Mattersight Corp
Form 10-Q
May 10, 2018

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, 2018

OR

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

Commission File Number 0-27975

Mattersight Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware	36-4304577
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

200 W. Madison Street

Suite 3100

Chicago, Illinois 60606

(Address of Principal Executive Offices) (Zip Code)

(877) 235-6925

(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

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

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

The number of shares of the registrant's common stock outstanding as of May 1, 2018 was 33,220,445.

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Part I. Financial Information

Forward-Looking Statements

Statements in this Quarterly Report on Form 10-Q that are not historical facts are “forward-looking statements” and are made pursuant to the safe harbor provisions 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). A reader can identify these forward-looking statements, because they are not limited to historical fact or they use words such as “scheduled,” “will,” “anticipate,” “project,” “estimate,” “forecast,” “goal,” “objective,” “committed,” “intend,” “continue,” “plan,” “may,” “ “expect,” “intend,” “could,” “would,” “should,” or “will likely result,” and other similar expressions, and terms of similar mear in connection with any discussion of our prospects, financial statements, business, financial condition, revenues, results of operations, or liquidity, involving risks and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. In addition to other factors and matters contained or incorporated in this document, important factors that could cause actual results or events to differ materially from those indicated by such forward-looking statements include, without limitation, those noted under Risk Factors included in Part I Item 1A of this Quarterly Report on Form 10-Q and included in Part I Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017, as well as the following:

- Uncertainties associated with the attraction of, and the ability to execute contracts with, new clients, the continuation of existing, and execution of new, engagements with existing clients, the conversion of free pilots to paid subscription contracts, and the timing of related client commitments;
- Reliance on a relatively small number of clients for a significant percentage of our revenue;
- Risks involving the variability and predictability of the number, size, scope, cost, and duration of, and revenue from, client engagements;
- Management of the other risks associated with complex client projects and new service offerings, including execution risk;
- Cyber-attacks or other privacy or data security incidents, and failure to comply with privacy and data security regulations;
- Management of growth and development of, and introduction of, new service offerings;
- The potential failure to satisfy conditions to the completion of the proposed Merger (defined below) due to the failure to receive a sufficient number of tendered shares in the tender offer; and
- The proposed Merger may not be completed on the timeframe expected or at all.

We cannot guarantee any future results, levels of activity, performance, or achievements. The statements made in this Quarterly Report on Form 10-Q represent our views as of the date of this report, and it should not be assumed that the statements made in this report remain accurate as of any future date. Moreover, we assume no obligation to update forward-looking statements, except as may be required by law. In light of Regulation FD, it is our policy not to comment on earnings, financial guidance, or operations other than through press releases, publicly announced conference calls, or other means that will constitute public disclosure for purposes of Regulation FD.

Item 1. Financial Statements

MATTERSIGHT CORPORATION

CONSOLIDATED BALANCE SHEETS

(Unaudited and in thousands, except share and per share data)

	March 31, 2018	December 31, 2017
ASSETS		
Current Assets:		
Cash and cash equivalents	$8,681	$ 9,044
Receivables net of allowances of $42 and $41, at March 31, 2018 and December 31, 2017, respectively	8,612	6,565
Prepaid expenses	6,352	5,805
Other current assets	60	65
Total current assets	23,705	21,479
Equipment and leasehold improvements, net of accumulated depreciation and amortization of $25,841 and $24,955, at March 31, 2018 and December 31, 2017, respectively	7,499	8,572
Goodwill	972	972
Intangible assets, net of amortization of $4,487 and $4,357, respectively	2,899	2,952
Other long-term assets (includes $2,475 and $2,675 in restricted cash, at March 31, 2018 and December 31, 2017, respectively)	5,885	5,960
Total assets	$40,960	$ 39,935
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Short-term debt	$96	$ 93
Accounts payable	1,788	1,474
Accrued compensation and related costs	3,568	3,312
Unearned revenue	8,200	3,032
Capital leases	1,701	1,967
Other current liabilities	4,223	3,399
Total current liabilities	19,576	13,277
Long-term debt	13,030	17,056
Long-term unearned revenue	1,039	914
Long-term capital leases	866	1,190
Other long-term liabilities	6,606	6,475
Total liabilities	41,117	38,912
7% Series B convertible preferred stock, $0.01 par value; 5,000,000 shares authorized and	8,353	8,353

designated; 1,637,786 and 1,637,786 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively, with a liquidation preference of $11,714 and $11,568, at March 31, 2018 and December 31, 2017, respectively		
Stockholders' Equity:		
Preferred stock, $0.01 par value; 35,000,000 shares authorized; none issued and outstanding	—	—
Common stock, $0.01 par value; 50,000,000 shares authorized; 33,307,647 and 33,083,180 shares issued at March 31, 2018 and December 31, 2017, respectively; 33,220,445 and 33,039,713 shares outstanding at March 31, 2018 and December 31, 2017, respectively	333	331
Additional paid-in capital	277,000	275,963
Accumulated deficit	(281,556)	(279,425)
Treasury stock, at cost, 87,202 and 43,467 shares at March 31, 2018 and December 31, 2017, respectively	(205)	(117)
Accumulated other comprehensive loss	(4,082)	(4,082)
Total stockholders' deficit	(8,510)	(7,330)
Total liabilities and stockholders' equity	$40,960	$ 39,935

See accompanying notes to the Unaudited Consolidated Financial Statements.

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MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited and in thousands, except per share data)

	Quarter Ended	
	March 31, 2018	March 31, 2017
Revenue:		
Subscription revenue	$ 12,986	$ 10,343
Other revenue	728	616
Total revenue	13,714	10,959
Operating expenses:		
Total cost of revenue, exclusive of depreciation and amortization	3,926	3,439
Product development	3,441	3,321
Sales and marketing	3,508	3,450
General and administrative	3,403	3,295
Depreciation and amortization	1,427	1,545
Total operating expenses	15,705	15,050
Operating loss	(1,991)	(4,091)
Non-operating income (expense):		
Interest and other borrowing costs	(266)	(969)
Change in fair value of warrant liability	110	97
Other non-operating income	1	10
Total non-operating expense	(155)	(862)
Loss before income taxes	(2,146)	(4,953)
Income tax benefit	15	1
Net loss	(2,131)	(4,952)
Dividends related to 7% Series B convertible preferred stock	(146)	(146)
Net loss available to common stockholders	$ (2,277)	$ (5,098)
Per share of common stock:		
Basic net loss available to common stockholders	$ (0.07)	$ (0.19)
Diluted net loss available to common stockholders	$ (0.07)	$ (0.19)
Shares used to calculate basic net loss per share	31,747	27,423
Shares used to calculate diluted net loss per share	31,747	27,423
Stock-based compensation expense is included in individual line items above:		
Total cost of revenue	$ 175	$ 81
Product development	351	134
Sales and marketing	184	123
General and administrative	570	354

See accompanying notes to the Unaudited Consolidated Financial Statements.

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MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited and in thousands)

	Quarter Ended	
	March 31, 2018	March 31, 2017
Net loss	$(2,131)	$(4,952)
Other comprehensive loss:		
Effect of foreign currency translation	—	(19)
Comprehensive net loss	$(2,131)	$(4,971)

See accompanying notes to the Unaudited Consolidated Financial Statements.

MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited and in thousands)

	Three Months Ended March 31, 2018	March 31, 2017
Cash Flows from Operating Activities:		
Net loss	$ (2,131)	$ (4,952)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,427	1,545
Stock-based compensation	1,280	692
Discount accretion and other debt-related costs	20	271
Provision for uncollectible accounts	1	(3)
Change in fair value of warrant liability	(110)	(97)
Changes in assets and liabilities:		
Receivables	(2,048)	(1,054)
Prepaid expenses	(215)	(246)
Other current assets	5	214
Other long-term assets	(25)	19
Accounts payable	(94)	(142)
Accrued compensation and related costs	256	904
Unearned revenue	5,293	(247)
Other current liabilities	1,152	38
Other long-term liabilities	(101)	(130)
Total adjustments	6,841	1,764
Net cash provided by (used in) operating activities	4,710	(3,188)
Cash Flows from Investing Activities:		
Capital expenditures	(164)	(659)
Investment in intangible assets	(49)	—
Net cash used in investing activities	(213)	(659)
Cash Flows from Financing Activities:		
Proceeds from line of credit	4,500	—
Repayments of line of credit	(8,500)	—
Repayments of other borrowings	(202)	(219)
Fees paid for debt amendment	(100)	—
Proceeds from issuance of common stock, net of costs	—	14,904
Cash paid to satisfy tax withholding upon vesting of employee stock awards	(206)	(537)
Principal payments on capital lease obligations	(604)	(592)
Proceeds from employee stock purchase plan	52	68
Net cash (used in) provided by financing activities	(5,060)	13,624
Effect of exchange rate changes on cash and cash equivalents	—	(19)
(Decrease) increase in total cash	(563)	9,758

Cash and cash equivalents	9,044	12,538
Restricted cash (included in Other long-term assets on the Consolidated Balance Sheets)	2,675	4,210
Total cash, beginning of period	11,719	16,748
Cash and cash equivalents	8,681	22,523
Restricted cash (included in Other long-term assets on the Consolidated Balance Sheets)	2,475	3,983
Total cash, end of period	$ 11,156	$ 26,506
Non-Cash Investing and Financing Activities:		
Capital lease obligations incurred	$ 14	$ 1,378
Capital equipment purchased on credit	14	1,378
Supplemental Disclosures of Cash Flow Information:		
Interest paid	$ 283	$ 532

See accompanying notes to the Unaudited Consolidated Financial Statements.

MATTERSIGHT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note One — Basis of Presentation

The accompanying interim consolidated financial statements include Mattersight Corporation and its subsidiaries (collectively, Mattersight or the company). The accompanying interim consolidated financial statements have been prepared without audit. Certain notes and other information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. In the opinion of management, the accompanying consolidated financial statements include all normal recurring adjustments considered necessary to present fairly the financial position of the company at March 31, 2018 and December 31, 2017 and the results of operations and cash flows for the periods indicated. Quarterly results are not necessarily indicative of results for any subsequent period.

On January 1, 2018, the company adopted ASU 2014-09: Revenue from Contracts with Customers (Topic 606). This update sets forth a new five-step revenue recognition model that replaces the prior revenue recognition guidance in its entirety and is intended to eliminate numerous industry-specific pieces of revenue recognition guidance that have historically existed. The underlying principle of the new standard is that an organization will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects what it expects in exchange for the goods or services. The company adopted using the modified retrospective transition method and there were no material adjustments to beginning retained deficits. Changes in the current period as a result of adopting the ASU relate to billings for certain non-cancelable contracts. The following table reconciles the balances as presented for the three months ended March 31, 2018 to the balances prior to the adjustments made to implement the new revenue recognition standard for the same period:

(In millions)	As Presented	Impact of New Revenue Standard	Previous Revenue Standard
Assets			
Receivables, net of allowances	$ 8.6	$ 0.5	$ 8.1
Liabilities			
Unearned revenue	8.2	0.4	7.8
Long-term unearned revenue	1.0	0.1	0.9

On January 1, 2018, the company adopted ASU No. 2017-09, Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting, which provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The standard was adopted with no impact to the financial statements.

On January 1, 2018, the company condensed the costs of revenue items to present cost of revenue as a single line item. Cost of other revenue was determined to be immaterial to the financial statements. There was no change to the expense classification and the current period is comparable to the prior period.

On April 25, 2018, the company entered into an Agreement and Plan of Merger with NICE Systems, Inc., a Delaware corporation ("Parent"), NICE Acquisition Sub, Inc., a Delaware corporation and wholly owned subsidiary of Parent ("Acquisition Sub"), and, solely for the purposes of Section 8.16 of the Merger Agreement, NICE Ltd., a company organized under the laws of the State of Israel ("Guarantor") (the "Merger Agreement") under which the company would be acquired by and merged into a wholly-owned subsidiary of NICE (See Note Fourteen — Subsequent Events).

The accompanying unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto in Mattersight's Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission (SEC) on March 12, 2018.

Note Two — Recent Accounting Pronouncements

In July 2017, the Financial Accounting Standards Board (FASB) issued ASU No. 2017-11—Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments with Down Round Features, (Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests with a Scope Exception to address narrow issues identified as a result of the complexity associated with applying generally accepted accounting principles for certain financial instruments with characteristics of liabilities and equity. Part I of the update changes the classification analysis of certain equity-linked financial instruments (or embedded features) with down round features. Part II of the update re-characterizes the indefinite deferral of certain provisions of Topic 480 that now are presented as pending content in the codification, to a scope exception. Part II does not have an accounting effect. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The company is currently evaluating the impact of this update on its consolidated financial statements.

In January 2017, FASB issued ASU No. 2017-04, Intangibles—Goodwill and Other, simplifying the test for goodwill impairment. This ASU simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Under this update, goodwill impairment will be measured as the amount by which a reporting unit's carrying value exceeds its fair value. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is needed. This ASU is effective for reporting periods beginning after December 15, 2019 and interim periods within those annual periods. The company is evaluating the standard and does not expect a change in value of goodwill when the standard is adopted.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments — Credit Losses: Measurement of Credit Losses on Financial Instruments. This update broadens the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The update is effective for annual periods beginning after December 15, 2019. The company is currently evaluating the impact of this update on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). This update is intended to improve financial reporting of leasing transactions. The ASU will require organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. This update is effective for periods beginning after December 15, 2018. The company is currently evaluating the impact of this update on its consolidated financial statements. Certain operating leases the company is party to are expected to be recognized as assets and liabilities as a result of adopting this standard.

Note Three — Revenue Recognition

Revenue is derived primarily from subscription services and professional services. Revenue is recognized upon transfer of control of these services to customers in an amount that reflects the consideration the company expects to receive in exchange for those services.

Subscription Revenue

Subscription revenue consists of revenue from Mattersight's Behavioral Analytics service offerings, including predictive behavioral routing, performance management, quality assurance, predictive analytics, and marketing managed services revenue derived from the performance of services on a continual basis.

Revenue is recognized ratably over the subscription period as the services are performed for the client. Subscription periods generally range from one to three years after the go-live date or, in cases where the company contracts with a client for a short-term pilot of a Behavioral Analytics offering prior to committing to a longer subscription period, if any, the subscription or pilot periods generally range from three to twelve months after the go-live date. Contracts may be billed annually, quarterly, and monthly in advance.

Other Revenue

Other revenue consists of deployment revenue, professional services revenue and reimbursed expenses revenue.

Deployment revenue consists of planning, deployment, and training fees derived from Behavioral Analytics contracts. These fees, which are considered to be installation fees related to Behavioral Analytics subscription contracts, are deferred until the installation is complete and are then recognized over the applicable subscription or pilot period. Deployment fees are typically billed in advance and generally non-cancelable.

Professional services revenue primarily consists of fees charged to the company's clients to provide post-deployment follow-on consulting services, which include custom data analysis, the implementation of enhancements, and training, as well as fees generated from the company's operational consulting services. Professional services are performed for the company's clients on a fixed-fee or time-and-materials basis. Revenue is recognized as the services are performed, with performance generally assessed on the ratio of actual hours incurred to-date compared with the total estimated hours over the entire term of the contract.

Reimbursed expenses revenue includes billable costs related to travel and other out-of-pocket expenses incurred while performing services for the company's clients. An equivalent amount of reimbursable expenses is included in total cost of other revenue.

Other Significant Judgements

Subscription and deployment contracts with customers are interdependent of each other and not capable of being distinct. As such they are accounted for together as one performance obligation.

For purposes of determining the transaction price, the company has elected to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the company from the customer. These include sales, use, value added and certain excise taxes.

A limited number of contracts with customers are sold with rebates or other credits. Additionally, some contracts allow for additional fees if a customer exceeds the baseline number of users during a billing period. These amounts are accounted for as variable consideration and estimated using the expected value approach.

Disaggregation of Revenue

The company's service contracts primarily fall into one of two categories (i) predictive behavioral routing and (ii) other behavioral analytics. Predictive behavioral routing revenue is included in subscription revenue and other behavioral analytics revenue is included in both subscription and other revenue. The following table sets forth revenue by service category:

	March 31,	March 31,
(In millions)	2018	2017
Predictive behavioral routing	$ 3.4	$ 1.4
Other behavioral analytics	10.3	9.6
Total	$ 13.7	$ 11.0

Assets Recognized from Costs to Obtain and Fulfill a Contract with a Customer

Assets recognized for costs to obtain and fulfill a contract include sales commissions and deployment costs. These costs are deferred up to an amount not to exceed the amount of deferred deployment revenue and additional amounts that are recoverable based on the contractual arrangement. These costs are included in prepaid expenses and other long-term assets. Such costs are amortized over the subscription period. Costs in excess of the foregoing revenue amount are expensed in the period incurred. There were no impairment losses related to deferred contract costs in the reporting period.

The following table sets forth the activity in deferred sales commissions and deferred deployment costs.

(In millions)

	Deferred Sales Commissions	Deferred Deployment Costs
Balance at January 1, 2018	$ 1.1	$ 3.1
Costs recognized as assets	0.3	0.5
Amortization of costs	(0.6)	(0.7)
Balance at March 31, 2018	$ 0.8	$ 2.9

Transaction Price Allocated to the Remaining Performance Obligations

As of March 31, 2018, of the contracts that have gone live or are in active deployments, approximately $65.6 million of revenue is expected to be recognized from remaining performance obligations for subscription contracts. We expect to recognize revenue on approximately 56% of these remaining performance obligations over the next 12 months, with the remainder thereafter. Revenue from remaining performance obligations for other revenue was immaterial at March 31, 2018.

Contract Balances

Certain contracts with customers allow for additional fees if a customer exceeds the baseline number of users during a billing period. These fees are recognized as contract assets and revenue in advance of the right to payment from customers. Substantially all fees recognized in advance of the right to payment were billed to customers by the end of the quarter ended March 31, 2018.

Customer contracts may be billed annually, quarterly, or monthly in advance and are recognized as contract liabilities until services are rendered. The following table sets forth the activity in contract liabilities:

(In millions)	Contract Liabilities
Balance January 1, 2018	$ 3.9
Revenue recognized that was included in the contract liability at the beginning of the period	(0.8)
Increases due to billings, excluding amounts recognized as revenue during the period	6.1
Net decrease (increase) due to changes in transaction price as a result of revised estimates of variable consideration	—
Balance March 31, 2018	$ 9.2

There was no revenue adjustment in the current period as a result of changes in transaction price that relate to performance obligations satisfied during a prior period.

Note Four — Current Prepaid Expenses

Current prepaid expenses primarily consist of prepaid technology maintenance costs, deferred deployment costs, and prepaid commissions related to Behavioral Analytics contracts. These costs are recognized over the subscription periods of the respective contracts generally one to three years after the go-live date or, in cases where the company contracts with a client for a short-term pilot of a Behavioral Analytics offering prior to committing to a longer subscription period, if any, the subscription or pilot periods generally range from three to twelve months after the go-live date. Current prepaid expenses also includes prepaid marketing and insurance costs. These costs will be recognized within the next twelve months.

Current prepaid expenses consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
Prepaid technology maintenance costs	$ 2.6	$ 2.0
Deferred deployment costs	1.8	1.9
Prepaid commissions	0.7	1.1
Prepaid marketing	0.5	0.5
Prepaid insurance	0.4	0.1
Other	0.4	0.2
Total	$ 6.4	$ 5.8

Note Five — Other Long-Term Assets

Other long-term assets includes the long-term portion of restricted cash, prepaid technology and maintenance support, deferred deployment costs, and prepaid commissions related to Behavioral Analytics. Restricted cash represents cash used to collateralize certain letters of credit issued to support the company's equipment leasing activities. Costs included in long-term assets will be recognized over the remaining term of the contracts beyond the first twelve months. Other long-term assets consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
Restricted cash	$ 2.5	$ 2.7
Prepaid technology and maintenance support	1.7	1.9
Deferred deployment costs	1.1	1.2
Prepaid commissions	0.1	—
Other	0.5	0.2
Total	$ 5.9	$ 6.0

Note Six — Other Current Liabilities

Other current liabilities consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
Accrued vendor payable	$ 2.1	$ 1.9
Customer rebates and credits	0.6	0.3
Deferred rent liability	0.5	0.5
Sales tax liability	0.3	0.1
Warrant liability	0.3	0.4
Accrued legal payable	0.3	0.1
Other	0.1	0.1
Total	$ 4.2	$ 3.4

On August 1, 2016, the company issued a warrant to Hercules Capital, Inc. (Hercules) that gives Hercules the right to purchase shares of the company's common stock at $3.50 per share. The warrant is exercisable for 357,142 shares of common stock and expires on August 1, 2023. The warrant is accounted for as a liability and carried at fair market value using the Black-Scholes model. Changes in the warrant's fair market value are recognized in non-operating income (expense) in the consolidated statements of operations.

Note Seven — Leases

Capital Leases

Assets under capital leases consist primarily of computer hardware and related equipment. The gross amount of assets recorded under capital leases was $6.8 million and $7.3 million at March 31, 2018 and December 31, 2017, respectively. Depreciation expense related to assets under capital leases is included in depreciation and amortization expense on the consolidated statements of operations.

As of March 31, 2018, the future minimum lease payments due under capital leases are expected to be as follows:

(In millions) Year	Amount
Remainder of 2018	$ 1.5
2019	1.1
2020	0.2
2021	—
Total minimum lease payments	$ 2.8
Less: amount representing interest	(0.3)
Present value of minimum lease payments	$ 2.5

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Note Eight — Debt

On June 29, 2017, the company entered into a loan agreement with CIBC Bank USA f/k/a The PrivateBank and Trust Company (CIBC). The loan agreement provides for a revolving line of credit to the company with a maximum credit limit of $20.0 million, which matures on June 29, 2020 (the credit facility). The credit facility is secured by a security interest in the company's assets. The company, subject to certain limits and restrictions, may from time to time request the issuance of letters of credit under the loan agreement.

The principal amount outstanding under the credit facility will accrue interest at a floating annual rate equal to 1 month, 2 month or 3 month LIBOR (as selected by the company) plus 5.50%, payable monthly. In addition, the company will pay a non-use fee on the credit facility of 25 basis points (0.25%) per annum of the average unused portion of the credit facility. The amount the company may borrow under the credit facility is limited to five times the company's monthly recurring revenue (as determined in accordance with the terms and conditions set forth in the loan agreement), multiplied by a dynamic churn factor that is based upon the ratio of recurring revenue retained in the prior twelve month period relative to the total amount of recurring revenue at the beginning of the period.

The loan agreement imposes various restrictions on the company, including usual and customary limitations on the ability of the company to incur debt and to grant liens upon its assets, increasing restrictions based on thresholds, prohibits certain consolidations, mergers, and sales and transfers of assets by the company and requires the company to comply with a trailing twelve months of total revenue and quarterly EBITDA (as adjusted in accordance with the loan agreement) targets. The loan agreement includes usual and customary events of default (with customary grace periods, as applicable) and provides that, upon the occurrence of an event of default, payment of all amounts payable under the loan agreement may be accelerated and/or the lender's commitments may be terminated. In addition, upon the occurrence of certain insolvency or bankruptcy related events of default, all amounts payable under the loan agreement will automatically become immediately due and payable, and the lender's commitments will automatically terminate.

On March 29, 2018, the company amended the loan agreement with CIBC. The amendment changes the quarterly EBITDA targets and increases the applicable margin for loans bearing interest at LIBOR from 4.50% to 5.50% and for loans bearing interest at the base rate from 1.75% to 2.75%. The amendment increases the company's minimum total revenue thresholds for the first and second quarters of 2018 by an average of approximately 3% each quarter and reduces the applicable total revenue thresholds for each of the third and fourth quarters of 2018 by an average of approximately 6% each quarter. The amendment also provides CIBC with the ability to impose discretionary reserves against the borrowing base. The company paid CIBC a non-refundable amendment fee of $0.1 million.

The average outstanding balance on the revolving line of credit during the first quarter of 2018 was $9.2 million. In March 2018, CIBC established a reserve of $5.0 million against the revolving loan agreement, effectively reducing total availability to $15 million. CIBC has the ability to increase the reserves against the revolving loan availability at their discretion. As of March 31, 2018, $12.9 million remains outstanding on the revolving line of credit with the ability to draw an additional $0.5 million. The company has classified the CIBC debt as long term and does not expect CIBC to demand repayment within the next 12 months. There was also $1.6 million in letters of credit issued by CIBC against the line of credit. During April 2018, the company repaid $4.5 million of principal on the revolving line of credit. If the NICE transaction does not occur or is delayed, the Company would need to raise capital and negotiate modifications to the loan agreement and there is no assurance that the company would have access to additional external capital resources on acceptable terms.

On April 25, 2018, the company entered into a second amendment to the loan agreement with CIBC. The amendment excludes certain expenses incurred in connection with the merger from the calculation of adjusted EBITDA, and changes the adjusted EBITDA target for the second quarter of 2018. The amendment also requires the company to have liquidity as of the last day of each calendar month of at least $2.0 million (See Note Fourteen — Subsequent Events).

Debt consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
CIBC loan due June 29, 2020, effective borrowing rate of 6.16% and 5.93% at March 31, 2018 and December 31, 2017	$ 12.9	$ 16.9
Furniture loan due May 2021, effective borrowing rate of 9.10%	0.1	0.1
Furniture loan due May 2021, effective borrowing rate of 9.55%	0.1	0.1
Furniture loan due July 2019, effective borrowing rate of 13.98%(1)	—	0.1
Total debt(2)	$ 13.1	$ 17.2

(1) Less than $0.1 million.
(2) Total debt of $13.1 million at March 31, 2018 includes the current portion of furniture loans of $0.1 million and the long term portion of the CIBC loan of $12.9 million. Total debt of $17.2 million at December 31, 2017, respectively, includes the current portion of the furniture loans of $0.1 million and the long term portion of the CIBC loan of $16.9 million.

Note Nine — Other Long-Term Liabilities

Other long-term liabilities consisted of the following:

(In millions)	March 31, 2018	December 31, 2017
7% Series B convertible preferred stock dividends payable	$ 3.4	$ 3.2
Deferred rent liability	1.8	1.9
Technology service liability	1.2	1.2
Deferred income tax liability	0.2	0.2
Total	$ 6.6	$ 6.5

Note Ten — Litigation and Other Contingencies

The company is a party to various agreements, including all its client contracts, under which it may be obligated to indemnify the other party with respect to certain matters, including, but not limited to, indemnification against third-party claims of (i) infringement of intellectual property rights with respect to services, software, and other deliverables provided by the company, and (ii) failure to comply with various data security and privacy regulations. These obligations may be subject to various limitations on the remedies available to the other party, including, without limitation, limits on the amounts recoverable and the time during which claims may be made, and may be supported by indemnities given to the company by applicable third parties. Payment by the company under these indemnification clauses is generally subject to the other party making a claim that is subject to challenge by the company. Historically, the company has not been obligated to pay any claim for indemnification under its agreements, and management is not aware of future indemnification payments that it would be obligated to make.

Under its by-laws, subject to certain exceptions, the company has agreed to indemnify its corporate officers and directors for certain events or occurrences while the officer or director is, or was, serving at its request in such capacity or in certain related capacities. The company has separate indemnification agreements with each of its corporate officers and directors that requires it, subject to certain exceptions, to indemnify them to the fullest extent authorized or permitted by its by-laws and the Delaware General Corporation Law. The maximum potential amount of future payments the company could be required to make under these indemnification agreements is unlimited; however, the company has a director and officer liability insurance policy that limits its exposure and enables it to recover a portion of any amounts paid under these indemnification agreements. As a result of its insurance policy coverage, the company believes the estimated fair value of these indemnification agreements is minimal. The company had no liabilities recorded for these agreements as of March 31, 2018.

The company's products may be subject to sales tax in certain jurisdictions. If a taxing authority were to successfully assert that the company has not properly collected sales or other transaction taxes, or if sales or other transaction tax laws or the interpretation thereof were to change, and the company was unable to enforce the terms of its contracts with customers that give it the right to reimbursement for assessed sales taxes, the company could incur tax liabilities in amounts that could be material. The company has considered the changing nature of tax laws, the terms of its customer contracts and its recent audit experience in assessing its exposure to possible and probable sales tax liabilities. Based on its assessment, the company has recorded a sales tax liability of $0.3 million at March 31, 2018.

Note Eleven — Stock-Based Compensation

Restricted Stock

Restricted stock awards are shares of common stock granted to an individual that vest over a period of time. During the vesting period, the holder of restricted stock receives all of the benefits of ownership (right to dividends, voting rights, etc.), other than the right to sell or otherwise transfer any interest in the stock. Restricted stock awards granted during the quarter ended March 31, 2018 were as follows:

Description	Grant Date	Shares	Vesting Schedule
Grants to employees	2/14/2018	105,611	100% on February 28, 2019
Grants to employees	2/14/2018	164,250	50% on February 28, 2020, 6.25% quarterly thereafter
Total		269,861	

Restricted stock award activity was as follows for the quarter ended March 31, 2018:

	Shares	Weighted Average Price
Unvested balance at December 31, 2017	1,365,200	$ 3.65
Granted	269,861	$ 2.55
Vested	(291,093)	$ 3.91
Forfeited	(30,547)	$ 2.75
Unvested balance at March 31, 2018	1,313,421	$ 3.39

Note Twelve — Loss Per Share

The following table presents the loss per share calculation for the periods presented:

	Quarter Ended March 31, 2018	Quarter Ended March 31, 2017
(In millions)		
Net loss	$(2.1)	$ (5.0)
Dividends related to 7% Series B convertible preferred stock[1]	(0.2)	(0.1)
Net loss available to common stockholders	$(2.3)	$ (5.1)
Per share of common stock:		
Basic/diluted net loss available to common stockholders	$(0.07)	$ (0.19)
(In thousands)		
Weighted average shares outstanding (basic and diluted)	31,747	27,423
Anti-dilutive common stock equivalents[2]	1,493	2,200

(1) Dividends on 7% Series B convertible preferred stock (Series B stock) are cumulative and have been accrued from July 1, 2012 to March 31, 2018. Total accrued dividends were $3.4 million as of March 31, 2018. Dividends will continue to accrue until they are declared by the company's board of directors. The company has not declared any Series B stock dividends in 2018 or 2017.
(2) In periods in which there was a loss, the effect of common stock equivalents, which is primarily related to the Series B stock, was not included in the diluted loss per share calculation as it was antidilutive.

Note Thirteen — Fair Value Measurements

The company uses a three-level classification hierarchy of fair value measurements to report certain assets and liabilities at fair value. The first tier, Level 1, uses quoted market prices in active markets for identical assets or liabilities. Level 2 uses observable market data, such as quoted market prices for similar assets and liabilities in active markets, or inputs other than quoted prices that are directly observable. Level 3 uses entity-specific inputs or unobservable inputs that are derived and cannot be corroborated by market data. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table presents financial instruments measured at fair value measured on a recurring basis:

	March 31, 2018			
(In millions)	Carrying value	Level 1	Level 2	Level 3
Warrant liability	$ 0.3	—	—	$ 0.3

	December 31, 2017			
	Carrying value	Level 1	Level 2	Level 3
Cash and cash equivalents - money market fund	$ 0.5	$ 0.5	$ —	$ —
Warrant liability	0.4	—	—	0.4

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, and short-term debt approximated their fair values as of March 31, 2018 due to the short-term nature of these instruments.

The company determined the fair value of the liability for the warrant issued to Hercules, considered a Level 3 liability, using the Black-Scholes model. At March 31