, or be required to adjust our business practices to accommodate future regulatory requirements.

***We face a number of risks in our tenant screening services business that could adversely affect our business or operating results.***

Our tenant screening services business is subject to a number of complex laws that are subject to varying interpretations, including without limitation the Fair Credit Reporting Act (the "FCRA") and related regulations. The FCRA has recently been the subject of multiple class-based litigation proceedings, as well as numerous regulatory inquiries and enforcement actions. In addition, entities such as the Federal Trade Commission (the "FTC") and the Consumer Financial Protection Bureau ("CFPB") have the authority to promulgate rules and regulations that may impact our customers and our business. Although we attempt to structure and adapt our tenant screening services to comply with these and other relevant laws and regulations, we may from time to time be found to be in violation of them. Further, regardless of our compliance with applicable laws and regulations, we may from time to time be subject to regulatory inquiries, enforcement actions, class-based litigation or indemnity demands.

As previously disclosed, we received a Civil Investigative Demand from the FTC in December 2018 requesting certain information relating to our compliance with the FCRA in connection with our tenant screening services business. On April 30, 2020, the FTC staff informed us of its belief that there is a reasonable basis for asserting claims against us for our alleged failure to comply with certain sections of the FCRA that could result in monetary penalty and injunctive relief. We are unable to predict the outcome of, or any potential costs or penalties associated with, this matter at this time.

In addition, we completed the settlement of a class action lawsuit related to alleged violations of the FCRA in 2019. Further, we received a Request for Information from the Civil Rights Division (Housing and Civil Enforcement Section) of the U.S. Department of Justice in July 2019 requesting certain information relating to our compliance with the Servicemembers Civil Relief Act in connection with our tenant screening services business.

Due to the large number of tenant screening transactions in which we participate, our potential liability in an enforcement action or a class action lawsuit could have a material impact on our business, especially given that certain applicable laws and regulations provide for fines or penalties on a per occurrence basis. The existence of any such enforcement action or class action lawsuit, whether meritorious or not, may adversely affect our ability to attract customers, result in the loss of existing customers, harm our reputation and cause us to incur defense costs or other expenses. Any of the foregoing events may have a material adverse impact on our business, financial condition, and operating results.

***We use third-party service providers for important electronic payment and tenant screening services, and their failure to fulfill their contractual obligations could harm our reputation, disrupt our business and adversely affect our operating results.***

We use third-party electronic payment services providers to enable us to provide electronic payment services to our customers, and third-party tenant screening services providers to enable us to provide tenant screening services, such as background and credit checks, to our customers. We rely on these service providers to provide us with accurate and timely information, and therefore have significantly less control over our electronic payment and tenant screening services than if we were to maintain and operate them ourselves. In some cases, functions necessary to our business are performed on proprietary third-party systems and software to which we have no access. We also generally do not have long-term contracts with these service providers. In addition, some of these service providers compete with us directly or indirectly in the markets we serve. The failure of these service providers to provide us with accurate and timely information, to fulfill their contractual obligations to us, or to renew their contracts with us, all of which may be more likely in light of the impacts and disruptions caused by the COVID-19 pandemic, could result in direct liability to us, harm our reputation, result in significant disruptions to our business, and adversely affect our operating results.

***Our corporate culture has contributed to our success and, if we cannot continue to foster this culture as we grow, we could lose the passion, creativity, teamwork, focus and innovation fostered by our culture.***

We believe that our culture has been and will continue to be a key contributor to our success. If we do not continue to develop our corporate culture or maintain our core values as we grow and evolve, we may be unable to foster the passion, creativity, teamwork, focus and innovation we believe we need to support our growth. Any failure to preserve our culture could negatively affect our ability to recruit and retain personnel and to effectively focus on and pursue our strategic objectives. Moreover, liquidity available to our employee security holders could lead to disparities of wealth among our employees, which could adversely impact relations among employees and our culture in general. As we grow and mature as a public company, we may find it difficult to maintain our corporate culture. This difficulty will only be exacerbated by the COVID-19 pandemic, which has resulted in travel restrictions, quarantines, shelter-in-place orders and similar government orders and restrictions that collectively make it more difficult for employees to interact, communicate and innovate.

***If we lose key members of our management team, our business may be harmed.***

Our success and future growth depend, in part, upon the continued services of our executive officers and other key employees. From time to time, there may be changes in our executive officers or other key employees resulting from the hiring or departure of these personnel, which may disrupt our business. Our executive officers and other key employees are generally employed on an at-will basis, which means that these personnel could terminate their employment with us at any time. Additionally, the equity awards held by many of our executive officers and other key employees are close to fully vested, and these employees may not have sufficient financial incentive to stay with us. The loss of one or more of our executive officers or other key employees, or the failure by our executive team to work effectively with our employees and lead our company, could have an adverse effect on our business.

***We depend on highly skilled personnel and, if we are unable to retain or hire additional qualified personnel, we may not be able to achieve our strategic objectives.***

To execute our growth plan and achieve our strategic objectives, we must continue to attract and retain highly qualified and motivated personnel across our organization. In particular, in order to continue to enhance our software solutions, add new and innovative core functionality and/or Value+ services, as well as develop new products, it will be critical for us to increase the size of our research and product development organization, including hiring highly skilled software engineers. Competition for software engineers is intense within our industry and there continues to be upward pressure on the compensation paid to these professionals. In addition, in order for us to achieve broader market acceptance of our software solutions, grow our customer base, and pursue adjacent markets and new verticals, we will need to continue to increase the size of our sales and marketing and customer service and support organizations. Identifying and recruiting qualified personnel, training them in the use of our software solutions, and ensuring they are well-equipped to provide great service to our customers, requires a significant investment of time and resources, and it can be particularly difficult to retain these individuals.

Many of the companies with which we compete for experienced personnel have greater name recognition and financial resources than we have. In addition, our headquarters are located in Santa Barbara, California, which is not generally recognized as a prominent commercial center, and it is challenging to attract qualified professionals due to our geographic location. As a result, we may have even greater difficulty hiring and retaining skilled personnel than our competitors. If we hire employees from other companies, their former employers may attempt to assert that we or these employees have breached their legal obligations, resulting in a diversion of our time and resources.

In addition, prospective and existing employees often consider the value of the equity awards they receive in connection with their employment. If the perceived value of our equity awards declines, or if the price of our Class A common stock experiences significant volatility, this may adversely affect our ability to recruit and retain highly skilled employees. If we are unable to attract and retain the personnel necessary to execute our growth plan, we may be unable to achieve our strategic objectives and our operating results may suffer.

As of March 2020, in an effort to manage the financial uncertainty involved with the COVID-19 pandemic, we have delayed the hiring of certain non-essential employees and deferred the retention of certain contractors. The timeline for when we may resume ordinary hiring activities is highly uncertain and subject to change.

***The markets in which we participate are intensely competitive and, if we do not compete effectively, our business could be harmed.***

The overall market for business management software is global, highly competitive and continually evolving in response to a number of factors, including changes in technology, operational requirements, and laws and regulations. The market for cloud-based business management software is also highly competitive and subject to similar market factors.

While we focus on providing industry-specific, cloud-based business management software solutions in our targeted verticals, we compete with other vertical cloud-based solution providers, as well as with horizontal cloud-based solution providers that provide broad cloud-based solutions across multiple verticals. Our competitors include established vertical software vendors, as well as newer entrants in the market. We also face competition from numerous cloud-based solution providers that focus almost exclusively on one or more point solutions. Continued consolidation among cloud-based providers could lead to significantly increased competition.

Although the domain expertise required to successfully develop, market and sell cloud-based business management software solutions in the real estate and legal verticals may hinder new entrants that are unable to invest the necessary resources to develop and deploy cloud-based solutions with the same level of functionality as ours, many of our competitors and potential competitors are larger and have greater name recognition, longer operating histories, and significantly greater resources than we do. As a result, our competitors may be able to respond more quickly and effectively to new or changing opportunities, technologies,

operational requirements and industry standards, as well as to new challenges such as those resulting from the COVID-19 pandemic. Some of these competitors may have more established customer relationships or strategic partnerships with third parties that enhance their products and services. Other competitors may offer products or services that address one or a number of business functions on a standalone basis at lower prices or bundled as part of a broader product sale, or with greater depth than our software solutions. In addition, our current and potential competitors may develop, market and sell new technologies with comparable functionality to our software solutions, which could cause us to lose customers, slow the rate of growth of new customers and cause us to decrease our prices in order to remain competitive. For all of these reasons, we may not be able to compete effectively against our current and future competitors, which could harm our business.

***Business management software for small and medium-sized businesses ("SMBs") is a relatively new and developing market and, if the market is smaller than we estimate or develops more slowly than we expect, our operating results could be adversely affected.***

We provide cloud-based business management software for SMBs in the real estate and, to a lesser extent, legal markets and will assess entry into new or adjacent markets consistent with our strategic plan. Our success will depend, in part, on the continued widespread adoption by SMBs of cloud computing in general and of cloud-based business management software in particular.

The market for industry-specific, cloud-based business management software for SMBs, both generally, and specifically within the real estate and legal markets, is evolving and, in comparison to the overall market for cloud-based solutions, is relatively small. The continued expansion of this market depends on numerous factors, including:

- the cost and perceived value associated with cloud-based business management software relative to on-premise software applications and disparate point solutions;
- the ability of cloud-based solution providers to offer SMBs the functionality they need to operate and grow their businesses;
- the willingness of SMBs to transition from their existing software systems, or otherwise alter their existing businesses practices, to migrate their businesses to a vertical cloud-based business management software solution; and
- the ability of cloud-based solution providers to address security, privacy, availability and other concerns.

Notwithstanding our efforts to increase sales of our software solutions to larger customers, if cloud-based business management software does not continue to achieve widespread market acceptance among SMBs, our revenue may increase at a slower rate than we expect and may even decline, which could adversely affect our operating results. In addition, it is difficult to estimate the rate at which SMBs will be willing to transition to vertical cloud-based business management software in any particular period, which makes it difficult to estimate the overall size and growth rate of the market for cloud-based business management software for SMBs at any given point in time or to forecast growth in our revenue or market share. This transition rate may be negatively impacted by the COVID-19 pandemic as customers may delay decisions to adopt our core products, or expand the use of our Value+ services, as they seek to reduce or delay spending within their businesses.

***If we are unable to introduce successful enhancements, including new and innovative core functionality and/or Value+ services, or new products for adjacent markets or additional verticals, our operating results could be adversely affected.***

The software industry in general, and our targeted verticals in particular, are characterized by rapid technological advances, changing industry standards, evolving customer requirements and intense competition. Our ability to attract new customers, increase revenue from our existing customers, and expand into adjacent markets or new verticals depends, in part, on our ability to enhance the functionality of our existing software solutions by introducing new and innovative core functionality and/or Value+ services that keep pace with technological developments and address the evolving business needs of our customers. In addition, our growth over the long term depends, in part, on our ability to introduce new products for adjacent markets and, potentially, additional verticals that we identify through our market validation process. Market acceptance of our current and future software solutions will depend on numerous factors, including:

- the unique functionality and ease of use of our software solutions and the extent to which our software solutions meet the business needs of our customers;
- the perceived benefits and security of our cloud-based business management software solutions relative to on-premise software applications or other competitive products;



- the pricing of our software solutions relative to competitive products;
- the availability of financial resources to new and existing customers to allow them to acquire or expand the use of our software solutions;
- perceptions about the security, privacy and availability of our software solutions relative to competitive products;
- time-to-market of the updates and enhancements to our core functionality, Value+ services and new products; and
- perceptions about the quality and responsiveness of our customer service organization.

If we are unable to successfully enhance the functionality of our existing software solutions, including our core solutions and Value+ services, and timely develop or acquire new products that gain market acceptance in adjacent markets and additional verticals consistent with our strategic plan, our revenue may increase at a slower rate than we expect and may even decline, which could adversely affect our operating results. These efforts to enhance our existing software solutions and develop new products, as well as our overall research and product development efforts, may be negatively impacted by the COVID-19 pandemic.

***Our business depends substantially on existing customers renewing their subscriptions with us and expanding their use of our Value+ services, and a decline in customer renewal rates, or failure to convince existing customers to adopt and utilize our Value+ services, could adversely impact our operating results.***

In order for us to maintain or increase our revenue and improve our operating results, it is important that our existing customers continue to pay subscription fees for the use of our core solutions, which tend to incrementally rise over time, as well as increase their adoption and utilization of our Value+ services. Our customers have no obligation to renew their subscriptions with us upon expiration of their subscription periods, which typically range from one month to one year. We cannot assure you that our customers will renew their subscriptions with us. In addition, our law firm customers that start their accounts using a 10-day free trial have no obligation to begin a paid subscription. Furthermore, although a significant portion of our revenue growth has historically resulted from the adoption and utilization of our Value+ services by our existing customers, we cannot assure you that our existing customers will continue to broaden their adoption and utilization of our Value+ services, or use our Value+ services at all. If our existing customers do not renew their subscriptions and increase their adoption and utilization of our existing or newly developed Value+ services, our revenue may increase at a slower rate than we expect and may even decline, which could adversely impact our financial condition and operating results. We may experience lower rates of subscription renewals, as well as lower rates of adoption and utilization of Value+ services, as a result of the COVID-19 pandemic as customers may seek to reduce or delay spending within their businesses.

Word-of-mouth referrals represent a significant source of new customers for us and provide us with an opportunity to cost-effectively market and sell our software solutions. The loss of our existing customers could have a significant impact on our reputation in our targeted verticals and our ability to acquire new customers cost-effectively. A reduction in the number of our existing customers, even if offset by an increase in new customers, could have the impact of reducing our revenue and operating margins.

In an effort to retain our customers and to expand our customers' adoption and utilization of our Value+ services, we may choose to use increasingly costly sales and marketing efforts. In addition, we may make significant investments in research and product development to introduce Value+ services that ultimately are not broadly adopted by our customers. In either of those cases, we could incur significantly increased costs without a corresponding increase in revenue. Furthermore, we may fail to identify Value+ services that our customers need for their businesses, in which case we could miss opportunities to increase our revenue.

***Pricing pressure may cause us to change our pricing model, which could hurt our renewal rates and our ability to attract new customers, as well as our ability to increase adoption and usage of our Value+ services, which could adversely affect our operating results.***

As the markets for our existing software solutions mature, or as current and future competitors introduce new products or services that compete with ours, we may experience pricing pressure and be unable to renew our subscription agreements with existing customers or increase adoption and usage of our Value+ services, or attract new customers at prices that are consistent with our current pricing model and operating budget. If this were to occur, it is possible that we would have to change our pricing model, offer pricing incentives, or generally reduce our prices, which may adversely affect our revenue even if adoption and utilization remain constant. In addition, many of our customers are smaller companies or firms, which are typically more cost sensitive than larger enterprises. Changes to our pricing model could harm our customer retention rates and our ability to attract

new customers, whether in connection with our core solutions or our Value+ services, which could adversely affect our operating results.

***We expect to continue to derive a significant portion of our revenue from our real estate customers, and factors resulting in a loss of these customers could adversely affect our operating results.***

Historically, more than 90% of our revenue has been derived from real estate customers, and we expect that our real estate customers will continue to account for a significant portion of our revenue for the foreseeable future. We could lose real estate customers as a result of numerous factors, including:

- the expiration and non-renewal of subscriptions or termination of subscription agreements;
- the introduction of competitive products or technologies;
- our failure to provide updates and enhancements to our core functionality and/or Value+ services, and to introduce new Value+ services to our customers;
- changes in pricing policies by us or our competitors;
- acquisitions or consolidations within the real estate vertical;
- bankruptcies or other financial difficulties facing our real estate customers, especially in light of the impacts and disruptions caused by the COVID-19 pandemic;
- new or enhanced legal or regulatory regimes that negatively impact the real estate vertical; and
- conditions or trends that are specific to the real estate vertical such as the economic factors that impact the rental market.

The loss of a significant number of our real estate customers, or the loss of even a small number of our larger real estate customers, could cause our revenue to increase at a slower rate than we expect or even decline. In addition, even if we are able to retain our real estate customers, we may be unable to grow revenue from these real estate customers by increasing their adoption and utilization of our Value+ services. Any of these outcomes could adversely affect our operating results.

***If we are unable to increase sales of our software solutions to larger customers while mitigating the risks associated with serving such customers, our business and operating results may suffer.***

While we plan to continue to market and sell our software solutions to smaller companies or firms, our growth strategy is dependent, in part, upon increasing sales of our software solutions to larger customers within the real estate and legal markets. Sales to larger customers may involve risks that are not present, or are present to a lesser extent, in sales to smaller businesses. As we seek to increase our sales to larger customers, we may invest considerably greater amounts of time and financial resources in our sales and marketing efforts. In addition, we may face longer sales cycles and experience less predictability and greater competition in completing some of our sales than we have in selling our software solutions to smaller businesses. Although we generally have not configured our software solutions or negotiated our pricing for specific customers, which has historically resulted in reduced upfront selling costs, our ability to successfully sell our software solutions to larger customers may be dependent, in part, on our ability to develop functionality, or to implement pricing policies, that are unique to particular customers or are necessary for success in a market segment dominated by larger customers. It may also be dependent on our ability to attract and retain sales personnel with experience selling to larger organizations. Also, because security breaches or other performance problems with respect to larger customers may result in greater economic harm to these customers and more adverse publicity, there is increased financial and reputational risk associated with serving such customers. Further, our ability to sell our software solutions to larger customers may depend largely upon our successful acquisition and integration of synergistic businesses and, if we are unable to acquire and integrate such businesses successfully, our business and operating results may be negatively impacted. If we are unable to increase sales of our software solutions to larger customers, while mitigating the risks associated with serving such customers, our business and operating results may suffer.

***Our growth depends in part on the success of our strategic relationships with third parties, and if we are unsuccessful in establishing or maintaining these relationships, our ability to compete in our targeted markets or grow our revenue could be impaired.***

In order to grow our business, we anticipate that we will continue to depend on our relationships with third parties, including our data center operators, cloud computing service providers, electronic payment, tenant screening and insurance services

providers, and other third parties that support delivery of our software solutions. Identifying partners, negotiating agreements and maintaining relationships requires significant time and resources. Our competitors may be more effective than us in cost-effectively building relationships with third parties that enhance their products and services, allow them to provide more competitive pricing, or offer other benefits to their customers. In addition, acquisitions of our partners by our competitors or others could result in a decrease in the number of current and potential strategic partners willing to establish or maintain relationships with us, and could increase the price at which products or services are available to us. If we are unsuccessful in establishing or maintaining our relationships with third parties, our ability to compete in the marketplace or to grow our revenue could be impaired, which could negatively impact our operating results. Even if we are successful, we cannot assure you that these relationships will result in increased customer adoption and usage of our software solutions or improved operating results. Furthermore, if our partners fail to perform as expected, we may be subjected to litigation, our reputation may be harmed, and our business and operating results could be adversely affected.

***We depend on data centers and computing infrastructure operated by third parties and any disruption in these operations could adversely affect our operating results.***

We currently serve our customers through a combination of our own servers located in third party data center facilities, and computing resources operated by Amazon and other third party cloud computing service providers. While we control and have access to our own servers and the other components of our network that are located in our third party data centers, we do not control the operation of any of these third party data center facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, or if one of our third party data center operators is acquired, we may be required to transfer our servers and other infrastructure to new data center facilities, and we may incur significant costs and possible service interruptions in connection with doing so. Further, our third party data center providers could experience significant outages outside of our control that could adversely affect our business.

Problems faced by our third party data center operators, or with any of the service providers with whom we or they contract, could adversely affect the experience of our customers. Our third party data center operators could decide to close their facilities without adequate notice. In addition, any financial difficulties or bankruptcies, faced by our third party data center operators, or any of the service providers with whom we or they contract, including as a result of the impacts and disruptions caused by the COVID-19 pandemic, may have a negative effect on our business. Additionally, if our data centers are unable to keep up with our growing needs for capacity or any spikes in customer demand, this could have an adverse effect on our business. Any changes in third party service levels at our data centers could result in loss of or damage to our customers' stored information and service interruptions, which could harm our reputation. These issues could also cause us to lose customers, harm our ability to attract new customers, and subject us to potential liability, any of which could adversely affect our operating results.

The cloud computing service providers with which we contract may experience service interruptions across multiple regions that are outside of our control. Furthermore, they may not be able to provide us with additional computing resources needed to scale our infrastructure ahead of our growing customer base. If any of these issues arise, we may be required to migrate our cloud computing resources, or add new computing resources, to other cloud computing service providers. Although our infrastructure is redundant across multiple geographic regions, it might require significant effort to migrate all of our services to a different region if we are forced to recover from a data center's severe impairment or total destruction, or from a regional, or multi-regional, outage by any of our cloud computing service providers. Any changes in service levels by our cloud computing service providers could result in loss of or damage to our customers' stored information and service interruptions, which could harm our reputation, subject us to potential liability, and adversely affect our operating results.

***Our platform must integrate with a variety of devices, operating systems and browsers that are developed by others, and if we are unable to ensure that our software solutions interoperate with such devices, operating systems and browsers, our software solutions may become less competitive, and our operating results may be harmed.***

We offer our software solutions across a variety of operating systems and through the Internet. We are dependent on the interoperability of our platform with third party devices, desktop and mobile operating systems, as well as web browsers that we do not control. Any changes in such devices, systems or web browsers that degrade the functionality of our software solutions or give preferential treatment to competitive services could adversely affect adoption and usage of our software solutions. In addition, in order to deliver high quality software solutions, we will need to continuously enhance and modify our functionality to keep pace with changes in Internet-related hardware, mobile operating systems such as iOS and Android, browsers and other software, communication, network and database technologies. We may not be successful in developing enhancements and modifications that operate effectively with these devices, operating systems, web browsers and other technologies or in bringing them to market in a timely manner. Furthermore, uncertainties regarding the timing or nature of new network platforms or technologies, and modifications to existing platforms or technologies, could increase our research and product development expenses. In the event

that it is difficult for our customers to access and use our software solutions, our software solutions may become less competitive, and our operating results could be adversely affected.

***If our property management customers stop requiring residents to provide proof of legal liability to landlord insurance, if insurance premiums decline or if insureds experience greater than expected losses, our operating results could be harmed.***

We generate revenue by offering legal liability to landlord insurance through a wholly owned subsidiary. Some of our property management customers require residents to provide proof of legal liability to landlord insurance and offer to enroll residents in their legal liability to landlord insurance policy. If demand for rental housing declines, or if our property management customers believe that it may decline, these customers may reduce their rental rates and stop requiring residents to provide proof of legal liability to landlord insurance in order to reduce the overall cost of renting and make their rental offerings more competitive. If our property management customers stop requiring residents to provide proof of legal liability to landlord insurance or elect to enroll residents in insurance programs offered by competing providers, or if insurance premiums otherwise decline, our revenues from insurance services could be adversely affected.

Additionally, our legal liability to landlord insurance policies are underwritten by us, and we are required by our insurance partner to maintain a reserve to cover potential claims under the policies. While our policies have a limit of \$100,000 per occurrence, there is no limit on the dollar amount of claims that could be made against us in any particular period or in the aggregate. In the event that claims by the insureds increase unexpectedly, our reserve may not be sufficient to cover our resulting liability under the policies. To the extent we are required to pay out amounts to insureds that are significantly higher than our current reserves, this could have a material adverse impact on our operating results.

***Our insurance business is subject to state governmental regulation, which could limit the growth of our insurance business and impose additional costs on us.***

Our insurance-related wholly owned subsidiaries and third-party service providers maintain licenses with a number of individual state departments of insurance. Collectively, we are subject to state governmental regulation and supervision in connection with the operation of our insurance business, which includes both our legal liability to landlord insurance and renters insurance businesses. This state governmental supervision could limit the growth of our insurance business by increasing the costs of regulatory compliance, limiting or restricting the products or services we provide or the methods by which we provide them, and subjecting us to the possibility of regulatory actions or proceedings. Our continued ability to maintain these insurance licenses in the jurisdictions in which we are licensed depends on our compliance with the rules and regulations promulgated from time to time by the regulatory authorities in each of these jurisdictions. Furthermore, state insurance departments conduct periodic examinations, audits and investigations of the affairs of insurance companies and agencies, any of which could result in the expenditure of significant management time or financial resources.

In all jurisdictions, the applicable laws and regulations are subject to amendment and interpretation by regulatory authorities. Generally, such authorities are vested with relatively broad discretion to grant, renew and revoke licenses and approvals and to implement and interpret rules and regulations. Accordingly, we may be precluded or temporarily suspended from carrying on some or all of the activities of our insurance business or otherwise be fined or penalized in a given jurisdiction. No assurances can be given that our insurance business can continue to be conducted in any given jurisdiction as it has been conducted in the past or that we will be able to expand our insurance business in the future.

***If we are unable to enter new verticals, or if our software solution for any new vertical fails to achieve market acceptance, our operating results could be adversely affected and we may be required to reconsider our growth strategy.***

Our growth strategy is dependent, in part, on our ability to expand into new verticals, beyond the real estate and legal markets. However, we may be unable to identify new verticals that meet our criteria for selecting industries that cloud-based solutions are ideally suited to address. In addition, our market validation process may not support entry into selected verticals due to our perception of the overall market opportunity or of the willingness of market participants within those verticals to adopt our software solutions. Further, instead of pursuing new verticals, we may prefer for various reasons to pursue alternative growth strategies, such as entry into markets that are adjacent to the markets in which we currently participate within our existing verticals, or the development of additional products or services for our existing markets.

Even if we choose to enter new verticals, our market validation process does not guarantee our success. We may be unable to develop a software solution for a new vertical or, in the event that we enter a new vertical by way of a strategic acquisition, we may be unable to leverage the acquired software solution in time to take advantage of the identified market opportunity, and any delay in our time-to-market could expose us to additional competition or other factors that could impede our success. In addition, any software solution we develop or acquire for a new vertical may not provide the functionality required by potential customers

and, as a result, may not achieve widespread market acceptance within the new vertical. To the extent we choose to enter new verticals, whether organically or via strategic acquisition, we may invest significant resources to develop and expand the functionality of our software solutions to meet the needs of customers in those verticals, which investments will occur in advance of our realization of revenue from them.

In addition, while we expedited our entry into the legal vertical through the acquisition of MyCase in 2012, our practice and case management solution is in an earlier stage of development than APM, our property management solution, and we are at an earlier stage in the process of expanding the core functionality and Value+ services associated with our legal software. We face significant competition in the legal market from both vertical software vendors and cloud-based solution providers that offer one or more point solutions. There can be no assurance that we will be able to achieve market acceptance for our legal software at or near the levels achieved by our property management software.

***All of our revenues are generated by sales to customers in our targeted verticals, and factors that adversely affect the applicable industry could also adversely affect us.***

Currently, all of our sales are to customers in the real estate market and, to a lesser extent, the legal market. Demand for our software solutions and services could be affected by factors that are unique to and adversely affect our targeted verticals. In particular, the real estate and legal markets, as well as many of the software solutions and services we offer in those markets, are highly regulated across multiple federal, state and local jurisdictions, subject to intense competition and impacted by changes in general economic and market conditions. For example, changes in applicable laws and regulations could significantly impact the features and functionality demanded by our customers and require us to expend significant resources to ensure our software solutions continue to meet their evolving needs. In addition, other industry-specific factors, such as industry consolidation or the introduction of competing or disruptive technology, could lead to a significant reduction in the number of customers that use our software solutions or the Value+ services demanded by these customers. Further, if the real estate or legal markets decline, our customers may decide not to renew their subscriptions or they may cease using our Value+ services in order to reduce costs to remain competitive. It is possible that the significant increase in unemployment rates and financial uncertainty caused by the COVID-19 pandemic could have a disproportionate impact on businesses within the real estate and legal markets. As a result, our ability to generate revenue from our real estate and legal market customers could be adversely affected, which could have a material adverse impact on our business, financial condition and operating results.

In addition to the foregoing risks associated with our targeted verticals themselves, there is an overarching risk stemming from potential widespread adoption of quickly evolving financial or other disruptive technology products that could significantly impact our targeted verticals, even if that technology is not specifically designed to apply directly to our targeted verticals. The adoption of these new technologies could significantly reduce the volume or demand of customers in our targeted verticals, thereby reducing our revenue, which could materially impact our business, financial condition and operating results.

***If we are unable to deliver effective customer service, it could harm our relationships with our existing customers and adversely affect our ability to attract new customers.***

Our business depends, in part, on our ability to satisfy our customers, both by providing software solutions that address their business needs, and by providing onboarding services and ongoing customer service, which contributes to retaining customers and increasing adoption and utilization of our Value+ services by our existing customers. Once our software solutions are deployed, our customers depend on our customer service organization to resolve technical issues relating to their use of our solutions. We may be unable to respond quickly to accommodate short-term increases in customer demand for support services or may otherwise encounter a customer issue that is difficult to resolve. If a customer is not satisfied with the quality or responsiveness of our customer service, we could incur additional costs to address the situation. As we do not separately charge our customers for support services, increased demand for our support services would increase costs without corresponding revenue, which could adversely affect our operating results. In addition, regardless of the quality or responsiveness of our customer service efforts, a customer that is not satisfied with an outcome may choose to terminate, or not to renew, their relationship with us.

Our sales process is highly dependent on the ease of use of our software solutions, our reputation and positive recommendations from our existing customers. Any failure to maintain high-quality or responsive customer service, or a market perception that we do not maintain high-quality or responsive customer service, could harm our reputation, cause us to lose customers and adversely impact our ability to sell our software solutions to prospective customers. Challenges associated with maintaining a responsive customer service organization may be exacerbated as a result of the COVID-19 pandemic, especially as we transition to a remote work environment.

***Our software solutions address functions within the heavily regulated real estate and legal markets, and our customers' failure to comply with applicable laws and regulations could subject us to litigation.***

We sell our software solutions to customers within the real estate market and, to a lesser extent, the legal market. Our customers use our software solutions for business activities that are subject to a number of laws and regulations, including without limitation federal, state and local real property laws and legal ethics rules. Any failure by our customers to comply with laws and regulations applicable to their businesses could result in fines, penalties or claims for substantial damages against our customers. To the extent our customers believe, or any other potentially aggrieved stakeholder believes, that our software solutions or our customer service and support organization caused or contributed to such failures, our customers and/or other third parties may make claims for damages against us, regardless of whether we are responsible for the failure. As a result, we may be subject to lawsuits or other proceedings that, even if unsuccessful, could divert our resources and our management's attention and adversely affect our business, and our insurance coverage may not be sufficient to cover such claims against us.

***If we are unable to maintain and promote our brands, or to do so in a cost-effective manner, our ability to maintain and expand our customer base will be impaired, and our operating results could be adversely affected.***

We believe that maintaining and promoting our brands is critical to achieving widespread awareness and acceptance of our software solutions, and maintaining and expanding our customer base. We also believe that the importance of brand recognition will increase as competition in our targeted verticals increases. If we do not continue to build awareness of our brands, we could be placed at a competitive disadvantage as compared to companies whose brands are, or become, more recognizable than ours. Maintaining and promoting our brands will depend, in part, on our ability to continue to provide new and innovative core functionality and Value+ services and best-in-class customer service, as well as the effectiveness of our sales and marketing efforts. If we fail to deliver products and functionality that address our customers' business needs, or if we fail to meet our customers' expectations for customer service, it could weaken our brands and harm our reputation. Our inability to meet in person with prospective or existing customers during the COVID-19 pandemic may have an adverse impact on our relationships with current or prospective customers, and reduce the demand for our software solutions. Additionally, the actions of third parties which are out of our control may affect our brands and reputation if customers do not have a positive experience using the services of our third party partners that support our software solutions. Maintaining and enhancing our brands may require us to make substantial investments, and these investments may not result in commensurate increases in our revenue. If we fail to successfully maintain and promote our brands, or if we make investments that are not offset by increased revenue, our operating results could be adversely affected.

***Failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brands, which could harm our business.***

We currently rely on patent, trademark, copyright and trade secret laws, trade secret protection and confidentiality or license agreements with our employees, customers, partners and others to protect our intellectual property rights. Our success and ability to compete depend, in part, on our ability to continue to protect our intellectual property, including our proprietary technology and our brands. If we are unable to protect our proprietary rights adequately, our competitors could use the intellectual property we have developed to enhance their own products and services, which could harm our business.

In order to monitor and protect our intellectual property rights, we may be required to expend significant resources. Litigation brought to protect and enforce our intellectual property rights could be costly, time-consuming and distracting to management, and could result in the impairment or loss of portions of our intellectual property or require us to pay costly royalties. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. Accordingly, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property. Our failure to secure, protect and enforce our intellectual property rights could adversely affect our business and operating results.

***We may be sued by third parties for alleged infringement of their proprietary rights, which could cause us to incur significant expenses and require us to pay substantial damages.***

There is considerable patent, trademark, copyright, trade secret and other intellectual property development activity in our industry. Our success depends, in part, on our not infringing upon the intellectual property rights of others. Our competitors, as well as a number of other entities and individuals, may legally own or claim to own intellectual property relating to our technology or software solutions, including without limitation technology we develop and build internally and that which we acquire. From time to time, our competitors or other third parties may claim that we are infringing upon their intellectual property rights. However, we may be unaware of the intellectual property rights that others may claim cover some or all of our technology or software solutions. Any claims or litigation, regardless of merit, could cause us to incur significant expenses and, if successfully asserted against us, could require that we pay substantial damages, settlement costs or ongoing royalty payments, require that we comply with other unfavorable license and other terms, or prevent us from offering our software solutions in their current form. Even if

the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the attention of our management and key personnel from our business operations and harm our operating results.

***We have incurred and expect to continue to incur significant costs as a result of operating as a public company, and our management is required to devote substantial time to compliance with legal requirements and corporate governance initiatives.***

As a public company, we have incurred and expect to continue to incur significant legal, accounting, compliance and other expenses. We are subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Sarbanes-Oxley Act of 2002, the listing requirements of the NASDAQ Global Market, and other applicable securities rules and regulations. Compliance with these rules and regulations will continue to increase our legal and financial compliance costs, make some activities more difficult, time-consuming or costly, and increase demand on our systems and resources.

In addition, changing laws, regulations and standards relating to corporate governance and public disclosure requirements are creating uncertainty for public companies, increasing legal and financial compliance costs, and making some activities more difficult and time consuming. These laws, regulations and standards are subject to varying interpretations and their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to governance practices. We intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative expenses and a diversion of management's time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new laws, regulations and standards differ from the activities intended by regulatory or governing bodies, regulatory authorities may initiate legal proceedings against us, which could result in a material adverse impact on our business.

***Because we recognize revenue from subscriptions for our software solutions over the term of each subscription agreement, downturns or upturns in new business may not be immediately reflected in our operating results.***

We recognize revenue from customers ratably over the term of each subscription agreement, which typically ranges from one month to one year. As a result, some of the revenue we report in each period is derived from the recognition of deferred revenue relating to subscription agreements entered into during previous periods. Consequently, a decline in new or renewed subscriptions in any one period may not be reflected in our revenue results for that period. However, any such decline will negatively affect our revenue in future quarters. Our subscription model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription period. Accordingly, the effect of downturns or upturns in our sales, the market acceptance of our software solutions, and potential changes in our customer retention rates, may not be apparent in our operating results until future periods.

***Our software solutions contain both third-party and open source software, which may pose risks to our proprietary source code and/or introduce security vulnerabilities, and could have a negative impact on our business and operating results.***

We use open source software in our software solutions and expect to continue to do so in the future. The terms of many open source licenses to which we are subject have not been interpreted by United States or foreign courts, and there is a risk that open source licenses could be construed in a manner that imposes unanticipated conditions, restrictions or costs on our ability to provide or distribute our software solutions. Additionally, we may from time to time face claims from third parties alleging ownership of, or demanding release of, the open source software or of derivative works that we developed using such software, which could include our proprietary source code, or otherwise seeking to enforce the terms of the applicable open source license. These claims could result in litigation, which could be costly for us to defend, and could require us to make our source code freely available, purchase a costly license or cease offering the implicated functionality unless and until we can re-engineer them to avoid infringement. This re-engineering process could require significant additional research and product development resources, and we may not be able to complete it successfully or in a timely manner. In addition to risks related to license requirements, usage of certain open source software can lead to greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of software. These risks could be difficult to eliminate or manage, and could have a negative impact on our business and operating results.

We also use third-party commercial software in our software solutions and expect to continue to do so in the future. Third-party commercial software is developed outside of our direct control and may introduce security vulnerabilities that may be difficult to anticipate or mitigate. Further, there is no guarantee that third-party software developers or open source software providers will continue active work on the third-party software that we use. Should development of in-use third-party software cease, significant engineering effort may be required to create an in-house solution. These risks could also be difficult to eliminate or manage, and could have a negative impact on our business and operating results.

***There are risks associated with our outstanding and future indebtedness that could adversely affect our financial condition.***

As of March 31, 2020, we had \$48.3 million of outstanding indebtedness under a term loan that will mature on December 24, 2023 (the "Term Loan"), pursuant to our Credit Agreement with Wells Fargo, and we may incur additional indebtedness in the future and/or enter into new financing arrangements. In addition, as of March 31, 2020, we had \$49.0 million outstanding under our Revolving Facility with Wells Fargo. Our ability to meet expenses, to remain in compliance with the covenants under our debt instruments, and to pay fees, interest and principal on our substantial level of indebtedness depends on, among other things, our operating performance and market conditions, which are likely to be impacted by the significant disruptions caused by the COVID-19 pandemic. Accordingly, our cash flow may not be sufficient to allow us to pay principal and interest on our debt and meet our other obligations.

Our level of indebtedness could have important consequences, including the following:

- We must use a portion of our cash flow from operations to pay fees, interest and principal on the Term Loan and Revolving Facility which reduces funds available to us for other purposes such as working capital, capital expenditures, other general corporate purposes, and potential acquisitions;
- We may be unable to refinance our indebtedness or to obtain additional financing for working capital, capital expenditures, acquisitions, or general corporate purposes;
- We are exposed to fluctuations in interest rates because borrowings under our credit facilities bear interest at variable rates;
- Our leverage may be greater than that of some of our competitors, which may put us at a competitive disadvantage and reduce our flexibility in responding to current and changing industry and financial market conditions;
- We may be more vulnerable to an economic downturn and adverse developments in our business; and
- We may be unable to comply with financial and other covenants in our debt agreements, which could result in an event of default that, if not cured or waived, may result in acceleration of certain of our debt, have an adverse effect on our business and prospects and force us into bankruptcy or liquidation.

There can be no assurance that we will be able to manage any of these risks successfully.

In addition, we conduct a portion of our operations through our subsidiaries. Accordingly, repayment of our indebtedness will be dependent in part on the generation of cash flow by our subsidiaries and their ability to make such cash available to us by dividend, distribution or otherwise. Our subsidiaries may not be able to, or may not be permitted to, make distributions to enable us to make payments in respect of our indebtedness. Each subsidiary is a distinct legal entity, and under certain circumstances, legal and contractual restrictions may limit our ability to obtain cash from our subsidiaries. In the event that we do not receive distributions from our subsidiaries, we may be unable to make the required fee, interest and principal payments on our indebtedness.

***Financing agreements that we are party to or may become party to may contain operating and financial covenants that restrict our business and financing activities. Failure to comply with these covenants, or other restrictions, could result in default under these agreements.***

Our existing Credit Agreement with Wells Fargo as administrative agent, and the lenders that are parties thereto, which we refer to as the Second Amendment of our Original Credit Agreement, contains certain operating and financial restrictions and covenants, including limitations on dividends, dispositions of all or substantially all of our assets, mergers or consolidations, incurrence of indebtedness and liens, and other corporate activities. These restrictions and covenants, as well as those contained in any future financing agreements that we may enter into, may restrict our ability to finance our operations, and to engage in, expand or otherwise pursue our business activities and strategic objectives. The substantial uncertainty and financial impacts caused by the COVID-19 pandemic may cause Wells Fargo to seek to amend the Second Amendment of our Original Credit Agreement, which could, among other things, result in greater operational or financial restrictions on our business. Our ability to comply with these restrictions and covenants may be affected by events beyond our control, including disruptions to our business relating to the COVID-19 pandemic, and breaches of these covenants could result in a default under the Second Amendment of our Original Credit Agreement and any future financing agreements that we may enter into. If not waived, defaults could cause any outstanding indebtedness under the Second Amendment of our Original Credit Agreement and any future financing agreements that we may enter into to become immediately due and payable, and allow the lenders to proceed against any collateral securing that indebtedness.



***Our ability to use our net operating loss carryforwards and certain other tax attributes may be limited.***

As of December 31, 2019, the date of our most recent audited financial statements, we had federal net operating loss carryforwards of \$82.1 million, which will begin to expire in 2031. At December 31, 2019, we had state net operating loss carryforwards of \$65.9 million, which will begin to expire in 2028. At December 31, 2019, we also had federal and state research and development credit carryforwards of \$11.4 million and \$10.8 million, respectively. The federal credit carryforwards will begin to expire in 2027, while the majority state credits carryforwards apply indefinitely. Under Section 382 of the Internal Revenue Code of 1986, as amended, if a corporation undergoes an “ownership change,” the corporation’s ability to use its pre-change net operating loss carryforwards and other pre-change tax attributes, such as research tax credits, to offset its post-change income and taxes may be limited. In general, an “ownership change” occurs if there is a cumulative change in our ownership by “5% shareholders” that exceeds 50% over a rolling three-year period. Similar rules may apply under state tax laws. It is possible that our existing net operating loss and/or credit carryforwards may be subject to limitations arising from previous ownership changes, and future issuances of our stock could cause an ownership change. Furthermore, our ability to utilize net operating loss and/or credit carryforwards of companies that we have acquired or may acquire in the future may be subject to limitations. There is also a risk that due to legislative changes, such as suspensions on the use of net operating loss carryforwards, or other unforeseen reasons, our existing net operating loss carryforwards could expire or otherwise be unavailable to offset future income tax liabilities. In addition, under the Tax Cuts and Jobs Act, the amount of net operating loss carryforwards from taxable years beginning after December 31, 2017 that we are permitted to deduct in any taxable year is limited to 80% of our taxable income in such year, where taxable income is determined without regard to the net operating loss carryforward deduction itself. However, the Coronavirus Aid, Relief, and Economic Security Act (also known as the “CARES Act”) suspended this limitation for taxable years beginning before January 1, 2021. Nonetheless, for aforementioned reasons, we may not be able to realize a tax benefit, or may realize less tax benefit, from the use of our net operating loss carryforwards. Any such limitations on our ability to use our net operating loss carryforwards and other tax assets could adversely impact our business, financial condition and operating results.

***Tax laws or regulations could be enacted or changed and existing tax laws or regulations could be applied to us or to our customers in a manner that could increase the costs of our software solutions and adversely impact our operating results.***

The application of federal, state, local and foreign tax laws to services provided electronically is continuously evolving. New income, sales, use or other tax laws, statutes, rules, regulations or ordinances could be enacted or amended at any time, possibly with retroactive effect, and could be applied solely or disproportionately to services provided over the Internet. These enactments or amendments could adversely affect our sales activity due to the inherent cost increase the taxes would represent and could ultimately result in a negative impact on our operating results.

In addition, existing tax laws, statutes, rules, regulations or ordinances could be interpreted, modified or applied adversely to us, possibly with retroactive effect, which could require us or our customers to pay additional tax amounts, as well as require us or our customers to pay fines or penalties, as well as interest on past amounts. If we are unsuccessful in collecting such taxes due from our customers, we could be held liable for such costs, thereby adversely impacting our operating results.

***Because our long-term growth strategy involves expansion of our sales to customers outside the United States, our business will be susceptible to the risks associated with international operations.***

A component of our growth strategy involves the expansion of our international operations and worldwide customer base. To date, we have realized an immaterial amount of revenue from customers outside the United States. Operating in international markets will require significant resources and management attention and will subject us to regulatory, economic, geographic and political risks, including but not limited to the risk of disruptions caused by regional natural disasters or health epidemics, that are different from those in the United States. Because of our limited experience with international operations and significant differences between the United States and international markets, our international expansion efforts may not be successful in creating demand for our software solutions outside of the United States or in effectively selling our software solutions in any international markets we may enter. The significant disruptions caused by the COVID-19 pandemic, especially in certain countries in the European Union and Asia, could have a prolonged negative impact on our ability to expand our sales to customers outside the United States. If we invest substantial time and resources to expand our international operations and are unable to do so successfully, our business and operating results could suffer.

**Risks Related to Our Class A Common Stock**

***The market price of our Class A common stock may be volatile or may decline regardless of our operating performance, which could result in substantial losses for our stockholders.***

The market price of our Class A common stock has been, and is likely to continue to be, highly volatile, and fluctuations in the price of our Class A common stock could cause you to lose all or part of your investment. For example, from March 31, 2019 to March 31, 2020, the share price of our Class A common stock on the NASDAQ Global Market fluctuated between \$77.74 and \$148.07.

There are numerous factors that could cause fluctuations in the market price of our Class A common stock, including:

- volatility in the trading volume of our Class A common stock;
- price and volume fluctuations in the overall stock market;
- volatility in the market prices and trading volumes of securities issued by software companies;
- changes in operating performance and stock market valuations of software companies generally or those in our markets in particular;
- sales of shares of our Class A common stock by us or our stockholders, or perceptions that such sales may occur;
- any future announcements to repurchase our Class A common stock, and any actual share repurchases that we may undertake from time to time;
- failure of securities analysts to maintain coverage of us, changes in financial estimates by securities analysts who follow us, or our failure to meet these estimates or the expectations of investors;
- the guidance we may provide to the public, any changes in that guidance, and our performance relative to that guidance;
- announcements by us or our competitors of new products or services;
- public reaction to our press releases, filings with the SEC and other public announcements;
- rumors and market speculation involving us or other software companies;
- actual or anticipated changes in our operating results or fluctuations in our operating results;
- actual or anticipated developments in our business, our competitors' businesses or the competitive landscape generally;
- impacts from widespread public health crises, including the COVID-19 global pandemic;
- legal proceedings, enforcement actions or regulatory inquiries relating to us or our competitors or to the markets in which we operate;
- developments or disputes concerning our intellectual property or other proprietary rights;
- announced or completed acquisitions of businesses or technologies by us or our competitors;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business or the markets in which we operate;
- changes in accounting standards, policies, guidelines, interpretations or principles;
- changes in our management; and
- general economic conditions and trends, including the impacts and disruptions caused by the COVID-19 pandemic.

In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. If instituted against us, any such litigation, regardless of its merit or final outcome, could result in substantial costs and a diversion of our management's attention, thereby adversely affecting our operating results and, potentially, the price of our Class A common stock.

***The dual class structure of our common stock has the effect of concentrating voting control with a limited number of stockholders, including our executive officers, directors and principal stockholders, which will limit your ability to influence corporate matters.***

Our Class B common stock has 10 votes per share, and our Class A common stock has one vote per share. At December 31, 2019, the holders of the outstanding shares of our Class B common stock, including our executive officers, directors, and principal stockholders, collectively hold approximately 91% of the combined voting power of our outstanding capital stock. Because of the 10-to-1 voting ratio between our Class B common stock and Class A common stock, the holders of our Class B common stock collectively control a majority of the combined voting power of our outstanding capital stock and therefore are able to exercise significant influence and control over the establishment and implementation of our future business plans and strategic objectives, as well as to control all matters submitted to our stockholders for approval. These persons may manage our business in ways with which you disagree and which may be adverse to your interests. This concentrated control may also have the effect of delaying, deterring or preventing a change-in-control transaction, depriving our stockholders of an opportunity to receive a premium for their capital stock or negatively affecting the market price of our Class A common stock.

Transfers by holders of our Class B common stock will generally result in those shares converting to Class A common stock, subject to limited exceptions. The conversion of our Class B common stock to Class A common stock will have the effect, over time, of increasing the relative voting power of the holders of our Class B common stock who retain their shares over the long term.

***We cannot predict the impact that our capital structure may have on our stock price.***

S&P Dow Jones, a provider of widely followed stock indices, has announced that companies with multiple classes of stock, will not be eligible for inclusion in certain of their indices. As a result, our Class A common stock will not be eligible for those stock indices. Additionally, FTSE Russell, another provider of widely followed stock indices, requires new constituents of its indices to have at least five percent of their voting rights in the hands of public stockholders. At March 31, 2020, the holders of the outstanding shares of our Class B common stock, including our executive officers, directors, and principal stockholders, collectively hold approximately 91% of the combined voting power of our outstanding capital stock. Many investment funds are precluded from investing in companies that are not included in such indices, and these funds would be unable to purchase our Class A common stock. We cannot assure you that other stock indices will not take a similar approach in the future. Exclusion from indices could make our Class A common stock less attractive to investors and, as a result, the market price of our Class A common stock could be adversely affected.

In addition, several shareholder advisory firms have announced their opposition to the use of multiple class structures. As a result, the dual class structure of our common stock may cause shareholder advisory firms to publish negative commentary about our corporate governance practices or otherwise seek to cause us to change our capital structure. Any actions or publications by shareholder advisory firms critical of our corporate governance practices or capital structure could also adversely affect the value of our Class A common stock.

***Share repurchases could increase the volatility of the trading price of our common stock and diminish our cash reserves, and we cannot guarantee that our share repurchase program will enhance long-term stockholder value.***

In October 2018, our Board of Directors adopted a \$30.0 million Share Repurchase Program relating to our outstanding shares of our Class A common stock. In February 2019, our Board of Directors adopted a \$100.0 million Share Repurchase Program relating to our outstanding shares of our Class A common stock, which is inclusive of, and not in addition to, the remaining availability under the October 2018 authorization. Although our Board of Directors has authorized the Repurchase Program, it does not obligate us to repurchase any specific dollar amount or number of shares, there is no expiration date for the Repurchase Program, and the Repurchase Program may be modified, suspended or terminated at any time and for any reason. The timing and actual number of shares repurchased under the Repurchase Program will depend on a variety of factors, including the acquisition price of the shares, our liquidity position, general market and economic conditions, legal and regulatory requirements and other considerations. Our ability to repurchase shares may also be limited by restrictive covenants in our existing Credit Agreement or in future borrowing arrangements we may enter into from time to time.

Repurchases of our shares could increase the volatility of the trading price of our shares, which could have a negative impact on the trading price of our shares. Similarly, the future announcement of the termination or suspension of the Repurchase Program, or our decision not to utilize the full authorized repurchase amount under the Repurchase Program, could result in a decrease in the trading price of our shares. In addition, the Repurchase Program could have the impact of diminishing our cash reserves, which may impact our ability to finance our growth, complete acquisitions and execute our strategic plan. There can be no assurance that any share repurchases we do elect to make will enhance stockholder value because the market price of our common stock may decline below the levels at which we repurchased our shares. Although our share repurchase program is intended to enhance long-term stockholder value, we cannot guarantee that it will do so and short-term stock price fluctuations could reduce the effectiveness of the Repurchase Program.

***Anti-takeover provisions contained in our amended and restated certificate of incorporation and amended and restated bylaws, as well as provisions of Delaware law, could impair a takeover attempt.***

Our amended and restated certificate of incorporation and our amended and restated bylaws contain provisions that could have the effect of rendering more difficult hostile takeovers, change-in-control transactions or changes in our Board of Directors or management. Among other things, these provisions:

- authorize the issuance of preferred stock with powers, preferences and rights that may be senior to our common stock, which can be created and issued by our Board of Directors without prior stockholder approval;
- provide for the adoption of a staggered Board of Directors whereby our board is divided into three classes, each of which has a different three-year term;
- provide that the number of directors will be fixed by our Board of Directors;
- prohibit our stockholders from filling vacancies on our Board of Directors;
- provide for the removal of a director only for cause and then only by the affirmative vote of the holders of a majority of the combined voting power of our outstanding capital stock;
- prohibit stockholders from calling special stockholder meetings;
- prohibit stockholders from acting by written consent without holding a meeting of stockholders;
- require the vote of at least two-thirds of the combined voting power of our outstanding capital stock to approve amendments to our certificate of incorporation or bylaws;
- require advance written notice of stockholder proposals and director nominations;
- provide for a dual-class common stock structure, as discussed above; and
- require the approval of the holders of at least a majority of the outstanding shares of our Class B common stock, voting as a separate class, prior to consummating a change-in-control transaction.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which may delay, deter or prevent a change-in-control transaction. Section 203 imposes certain restrictions on mergers, business combinations and other transactions between us and holders of 15% or more of our common stock.

Any provision of Delaware law, our amended and restated certificate of incorporation, or our amended and restated bylaws, that has the effect of rendering more difficult, delaying, deterring or preventing a change-in-control transaction could limit the opportunity for our stockholders to receive a premium for their shares of our capital stock, and could also affect the price that some investors are willing to pay for our Class A common stock.

***Future sales of shares of our Class A common stock, or the perception that these sales could occur, could depress the market price of our Class A common stock.***

Sales of a substantial number of shares of our Class A common stock in the public market, or the perception that these sales might occur, could cause the market price of our Class A common stock to decline or make it more difficult for you to sell your Class A common stock at a time and price that you deem appropriate, and could impair our ability to raise capital through the sale of additional equity securities. We are unable to predict the effect that sales, or the perception that our shares may be available for sale, will have on the prevailing market price of our Class A common stock.

At March 31, 2020, we had an aggregate of 1.3 million options outstanding that, if fully exercised, would result in the issuance of additional shares of Class A common stock or Class B common stock, as applicable. Our Class B common stock converts into Class A common stock on a one-for-one basis. In addition, at March 31, 2020, we had 0.6 million restricted stock units ("RSUs"), outstanding which, if fully vested and settled in shares, would result in the issuance of additional shares of Class A common stock. All of the shares of Class A common stock issuable upon the exercise of options (or upon conversion of shares of Class B common stock issued upon the exercise of options), or upon the vesting and settlement of RSUs, have been registered for public resale under the Securities Act. Accordingly, these shares will be able to be freely sold in the public market upon issuance.

Certain holders of our Class A common stock and Class B common stock have rights, subject to certain conditions, to require us to file registration statements for the public resale of such shares (in the case of Class B common stock, the Class A common stock issuable upon conversion of such shares) or to include such shares in registration statements that we may file for us or other stockholders. Any sales of securities by these stockholders could have a material adverse effect on the market price of our Class A common stock.

***If securities or industry analysts do not publish or cease publishing research or reports about us, our business, our market or our competitors, or if they adversely change their recommendations regarding our Class A common stock, the market price and trading volume of our Class A common stock could decline.***

The trading market for our Class A common stock is influenced, to some extent, by the research and reports that securities or industry analysts may publish about us, our business, our market or our competitors. If any of the analysts who cover us adversely change their recommendations regarding our Class A common stock or provide more favorable recommendations about our competitors, the market price of our Class A common stock may decline. If any of the analysts who cover us were to cease coverage of us or fail to regularly publish reports, we could lose visibility in the financial markets, which in turn could cause the market price and trading volume of our Class A common stock to decline.

***We do not expect to declare any dividends in the foreseeable future.***

We have never declared or paid any cash dividends on our existing common stock. We do not anticipate declaring or paying any cash dividends to holders of our Class A common stock in the foreseeable future and intend to retain all future earnings for use in the growth of our business. In addition, the terms of our Credit Agreement restrict our ability to pay dividends. Consequently, investors may need to rely on sales of our Class A common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investment. Investors should not purchase our Class A common stock with the expectation of receiving cash dividends.

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

On February 20, 2019, the Board of Directors authorized a \$100.0 million Share Repurchase Program (the "Program") of our outstanding Class A Common Stock. Share repurchases made under the Program were made through open market transactions as follows:

	Total Number of Shares Repurchased <sup>(1)</sup>	Average Price Paid per Share <sup>(2)</sup>	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1)</sup>	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
				(in thousands)
January 1, 2020 to January 31, 2020	—	—	—	100,000
February 1, 2020 to February 29, 2020	—	—	—	100,000
March 1, 2020 to March 31, 2020	48,002	\$ 87.35	48,002	95,807

<sup>(1)</sup>These repurchased shares of common stock were recorded as treasury stock and were accounted for under the cost method. None of the repurchased shares of common stock have been retired.

<sup>(2)</sup>Excludes broker commissions.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

See the Exhibit Index immediately following the signature page of this Quarterly Report, which is incorporated herein by reference.

**SIGNATURES**

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

AppFolio, Inc.

Date: May 4, 2020

By: /s/ Ida Kane  
Ida Kane  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

**EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Description of Document</b>
31.1	<a href="#">Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.</a>
31.2	<a href="#">Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.</a>
32.1*	<a href="#">Certifications of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</a>
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

\* The certifications attached as Exhibit 32.1 accompany this Quarterly Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed “filed” by the registrant for purposes of Section 18 of the Exchange Act, and are not to be incorporated by reference into any of the registrant’s filings under the Securities Act or the Exchange Act, whether made before or after the date of this Quarterly Report, irrespective of any general incorporation language contained in any such filing.



**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Jason Randall, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of AppFolio, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 4, 2020

/s/ Jason Randall

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Jason Randall

Chief Executive Officer

**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Ida Kane, certify that:

1. I have reviewed this Annual Report on Form 10-Q of AppFolio, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 4, 2020

/s/ Ida Kane

Ida Kane

Chief Financial Officer

**CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER  
PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The following certifications are hereby made in connection with the Quarterly Report on Form 10-Q of AppFolio, Inc. (the "Company") for the period ended March 31, 2020, as filed with the Securities and Exchange Commission on the date hereof (the "Report"):

I, Jason Randall, President and Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge, (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods presented.

Date: May 4, 2020

By: /s/ Jason Randall

Jason Randall

President and Chief Executive Officer

I, Ida Kane, Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge, (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods presented.

Date: May 4, 2020

By: /s/ Ida Kane

Ida Kane

Chief Financial Officer