

PROGRESS SOFTWARE CORP /MA

Form 10-Q

October 07, 2016

Table of Contents

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 August 31, 2016

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

Commission File Number: 0-19417

PROGRESS SOFTWARE CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE 04-2746201  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)  
14 Oak Park  
Bedford, Massachusetts 01730  
(Address of principal executive offices)(Zip code)  
Telephone Number: (781) 280-4000

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

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

As of September 29, 2016, there were 48,592,417 shares of the registrant’s common stock, \$.01 par value per share, outstanding.

Table of Contents

PROGRESS SOFTWARE CORPORATION  
FORM 10-Q  
FOR THE NINE MONTHS ENDED AUGUST 31, 2016  
INDEX

PART I FINANCIAL INFORMATION

Item 1.	<u>Financial Statements (Unaudited)</u>	<u>3</u>
	<u>Condensed Consolidated Balance Sheets as of August 31, 2016 and November 30, 2015</u>	<u>3</u>
	<u>Condensed Consolidated Statements of Operations for the three and nine months ended August 31, 2016 and 2015</u>	<u>4</u>
	<u>Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended August 31, 2016 and 2015</u>	<u>5</u>
	<u>Condensed Consolidated Statements of Cash Flows for the nine months ended August 31, 2016 and 2015</u>	<u>6</u>
	<u>Notes to Condensed Consolidated Financial Statements</u>	<u>8</u>
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>21</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>35</u>
Item 4.	<u>Controls and Procedures</u>	<u>35</u>

PART II OTHER INFORMATION

Item 1.	<u>Legal Proceedings</u>	<u>36</u>
Item 1A.	<u>Risk Factors</u>	<u>36</u>
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>42</u>
Item 5.	<u>Other Matters</u>	<u>42</u>
Item 6.	<u>Exhibits</u>	<u>42</u>
	<u>Signatures</u>	<u>43</u>
	<u>Exhibit Index</u>	<u>44</u>

Table of Contents

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements (Unaudited)

## Condensed Consolidated Balance Sheets

(In thousands, except share data)	August 31, 2016	November 30, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 188,084	\$ 212,379
Short-term investments	44,600	28,900
Total cash, cash equivalents and short-term investments	232,684	241,279
Accounts receivable (less allowances of \$1,565 and \$2,193, respectively)	55,758	66,459
Other current assets	20,521	15,671
Total current assets	308,963	323,409
Property and equipment, net	50,778	54,226
Intangible assets, net	87,684	114,113
Goodwill	370,097	369,985
Deferred tax assets	11,626	10,971
Other assets	3,631	4,419
Total assets	\$ 832,779	\$ 877,123
Liabilities and shareholders' equity		
Current liabilities:		
Current portion of long-term debt	\$ 13,125	\$ 9,375
Accounts payable	9,647	11,188
Accrued compensation and related taxes	20,967	29,720
Income taxes payable	5,098	2,941
Other accrued liabilities	17,796	21,465
Short-term deferred revenue	129,354	125,227
Total current liabilities	195,987	199,916
Long-term debt	123,750	135,000
Long-term deferred revenue	8,529	8,844
Deferred tax liabilities	6,149	7,112
Other noncurrent liabilities	3,785	3,787
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, \$0.01 par value; authorized, 1,000,000 shares; issued, none	—	—
Common stock, \$0.01 par value, and additional paid-in capital; authorized, 200,000,000 shares; issued and outstanding, 48,575,307 shares in 2016 and 50,579,539 shares in 2015	237,136	227,930
Retained earnings	281,303	319,162
Accumulated other comprehensive loss	(23,860 )	(24,628 )
Total shareholders' equity	494,579	522,464
Total liabilities and shareholders' equity	\$ 832,779	\$ 877,123
See notes to unaudited condensed consolidated financial statements.		

Table of Contents

## Condensed Consolidated Statements of Operations

(In thousands, except per share data)	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Revenue:				
Software licenses	\$33,624	\$ 31,840	\$86,366	\$ 85,794
Maintenance and services	68,394	62,797	201,251	179,042
Total revenue	102,018	94,637	287,617	264,836
Costs of revenue:				
Cost of software licenses	1,424	1,441	4,139	4,526
Cost of maintenance and services	11,825	9,612	33,217	31,174
Amortization of acquired intangibles	3,940	4,079	11,818	12,805
Total costs of revenue	17,189	15,132	49,174	48,505
Gross profit	84,829	79,505	238,443	216,331
Operating expenses:				
Sales and marketing	29,852	30,004	88,648	92,607
Product development	21,706	20,422	65,800	65,533
General and administrative	11,411	14,076	36,055	42,065
Amortization of acquired intangibles	3,186	3,186	9,556	9,559
Impairment of intangible assets	5,051	—	5,051	—
Restructuring expenses	(36 )	2,561	229	8,715
Acquisition-related expenses	53	662	449	3,180
Total operating expenses	71,223	70,911	205,788	221,659
Income (loss) from operations	13,606	8,594	32,655	(5,328 )
Other (expense) income:				
Interest expense	(1,174 )	(987 )	(3,244 )	(2,808 )
Interest income and other, net	260	450	686	1,153
Foreign currency (loss) gain, net	(374 )	(628 )	(1,916 )	397
Total other (expense) income, net	(1,288 )	(1,165 )	(4,474 )	(1,258 )
Income (loss) before income taxes	12,318	7,429	28,181	(6,586 )
Provision (benefit) for income taxes	4,742	11,555	10,114	(7,256 )
Net income (loss)	\$7,576	\$ (4,126 )	\$18,067	\$ 670
Earnings per share:				
Basic	\$0.16	\$ (0.08 )	\$0.36	\$ 0.01
Diluted	\$0.15	\$ (0.08 )	\$0.36	\$ 0.01
Weighted average shares outstanding:				
Basic	48,611	50,120	49,765	50,377
Diluted	49,135	50,120	50,310	51,117

See notes to unaudited condensed consolidated financial statements.

Table of Contents

## Condensed Consolidated Statements of Comprehensive Income (Loss)

(In thousands)	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Net income (loss)	\$7,576	\$(4,126)	\$18,067	\$ 670
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	(1,332)	(257)	485	(8,411)
Reclassification adjustment for losses included in net income, net of tax of \$0 for the third quarter and first nine months of 2016	—	—	256	—
Unrealized gains (losses) on investments, net of tax of \$16 for the third quarter and first nine months of 2016 and \$0 for the third quarter and first nine months of 2015	30	(17)	27	(52)
Total other comprehensive income (loss), net of tax	(1,302)	(274)	768	(8,463)
Comprehensive income (loss)	\$6,274	\$(4,400)	\$18,835	\$(7,793)

See notes to unaudited condensed consolidated financial statements.

Table of Contents

## Condensed Consolidated Statements of Cash Flows

(In thousands)	Nine Months Ended	
	August 31, 2016	August 31, 2015
Cash flows from operating activities:		
Net income	\$ 18,067	\$ 670
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	6,480	7,209
Amortization of intangibles and other	23,316	24,420
Stock-based compensation	19,009	18,812
Loss on disposal of property	364	—
Asset impairment	5,051	3,999
Deferred income taxes	(996)	(23,067)
Excess tax benefit from stock plans	(305)	(1,107)
Allowances for accounts receivable	(334)	356
Changes in operating assets and liabilities:		
Accounts receivable	11,209	11,160
Other assets	(3,866)	(508)
Accounts payable and accrued liabilities	(14,920)	(3,378)
Income taxes payable	2,025	7,367
Deferred revenue	3,810	31,255
Net cash flows from operating activities	68,910	77,188
Cash flows used in investing activities:		
Purchases of investments	(33,861)	(20,068)
Sales and maturities of investments	17,275	10,436
Purchases of property and equipment	(3,747)	(6,079)
Capitalized software development costs	—	(1,661)
Payments for acquisitions, net of cash	—	(246,275)

acquired				
Proceeds from divestitures, net	—		4,500	
Net cash flows used in investing activities	(20,333	)	(259,147	)
Cash flows (used in) from financing activities:				
Proceeds from stock-based compensation plans	8,166		10,459	
Purchases of stock related to withholding taxes from the issuance of restricted stock units	(2,751	)	(2,850	)
Repurchases of common stock	(71,507	)	(32,868	)
Excess tax benefit from stock plans	305		1,107	
Payment of contingent consideration	—		(209	)
Proceeds from the issuance of debt	—		150,000	
Payment of long-term debt	(7,500	)	(5,625	)
Payment of issuance costs for long-term debt	—		(1,787	)
Net cash flows (used in) from financing activities	(73,287	)	118,227	
Effect of exchange rate changes on cash	415		(10,237	)
Net decrease in cash and cash equivalents	(24,295	)	(73,969	)
Cash and cash equivalents, beginning of period	212,379		263,082	
Cash and cash equivalents, end of period	\$ 188,084		\$ 189,113	

Table of Contents

Condensed Consolidated Statements of Cash Flows, continued

	Nine Months Ended	
	August 31,	August 31,
	2016	2015
Supplemental disclosure:		
Cash paid for income taxes, net of refunds of \$781 in 2016 and \$1,887 in 2015	\$11,918	\$ 7,329
Cash paid for interest	\$2,348	\$ 2,150
Non-cash financing activities:		
Total fair value of restricted stock awards, restricted stock units and deferred stock units on date vested	\$12,137	\$ 9,963
See notes to unaudited condensed consolidated financial statements.		

7

---



Table of Contents

Notes to Condensed Consolidated Financial Statements

Note 1: Basis of Presentation

Company Overview - We are a global leader in application development, empowering the digital transformation organizations need to create and sustain engaging user experiences in today's evolving marketplace. With offerings spanning web, mobile and data for on-premise and cloud environments, we power startups and industry titans worldwide. Our solutions are used across a variety of industries.

Our products are generally sold as perpetual licenses, but certain products also use term licensing models and our cloud-based offerings use a subscription based model. More than half of our worldwide license revenue is realized through relationships with indirect channel partners, principally application partners and original equipment manufacturers (OEMs). Application partners are independent software vendors (ISVs) that develop and market applications using our technology and resell our products in conjunction with sales of their own products that incorporate our technology. OEMs are companies that embed our products into their own software products or devices.

We operate in North America and Latin America (the Americas); Europe, the Middle East and Africa (EMEA); and the Asia Pacific region, through local subsidiaries as well as independent distributors.

Basis of Presentation and Significant Accounting Policies - We prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (GAAP) for complete financial statements and these unaudited financial statements should be read in conjunction with the audited financial statements included in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015.

We made no significant changes in the application of our significant accounting policies that were disclosed in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015. We have prepared the accompanying unaudited condensed consolidated financial statements on the same basis as the audited financial statements included in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015, and these financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results of the interim periods presented. The operating results for the interim periods presented are not necessarily indicative of the results expected for the full fiscal year.

Recent Accounting Pronouncements - In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-15, Classification of Certain Cash Receipts and Cash Payments (ASU 2016-15). ASU 2016-15 is intended to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows and to eliminate the diversity in practice related to such classifications. The guidance in ASU 2016-15 is required for annual reporting periods beginning after December 15, 2017, with early adoption permitted. We are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated statement of cash flows.

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). ASU 2016-09 is intended to simplify various aspects of the accounting for employee share-based payment transactions, including accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The guidance in ASU 2016-09 is required for annual reporting periods beginning after December 15, 2016, with early adoption permitted. We are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated

financial position and results of operations.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (ASU 2016-02), which requires lessees to record most leases on their balance sheets, recognizing a lease liability for the obligation to make lease payments and a right-to-use asset for the right to use the underlying asset for the lease term. The guidance in ASU 2016-02 is required for annual reporting periods beginning after December 15, 2018, with early adoption permitted. We currently expect that most of our operating lease commitments will be subject to the update and recognized as operating lease liabilities and right-of-use assets upon adoption. However, we are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated financial position and results of operations.

Table of Contents

In April 2015, the FASB issued Accounting Standards Update No. 2015-03, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03). ASU 2015-03 requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability, consistent with the presentation of a debt discount. The guidance in ASU 2015-03 is required for annual reporting periods beginning after December 15, 2015, including interim periods within the reporting period. Early adoption is permitted for financial statements that have not been previously issued. We estimate that the impact on our consolidated balance sheets will be a reclassification of up to \$1.1 million from other assets to long-term debt as of December 1, 2016.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09). ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This new guidance is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. Early adoption is not permitted. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance. In July 2015, the FASB voted to defer the effective date of this ASU by one year for reporting periods beginning after December 15, 2017, with early adoption permitted as of the original effective date. As a result, the new effective date for the Company will be December 1, 2018. This update will impact the timing and amounts of revenue recognized. Management is currently assessing the impact the adoption of this ASU will have on the Company's consolidated financial statements.

## Note 2: Cash, Cash Equivalents and Investments

A summary of our cash, cash equivalents and available-for-sale investments at August 31, 2016 is as follows (in thousands):

	Amortized Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash	\$ 179,548	\$ —		\$ 179,548
Money market funds	8,536	—		8,536
State and municipal bond obligations	34,489	43		34,532
U.S. treasury bonds	6,534	—		6,534
U.S. government agency bonds	525	1	(4 )	522
Corporate bonds	3,006	6		3,012
Total	\$ 232,638	\$ 50	\$ (4 )	\$ 232,684

A summary of our cash, cash equivalents and available-for-sale investments at November 30, 2015 is as follows (in thousands):

	Amortized Cost Basis	Unrealized Gains	Unrealized Losses	Fair Value
Cash	\$ 186,241	\$ —	\$ —	\$ 186,241
Money market funds	26,138	—	—	26,138
State and municipal bond obligations	20,387	30	—	20,417
U.S. treasury bonds	3,109	—	(15 )	3,094
U.S. government agency bonds	1,645	—	(4 )	1,641
Corporate bonds	3,756	—	(8 )	3,748
Total	\$ 241,276	\$ 30	\$ (27 )	\$ 241,279



Table of Contents

Such amounts are classified on our condensed consolidated balance sheets as follows (in thousands):

	August 31, 2016		November 30, 2015	
	Cash and Equivalents	Short-Term Investments	Cash and Equivalents	Short-Term Investments
Cash	\$179,548	\$ —	\$186,241	\$ —
Money market funds	8,536	—	26,138	—
State and municipal bond obligations	—	34,532	—	20,417
U.S. treasury bonds	—	6,534	—	3,094
U.S. government agency bonds	—	522	—	1,641
Corporate bonds	—	3,012	—	3,748
Total	\$188,084	\$ 44,600	\$212,379	\$ 28,900

The fair value of debt securities by contractual maturity is as follows (in thousands):

	August 31, November 30,	
	2016	2015
Due in one year or less	\$ 23,474	\$ 15,945
Due after one year <sup>(1)</sup>	21,126	12,955
Total	\$ 44,600	\$ 28,900

(1) Includes state and municipal bond obligations and corporate bonds, which are securities representing investments available for current operations and are classified as current in the consolidated balance sheets.

We did not hold any investments with continuous unrealized losses as of August 31, 2016 and as of November 30, 2015.

### Note 3: Derivative Instruments

We generally use forward contracts that are not designated as hedging instruments to hedge economically the impact of the variability in exchange rates on intercompany accounts receivable and loans receivable denominated in certain foreign currencies. We generally do not hedge the net assets of our international subsidiaries. All forward contracts are recorded at fair value in other current assets or other accrued liabilities on the consolidated balance sheets at the end of each reporting period and expire from 30 days to one year. In the three and nine months ended August 31, 2016, realized and unrealized gains of \$2.2 million and \$1.4 million, respectively, from our forward contracts were recognized in foreign currency (loss) gain, net, in the condensed consolidated statements of operations. In the three and nine months ended August 31, 2015, realized and unrealized gains of \$0.6 million and realized and unrealized losses of \$1.9 million, respectively, from our forward contracts were recognized in foreign currency gain (loss), net, in the condensed consolidated statements of operations. The gains and losses were substantially offset by realized and unrealized losses and gains on the offsetting positions.

The table below details outstanding foreign currency forward contracts where the notional amount is determined using contract exchange rates (in thousands):

	August 31, 2016		November 30, 2015	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Forward contracts to sell U.S. dollars	\$83,992	\$ (5,170 )	\$76,748	\$ (4,026 )
Forward contracts to purchase U.S. dollars	2,209	4	2,077	5
Total	\$86,201	\$ (5,166 )	\$78,825	\$ (4,021 )



Table of Contents

## Note 4: Fair Value Measurements

## Recurring Fair Value Measurements

The following table details the fair value measurements within the fair value hierarchy of our financial assets and liabilities at August 31, 2016 (in thousands):

	Total Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
<b>Assets</b>				
Money market funds	\$ 8,536	\$ 8,536	\$—	\$ —
State and municipal bond obligations	34,532	—	34,532	—
U.S. treasury bonds	6,534	—	6,534	—
U.S. government agency bonds	522	—	522	—
Corporate bonds	3,012	—	3,012	—
<b>Liabilities</b>				
Foreign exchange derivatives	\$(5,166 )	\$—	\$(5,166)	\$ —

The following table details the fair value measurements within the fair value hierarchy of our financial assets and liabilities at November 30, 2015 (in thousands):

	Total Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
<b>Assets</b>				
Money market funds	\$ 26,138	\$ 26,138	\$—	\$ —
State and municipal bond obligations	20,417	—	20,417	—
U.S. treasury bonds	3,094	—	3,094	—
U.S. government agency bonds	1,641	—	1,641	—
Corporate bonds	3,748	—	3,748	—
<b>Liabilities</b>				
Foreign exchange derivatives	\$(4,021 )	\$—	\$(4,021)	\$ —

When developing fair value estimates, we maximize the use of observable inputs and minimize the use of unobservable inputs. When available, we use quoted market prices to measure fair value. The valuation technique used to measure fair value for our Level 1 and Level 2 assets is a market approach, using prices and other relevant information generated by market transactions involving identical or comparable assets. If market prices are not available, the fair value measurement is based on models that use primarily market based parameters including yield curves, volatilities, credit ratings and currency rates. In certain cases where market rate assumptions are not available, we are required to make judgments about assumptions market participants would use to estimate the fair value of a financial instrument.

The following table reflects the activity for our liabilities measured at fair value using Level 3 inputs, which relate to a contingent consideration obligation in connection with a prior acquisition, for each period presented (in thousands):

	Three Months Ended August 31, 2015	Nine Months Ended August 31, 2015
Balance, beginning of period	\$ 295	\$ 1,717
Changes in fair value of contingent consideration obligation	—(295 )	—(1,508 )
Transfer to Level 2 fair value measurement	—	—(209 )
Balance, end of period	\$ —	\$ —



Table of Contents

We recorded credits of approximately \$0.3 million and \$1.5 million during the three and nine months ended August 31, 2015, respectively, due to the change in fair value of a contingent consideration obligation in connection with a prior acquisition, which is included in acquisition-related expenses in our condensed consolidated statement of operations. The contingent consideration obligation was reduced to \$0 during the fiscal year ended November 30, 2015.

## Nonrecurring Fair Value Measurements

During the third quarter of fiscal year 2016, certain assets have been measured at fair value on a nonrecurring basis using significant unobservable inputs (Level 3). Based on the fair value measurement, we recorded a \$5.1 million asset impairment charge as of August 31, 2016, which was applicable to the intangible assets obtained in connection with our acquisition of Modulus during the second quarter of fiscal year 2014 (Note 5).

The following table presents nonrecurring fair value measurements as of August 31, 2016 (in thousands):

	Total Fair Value	Total Losses
Intangible assets \$		—\$ 5,051

The fair value measurement was determined using an income-based valuation methodology, which incorporates unobservable inputs, including expected cash flows over the remaining estimated useful life of the technology, thereby classifying the fair value as a Level 3 measurement within the fair value hierarchy. The expected cash flows include subscription fees to be collected from existing customers using the platform, offset by hosting fees and compensation related costs to be incurred over the remaining estimated useful life.

## Note 5: Intangible Assets and Goodwill

## Intangible Assets

Intangible assets are comprised of the following significant classes (in thousands):

	August 31, 2016			November 30, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Purchased technology	\$109,880	\$(64,438)	\$45,442	\$117,151	\$(54,963)	\$62,188
Customer-related	67,602	(33,257)	34,345	67,602	(25,493)	42,109
Trademarks and trade names	15,140	(7,243)	7,897	15,330	(5,514)	9,816
Total	\$192,622	\$(104,938)	\$87,684	\$200,083	\$(85,970)	\$114,113

During the third quarter of fiscal year 2016, we evaluated the ongoing value of the intangible assets associated with the technology obtained in connection with the acquisition of Modulus. As a result of our decision to abandon the related assets due to a change in our expected ability to use the technology internally, we determined that the intangible assets were fully impaired. As a result, we incurred an impairment charge of \$5.1 million in the third quarter of fiscal year 2016.

In the three and nine months ended August 31, 2016, amortization expense related to intangible assets was \$7.1 million and \$21.4 million, respectively. In the three and nine months ended August 31, 2015, amortization expense

related to intangible assets was \$7.3 million and \$22.4 million, respectively.

Table of Contents

Future amortization expense for intangible assets as of August 31, 2016, is as follows (in thousands):

Remainder of 2016	\$6,852
2017	27,426
2018	26,613
2019	25,489
2020	714
Thereafter	590
Total	\$87,684

## Goodwill

Changes in the carrying amount of goodwill in the nine months ended August 31, 2016 are as follows (in thousands):

Balance, November 30, 2015	\$369,985
Translation adjustments	112
Balance, August 31, 2016	\$370,097

Changes in the goodwill balances by reportable segment in the nine months ended August 31, 2016 are as follows (in thousands):

	November 30, 2015	Translation Adjustments	August 31, 2016
OpenEdge	\$211,980	\$ 112	\$212,092
Data Connectivity and Integration	19,040	—	19,040
Application Development and Deployment	138,965	—	138,965
Total goodwill	\$369,985	\$ 112	\$370,097

During the fourth quarter of fiscal year 2015, we completed our annual testing for impairment of goodwill and, based on those tests, concluded that no impairment of goodwill existed as of October 31, 2015. During the quarter ending August 31, 2016, no triggering events have occurred that would indicate that it is more likely than not that the carrying values of any of our reporting units exceeded their fair values.

## Note 6: Business Combinations

## Telerik Acquisition

On December 2, 2014, we completed the acquisition of all of the outstanding securities of Telerik AD (Telerik), a leading provider of application development tools based in Sofia, Bulgaria, for total consideration of \$262.5 million. Approximately \$10.5 million of the total consideration was paid to Telerik's founders and certain other key employees in restricted stock units, subject to a vesting schedule and continued employment. Under the Securities Purchase Agreement, 10% of the total consideration was deposited into an escrow account to secure certain indemnification and other obligations of the sellers to Progress. In accordance with the agreement, the full amount of the escrow was released to the former equity holders in June 2016.

Through this acquisition, we now provide comprehensive cloud and on-premise platform offerings that enable developers to rapidly create applications, driven by data for any web, desktop or mobile platform. We funded the acquisition through a combination of existing cash resources and a \$150 million term loan (Note 7).

Acquisition-related transaction costs (e.g., legal, due diligence, valuation, and other professional fees) and certain acquisition restructuring and related charges are not included as a component of consideration transferred, but are required to be expensed as incurred. We incurred \$0 and \$0.3 million of acquisition-related costs during the three and nine months ended August 31, 2016, respectively, and \$0.8 million and \$2.7 million during the three and nine months ended August 31, 2015, respectively, which are included in acquisition-related expenses in our condensed consolidated statement of operations.

Table of Contents

In connection with the acquisition of Telerik, we agreed to provide retention bonuses to certain Telerik employees as an incentive for those employees to remain with Telerik for at least one year following the acquisition. We concluded that the retention bonuses for these individuals, which totaled approximately \$2.2 million, are compensation arrangements and recognized these costs over the one-year service period. During the three and nine months ended August 31, 2015, we incurred \$0.6 million and \$1.8 million of expense related to the retention bonuses, respectively, which is included in the acquisition-related expenses in our consolidated statement of operations. There were no additional expenses related to the retention bonuses incurred during the three and nine months ended August 31, 2016 and the entire amount accrued during fiscal year 2015 was paid in December 2015.

The operations of Telerik are included in our operating results as part of the Application Development and Deployment segment from the date of acquisition. The amount of revenue of Telerik included in our condensed consolidated statement of operations during the three and nine months ended August 31, 2016 was \$19.4 million and \$56.0 million, respectively. The amount of revenue of Telerik included in our condensed consolidated statement of operations during the three and nine months ended August 31, 2015 was \$12.5 million and \$26.2 million, respectively. The revenue from sales of Telerik products and maintenance is primarily recognized ratably over the maintenance period, which is generally one year, as vendor specific objective evidence of fair value cannot be established for such maintenance. The amount of pretax losses of Telerik included in our condensed consolidated statement of operations during the three and nine months ended August 31, 2016 was \$7.0 million and \$20.2 million, respectively. The amount of pretax losses of Telerik included in our condensed consolidated statement of operations during the three and nine months ended August 31, 2015 was \$10.2 million and \$41.2 million, respectively. The pretax losses in each three and nine month period includes the amortization expense of approximately \$6.2 million and \$18.5 million, respectively, related to the acquired intangible assets discussed above. In addition, the pretax losses in the three and nine months ended August 31, 2016 includes stock-based compensation expense of approximately \$2.2 million and \$6.5 million, respectively.

Note 7: Term Loan and Line of Credit

Our credit agreement provides for a \$150 million secured term loan and a \$150 million secured revolving credit facility, which may be made available in U.S. Dollars and certain other currencies. The revolving credit facility may be increased by up to an additional \$75 million if the existing or additional lenders are willing to make such increased commitments. We borrowed the \$150 million term loan included in our credit agreement to partially fund our acquisition of Telerik, as described in Note 6. The revolving credit facility has sublimits for swing line loans up to \$25.0 million and for the issuance of standby letters of credit in a face amount up to \$25.0 million. We expect to use the revolving credit facility for general corporate purposes, including acquisitions of other businesses, and may also use it for working capital.

The credit facility matures on December 2, 2019, when all amounts outstanding will be due and payable in full. The revolving credit facility does not require amortization of principal. The outstanding balance of the \$150 million term loan as of August 31, 2016 was \$136.9 million, with \$13.1 million due in the next 12 months. The term loan requires repayment of principal at the end of each fiscal quarter, beginning with the fiscal quarter ended February 28, 2015. The first eight payments are in the principal amount of \$1.9 million each, the following eight payments are in the principal amount of \$3.8 million each, the following three payments are in the principal amount of \$5.6 million each, and the last payment is of the remaining principal amount. The term loan may be prepaid before maturity in whole or in part at our option without penalty or premium. As of August 31, 2016, the carrying value of the term loan approximates the fair value, based on Level 2 inputs (observable market prices in less than active markets), as the interest rate is variable over the selected interest period and is similar to current rates at which we can borrow funds. The interest rate of the credit facility as of August 31, 2016 was 2.25%.

Costs incurred to obtain our long-term debt of \$1.8 million were recorded as debt issuance costs within other assets in our consolidated balance sheet as of August 31, 2016 and are being amortized over the term of the debt agreement using the effective interest rate method. Amortization expense related to debt issuance costs of \$0.1 million and \$0.3 million for the three and nine months ended August 31, 2016, respectively, and \$0.1 million and \$0.3 million for the three and nine months ended August 31, 2015, respectively, is recorded within interest expense in our condensed consolidated statements of operations.

Revolving loans may be borrowed, repaid and reborrowed until December 2, 2019, at which time all amounts outstanding must be repaid. As of August 31, 2016, there were no amounts outstanding under the revolving line and \$0.5 million of letters of credit.

Table of Contents

As of August 31, 2016, aggregate principal payments of long-term debt for the next five years and thereafter are (in thousands):

Remainder of 2016	\$1,875
2017	15,000
2018	15,000
2019	105,000
Total	\$136,875

## Note 8: Common Stock Repurchases

We repurchased and retired 0.4 million shares of our common stock for \$11.5 million in the three months ended August 31, 2016 and 2.8 million shares for \$71.5 million in the nine months ended August 31, 2016. We did not repurchase shares of our common stock during the three months ended August 31, 2015 and in the nine months ended August 31, 2015, we repurchased and retired 1.3 million shares for \$32.9 million. The shares were repurchased in both periods as part of our Board of Directors authorized share repurchase program.

In March 2016, our Board of Directors authorized a new \$100.0 million share repurchase program, which increased the total authorization to \$202.8 million. As of August 31, 2016, there is \$143.0 million remaining under this current authorization.

## Note 9: Stock-Based Compensation

Stock-based compensation expense reflects the fair value of stock-based awards measured at the grant date and recognized over the relevant service period. We estimate the fair value of each stock-based award on the measurement date using the current market price of the stock or the Black-Scholes option valuation model. In addition, during the first quarter of fiscal year 2014, each of the first three quarters of fiscal year 2015, and the first and third quarters of fiscal year 2016, we granted performance-based restricted stock units to members of executive management that include a three-year market condition. In order to estimate the fair value of such awards, we used a Monte Carlo Simulation valuation model. The Black-Scholes and Monte Carlo Simulation valuation models incorporate assumptions as to stock price volatility, the expected life of options or awards, a risk-free interest rate and dividend yield. We recognize stock-based compensation expense related to options and restricted stock units on a straight-line basis over the service period of the award, which is generally 4 or 5 years for options and 3 years for restricted stock units. We recognize stock-based compensation expense related to performance stock units and our employee stock purchase plan using an accelerated attribution method.

The following table provides the classification of stock-based compensation as reflected in our condensed consolidated statements of operations (in thousands):

	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Cost of maintenance and services	\$223	\$ 144	\$599	\$ 462
Sales and marketing	751	1,604	2,792	4,328
Product development	2,524	912	7,600	3,476
General and administrative	2,281	3,878	8,018	10,546
Total stock-based compensation	\$5,779	\$ 6,538	\$19,009	\$ 18,812





Table of Contents

## Note 10: Accumulated Other Comprehensive Loss

The following table summarizes the changes in accumulated balances of other comprehensive loss during the nine months ended August 31, 2016 (in thousands):

	Foreign Currency Translation Adjustment	Unrealized Gains (Losses) on Investments	Accumulated Other Comprehensive Loss
Balance, December 1, 2015	\$ (24,582 )	\$ (46 )	\$ (24,628 )
Other comprehensive loss before reclassifications, net of tax	485	27	512
Amounts reclassified from accumulated other comprehensive loss to realized losses included in earnings	256	—	256
Balance, August 31, 2016	\$ (23,841 )	\$ (19 )	\$ (23,860 )

The tax effect on accumulated unrealized gains (losses) on investments was minimal as of August 31, 2016 and November 30, 2015.

## Note 11: Restructuring Charges

The following table provides a summary of activity for all of the restructuring actions, which are detailed further below (in thousands):

	Excess Facilities and Other Costs	Employee Severance and Related Benefits	Total
Balance, December 1, 2015	\$ 412	\$ 2,949	\$3,361
Costs incurred	338	(109 )	229
Cash disbursements	(514 )	(2,487 )	(3,001 )
Translation adjustments and other	4	20	24
Balance, August 31, 2016	\$ 240	\$ 373	\$613

## 2015 Restructurings

During the first quarter of fiscal year 2015, we restructured our operations in connection with the acquisition of Telerik. This restructuring resulted in a reduction of redundant positions primarily within the administrative functions. This restructuring also resulted in the closing of two facilities as well as asset impairment charges for assets no longer deployed as a result of the acquisition. During the second and third quarters of fiscal year 2015, we incurred additional costs with respect to this restructuring, including reduction of redundant positions primarily within the product development function, as well as an impairment charge discussed further below.

Restructuring expenses are related to employee costs, including severance, health benefits and outplacement services (but excluding stock-based compensation), facilities costs, which include fees to terminate lease agreements and costs for unused space, net of sublease assumptions, and other costs, which include asset impairment charges.

During the second quarter of fiscal year 2015, we decided to replace our existing cloud-based mobile application development technology with technology acquired in connection with the acquisition of Telerik. Accordingly, we evaluated the ongoing value of the assets associated with this prior mobile technology and, based on this evaluation, we determined that the long-lived assets with a carrying amount of \$4.0 million were no longer recoverable and were

impaired and wrote them down to their estimated fair value of \$0.1 million. Fair value was based on expected future cash flows using Level 3 inputs under ASC 820.

As part of this first quarter of fiscal year 2015 restructuring, for the three months ended August 31, 2016 we incurred minimal expenses and for the nine months ended August 31, 2016 we incurred expenses of \$0.3 million. For the three and nine months ended August 31, 2015, we incurred expenses of \$2.5 million and \$7.4 million, respectively. The expenses are recorded as restructuring expenses in the condensed consolidated statements of operations. We do not expect to incur additional material costs with respect to this restructuring.

Table of Contents

A summary of the first nine months of fiscal year 2016 activity for this restructuring action is as follows (in thousands):

	Excess Facilities and Other Costs	Employee Severance and Related Benefits	Total
Balance, December 1, 2015	\$ 209	\$ 309	\$518
Costs incurred	323	(43 )	280
Cash disbursements	(358 )	(267 )	(625 )
Translation adjustments and other	4	3	7
Balance, August 31, 2016	\$ 178	\$ 2	\$180

Cash disbursements for expenses incurred to date under this restructuring are expected to be made through the fourth quarter of fiscal year 2016. As a result, the total amount of the restructuring reserve of \$0.2 million is included in other accrued liabilities on the condensed consolidated balance sheet at August 31, 2016.

During the fourth quarter of fiscal year 2015, our management approved, committed to and initiated plans to make strategic changes to our organization to further build on the focus gained from operating under our business segment structure and to enable stronger cross-collaboration among product management, marketing and sales teams and a tighter integration of the product management and product development teams. In connection with the new organizational structure, we no longer have presidents of our three segments, as well as certain other positions within the administrative organization. Our Chief Operating Officer, appointed during fiscal year 2015, assumed responsibility for driving the operations of our three segments. The organizational changes did not result in the closing of any of our facilities.

Restructuring expenses are related to employee costs, including severance, health benefits and outplacement services (but excluding stock-based compensation), and other costs, which include charges for the abandonment of certain assets.

As part of this fourth quarter of fiscal year 2015 restructuring, for the three and nine months ended August 31, 2016, we recorded a minimal credit to restructuring expenses in the consolidated statements of operations due to changes in estimates of severance to be paid. We do not expect to incur additional material costs with respect to this restructuring.

A summary of the first nine months of fiscal year 2016 activity for this restructuring action is as follows (in thousands):

	Excess Facilities and Other Costs	Employee Severance and Related Benefits	Total
Balance, December 1, 2015	\$ —	—\$ 2,617	\$2,617
Costs incurred	—	(42 )	(42 )
Cash disbursements	—	(2,220 )	(2,220 )
Translation adjustments and other	—	16	16
Balance, August 31, 2016	\$ —	—\$ 371	\$371

Cash disbursements for expenses incurred to date under this restructuring are expected to be made through the fourth quarter of fiscal year 2016. As a result, the total amount of the restructuring reserve of \$0.4 million is included in other accrued liabilities on the condensed consolidated balance sheet at August 31, 2016.

## 2012 - 2014 Restructurings

During fiscal years 2012, 2013, and 2014, our management approved, committed to and initiated plans to make strategic changes to our organization to provide greater focus and agility in the delivery of next generation application development, deployment and integration solutions. During each of these fiscal years, we took restructuring actions that involved the elimination of personnel and/or the closure of facilities.

As part of these restructuring actions, for the three and nine months ended August 31, 2016, we incurred minimal expenses, and for the three and nine months ended August 31, 2015, we incurred expenses of \$0 and \$1.3 million, respectively, which are related to employee costs, including severance, health benefits, and outplacement services (but excluding stock-based

Table of Contents

compensation), and facilities costs, which include fees to terminate lease agreements and costs for unused space, net of sublease assumptions. The expenses are recorded as restructuring expenses in the condensed consolidated statements of operations. We do not expect to incur additional material costs with respect to the 2012, 2013, and 2014 restructuring actions. The restructuring reserve of \$0.1 million is included in other accrued liabilities on the condensed consolidated balance sheet as of August 31, 2016.

## Note 12: Income Taxes

Our income tax provision for the third quarter of fiscal years 2016 and 2015 reflects our estimates of the effective tax rates expected to be applicable for the full fiscal years, adjusted for any discrete events which are recorded in the period they occur. The estimates are reevaluated each quarter based on our estimated tax expense for the full fiscal year.

The decrease in our effective tax rate in the nine months ended August 31, 2016 compared to the same period in the prior year is primarily due to the jurisdictional mix of profits as a result of the acquisition of Telerik, where substantial losses were incurred in Bulgaria in fiscal year 2015 and tax effected at a 10% statutory rate and other jurisdictions' earnings, primarily in the United States, were taxed at higher rates.

In addition, during the preparation of our condensed consolidated financial statements for the three months ended May 31, 2016, we identified an error in our prior year income tax provision whereby income tax expense was overstated for the year ended November 30, 2015 by \$2.7 million related to our tax treatment of an intercompany gain. We determined that the error is not material to the prior year financial statements. We also concluded that recording an out-of-period correction would not be material and have therefore corrected this error by recording an out-of-period \$2.7 million tax benefit in our interim financial statements for the periods ended May 31, 2016.

The Internal Revenue Service is currently examining our U.S. Federal income tax returns for fiscal years 2013 and 2014. Our Federal income tax returns have been examined or are closed by statute for all years prior to fiscal year 2012, and we are no longer subject to audit for those periods. Our state income tax returns have been examined or are closed by statute for all years prior to fiscal year 2011, and we are no longer subject to audit for those periods.

Tax authorities for certain non-U.S. jurisdictions are also examining returns, none of which are material to our consolidated balance sheets, cash flows or statements of income. With some exceptions, we are generally no longer subject to tax examinations in non-U.S. jurisdictions for years prior to fiscal year 2010.

## Note 13: Earnings Per Share

We compute basic earnings per share using the weighted average number of common shares outstanding. We compute diluted earnings per share using the weighted average number of common shares outstanding plus the effect of outstanding dilutive stock options, restricted stock units and deferred stock units, using the treasury stock method. The following table sets forth the calculation of basic and diluted earnings per share on an interim basis (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Net income (loss)	\$7,576	\$(4,126)	\$18,067	\$ 670
Weighted average shares outstanding	48,611	50,120	49,765	50,377
Dilutive impact from common stock equivalents	524	—	545	740

Edgar Filing: PROGRESS SOFTWARE CORP /MA - Form 10-Q

Diluted weighted average shares outstanding	49,135	50,120	50,310	51,117
Basic earnings per share	\$0.16	\$(0.08)	) \$0.36	\$ 0.01
Diluted earnings per share	\$0.15	\$(0.08)	) \$0.36	\$ 0.01

We excluded stock awards representing approximately 287,000 shares and 423,000 shares of common stock from the calculation of diluted earnings per share in the three and nine months ended August 31, 2016, respectively, because these awards were anti-dilutive. In the three and nine months ended August 31, 2015, we excluded stock awards representing 1,173,000 shares and 296,000 shares of common stock, respectively, from the calculation of diluted earnings per share as they were anti-dilutive.

Table of Contents

## Note 14: Business Segments and International Operations

Operating segments are components of an enterprise that engage in business activities for which discrete financial information is available and regularly reviewed by the chief operating decision maker in deciding how to allocate resources and assess performance. Our chief operating decision maker is the combination of our Chief Executive Officer and Chief Operating Officer.

We do not manage our assets or capital expenditures by segment or assign other income (expense) and income taxes to segments. We manage and report such items on a consolidated company basis.

The following table provides revenue and contribution from our reportable segments and reconciles to the consolidated income (loss) before income taxes:

(In thousands)	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Segment revenue:				
OpenEdge	\$67,534	\$73,398	\$198,595	\$214,775
Data Connectivity and Integration	14,251	8,281	30,852	22,669
Application Development and Deployment	20,233	12,958	58,170	27,392
Total revenue	102,018	94,637	287,617	264,836
Segment costs of revenue and operating expenses:				
OpenEdge	18,180	18,550	53,539	56,529
Data Connectivity and Integration	2,828	3,180	8,863	9,563
Application Development and Deployment	11,021	9,933	29,555	30,169
Total costs of revenue and operating expenses	32,029	31,663	91,957	96,261
Segment contribution:				
OpenEdge	49,354	54,848	145,056	158,246
Data Connectivity and Integration	11,423	5,101	21,989	13,106
Application Development and Deployment	9,212	3,025	28,615	(2,777 )
Total contribution	69,989	62,974	195,660	168,575
Other unallocated expenses (1)	56,383	54,380	163,005	173,903
Income (loss) from operations	13,606	8,594	32,655	(5,328 )
Other (expense) income, net	(1,288 )	(1,165 )	(4,474 )	(1,258 )
Income (loss) before income taxes	\$12,318	\$7,429	\$28,181	\$(6,586 )

(1) The following expenses are not allocated to our segments as we manage and report our business in these functional areas on a consolidated basis only: product development, corporate marketing, administration, amortization and impairment of acquired intangibles, stock-based compensation, restructuring, and acquisition related expenses.

Our revenues are derived from licensing our products, and from related services, which consist of maintenance and consulting and education. Information relating to revenue from customers by revenue type is as follows (in thousands):

(In thousands)	Three Months Ended	Nine Months Ended
----------------	--------------------	-------------------

Edgar Filing: PROGRESS SOFTWARE CORP /MA - Form 10-Q

	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
Software licenses	\$33,624	\$31,840	\$86,366	\$85,794
Maintenance	60,368	55,365	178,189	157,259
Professional services	8,026	7,432	23,062	21,783
Total	\$102,018	\$94,637	\$287,617	\$264,836



Table of Contents

In the following table, revenue attributed to North America includes sales to customers in the U.S. and sales to certain multinational organizations. Revenue from Europe, the Middle East and Africa (EMEA), Latin America and the Asia Pacific region includes sales to customers in each region plus sales from the U.S. to distributors in these regions. Information relating to revenue from external customers from different geographical areas is as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	August 31, 2016	August 31, 2015	August 31, 2016	August 31, 2015
(In thousands)				
North America	\$58,275	\$49,810	\$160,732	\$139,454
EMEA	32,719	30,656	95,517	89,667
Latin America	4,667	4,621	12,749	13,977
Asia Pacific	6,357	9,550	18,619	21,738
Total	\$102,018	\$94,637	\$287,617	\$264,836

## Note 15: Subsequent Events

On September 27, 2016, our Board of Directors approved the initiation of a quarterly cash dividend to Progress shareholders. The first quarterly dividend of \$0.125 per share of common stock will be paid on December 15, 2016 to shareholders of record as of the close of business on December 1, 2016.

On September 28, 2016, we announced the appointment of Kurt J. Abkemeier as our new chief financial officer. As CFO, Mr. Abkemeier will oversee the company's global finance and accounting operations and be a member of the company's executive leadership team, reporting to Phil Pead, president and chief executive officer. Mr. Abkemeier succeeds Chris E. Perkins, who informed the company in March 2016 that he would retire as CFO upon the appointment of his successor. Mr. Abkemeier began as CFO at Progress on September 28, 2016.

Table of Contents

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

Cautionary Note Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 contains certain safe harbor provisions regarding forward-looking statements. This Form 10-Q, and other information provided by us or statements made by our directors, officers or employees from time to time, may contain "forward-looking" statements and information, which involve risks and uncertainties. Actual future results may differ materially. Statements indicating that we "expect," "estimate," "believe," "are planning" or "plan to" are forward-looking, as are other statements concerning future financial results, product offerings or other events that have not yet occurred. There are various factors that could cause actual results or events to differ materially from those anticipated by the forward-looking statements, including but not limited to the following: (1) Economic, geopolitical and market conditions, including the continued difficult economic environment in Brazil, and the continued slow economic recovery in Europe, parts of the U.S. and other parts of the world, can adversely affect our business, results of operations and financial condition, including our revenue growth and profitability, which in turn could adversely affect our stock price. (2) We may fail to achieve our financial forecasts due to such factors as delays or size reductions in transactions, fewer large transactions in a particular quarter, fluctuations in currency exchange rates, or a decline in our renewal rates for contracts. (3) Our ability to successfully manage transitions to new business models and markets, including an increased emphasis on a cloud and subscription strategy, may not be successful. (4) If we are unable to develop new or sufficiently differentiated products and services, or to enhance and improve our existing products and services in a timely manner to meet market demand, partners and customers may not purchase new software licenses or subscriptions or purchase or renew support contracts. (5) We depend upon our extensive partner channel and we may not be successful in retaining or expanding our relationships with channel partners. (6) Our international sales and operations subject us to additional risks that can adversely affect our operating results, including risks relating to foreign currency gains and losses. (7) If the security measures for our software, services or other offerings are compromised or subject to a successful cyber-attack, or if such offerings contain significant coding or configuration errors, we may experience reputational harm, legal claims and financial exposure. (8) We may make acquisitions in the future and those acquisitions may not be successful, may involve unanticipated costs or other integration issues or may disrupt our existing operations and those factors discussed in Part II, Item 1A (Risk Factors) in this Quarterly Report on Form 10-Q, and in Part I, Item 1A (Risk Factors) in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015. Although we have sought to identify the most significant risks to our business, we cannot predict whether, or to what extent, any of such risks may be realized. We also cannot assure you that we have identified all possible issues which we might face. We undertake no obligation to update any forward-looking statements that we make.

Use of Constant Currency

Revenue from our international operations has historically represented a substantial portion of our total revenue. As a result, our revenue results have been impacted, and we expect will continue to be impacted, by fluctuations in foreign currency exchange rates. For example, if the local currencies of our foreign subsidiaries weaken, our consolidated results stated in U.S. dollars are negatively impacted.

As exchange rates are an important factor in understanding period to period comparisons, we believe the presentation of revenue growth rates on a constant currency basis enhances the understanding of our revenue results and evaluation of our performance in comparison to prior periods. The constant currency information presented is calculated by translating current period results using prior period weighted average foreign currency exchange rates. These results should be considered in addition to, not as a substitute for, results reported in accordance with accounting principles generally accepted in the United States of America (GAAP).

Overview

We are a global leader in application development, empowering the digital transformation organizations need to create and sustain engaging user experiences in today's evolving marketplace. With offerings spanning web, mobile and data for on-premise and cloud environments, we power startups and industry titans worldwide. Our solutions are used across a variety of industries. We operate as three distinct segments: OpenEdge, Data Connectivity and Integration, and Application Development and Deployment, each with dedicated product management and product marketing functions.

At the beginning of fiscal year 2015, we acquired Telerik AD, a leading provider of application development tools. Telerik enables its 1.9 million strong developer community to create compelling user experiences across cloud, web, mobile and desktop applications. Through this acquisition, we provide comprehensive cloud and on-premise platform offerings that enable developers to rapidly create applications, driven by data for any web, desktop or mobile platform.

## Table of Contents

The revenue of Telerik is being recognized ratably over the maintenance period, which is generally one year, as vendor specific objective evidence (or VSOE) of fair value cannot be established for such maintenance. As a result of acquisition accounting, the acquired deferred revenue balance was significantly reduced to reflect its fair value as of the acquisition date. However, we are still incurring the associated costs to fulfill the acquired deferred revenue, which are reflected in our consolidated statement of operations. As a result, during fiscal year 2015, our expenses as a percentage of total revenue were higher than we expect they will be in future periods once this acquired deferred revenue balance is recognized. The impact of this on fiscal year 2016 has been, and is expected to continue to be, minimal.

In the first nine months of fiscal year 2016, our results were adversely impacted by decreases in sales to OpenEdge direct enterprise customers. During the past three fiscal years, our results have benefited from several large license sales to OpenEdge direct enterprise customers. These large transactions are difficult to predict as they are subject to longer sales cycles and the timing of completion is often uncertain. If we fail to complete these large transactions or if completion is delayed, our results will be adversely impacted.

In March 2016, our Board of Directors authorized a new \$100.0 million share repurchase program, which increased the total authorization to \$202.8 million. During the three months ended August 31, 2016, we repurchased and retired 0.4 million shares of our common stock for \$11.5 million. As of August 31, 2016, there is \$143.0 million remaining under the current authorization.

In September 2016, our Board of Directors approved the initiation of a quarterly cash dividend to Progress shareholders. The first quarterly dividend of \$0.125 per share of common stock will be paid on December 15, 2016 to shareholders of record as of the close of business on December 1, 2016.

We derive a significant portion of our revenue from international operations, which are primarily conducted in foreign currencies. As a result, changes in the value of these foreign currencies relative to the U.S. dollar have significantly impacted our results of operations and may impact our future results of operations. Beginning in the fourth quarter of 2014, the value of the U.S. dollar strengthened in comparison to certain foreign currencies, including in Europe, Brazil and Australia, and continued to strengthen during the first half of 2015. The U.S. dollar has remained strong in comparison to foreign currencies in 2016. Since approximately one-third of our revenue is denominated in foreign currency, our revenue results have been negatively impacted, and we expect will continue to be impacted, by fluctuations in foreign currency exchange rates.

In addition, the announcement of the Referendum of the United Kingdom's (or the U.K.) Membership of the European Union (E.U.) (referred to as Brexit), advising for the exit of the United Kingdom from the European Union, has resulted in significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the further strengthening of the U.S. dollar against foreign currencies. The announcement of Brexit may create further global economic uncertainty, which may cause our customers to closely monitor their costs and reduce their spending budget on our products and services. If the Referendum is passed into law, there could be further uncertainty as the U.K. determines the future terms of its relationship with the E.U. Any of these effects of Brexit, among others, could materially adversely affect our business, results of operations and financial condition.

We have evaluated, and expect to continue to evaluate, possible acquisitions and other strategic transactions designed to expand our business and/or add complementary products and technologies to our existing product sets. As a result, our expected uses of cash could change, our cash position could be reduced and we may incur additional debt obligations to the extent we complete additional acquisitions.

We believe that existing cash balances, together with funds generated from operations and amounts available under our credit facility, will be sufficient to finance our operations and meet our foreseeable cash requirements, including

our newly announced quarterly cash dividend to Progress shareholders, through at least the next twelve months.

Table of Contents

## Results of Operations

## Revenue

	Three Months Ended		Percentage Change	
(In thousands)	August 31, 2016	August 31, 2015	As Reported	Constant Currency
Revenue	\$ 102,018	\$ 94,637	8 %	9 %
	Nine Months Ended		Percentage Change	
(In thousands)	August 31, 2016	August 31, 2015	As Reported	Constant Currency
Revenue	\$ 287,617	\$ 264,836	9 %	11 %

Total revenue increased \$7.4 million, or 8%, in the third quarter of fiscal year 2016 as compared to the same quarter last year. Revenue would have increased by 9% if exchange rates had been constant during the period as compared to exchange rates in the same quarter last year. In addition, total revenue increased \$22.8 million, or 11% on a constant currency basis and 9% using actual exchange rates, in the first nine months of fiscal year 2016 as compared to the same period last year. The increase in all periods was primarily a result of an increase in maintenance and services revenue as further described below. Changes in prices from fiscal year 2015 to 2016 did not have a significant impact on our revenue.

## License Revenue

	Three Months Ended		Percentage Change	
(In thousands)	August 31, 2016	August 31, 2015	As Reported	Constant Currency
License	\$ 33,624	\$ 31,840	6 %	6 %
As a percentage of total revenue	33 %	34 %		
	Nine Months Ended		Percentage Change	
(In thousands)	August 31, 2016	August 31, 2015	As Reported	Constant Currency
License	\$ 86,366	\$ 85,794	1 %	2 %
As a percentage of total revenue	30 %	32 %		

License revenue increased \$1.8 million, or 6%, in the third quarter of fiscal year 2016 as compared to the same quarter last year and increased \$0.6 million, or 1%, in the first nine months of fiscal year 2016 as compared to the same period last year. The increase in license revenue was primarily due to an increase in Data Connectivity and Integration license sales, partially offset by decreases in sales to OpenEdge customers and in Corticon license sales.

## Maintenance and Services Revenue

	Three Months Ended		Percentage Change	
(In thousands)	August 31, 2016	August 31, 2015	As Reported	Constant Currency

Edgar Filing: PROGRESS SOFTWARE CORP /MA - Form 10-Q

Maintenance	\$60,368	\$55,365	9 %	11 %
As a percentage of total revenue	59	% 59	%	
Services	8,026	7,432	8 %	8 %
As a percentage of total revenue	8	% 8	%	
Total maintenance and services revenue	\$68,394	\$62,797	9 %	10 %
As a percentage of total revenue	67	% 66	%	

23

---

Table of Contents

(In thousands)	Nine Months Ended		Percentage Change		
	August 31, 2016	August 31, 2015	As Reported	Constant Currency	
Maintenance	\$178,189	\$157,259	13 %	16 %	
As a percentage of total revenue	62 %	59 %			
Services	23,062	21,783	6 %	6 %	
As a percentage of total revenue	8 %	8 %			
Total maintenance and services revenue	\$201,251	\$179,042	12 %	14 %	
As a percentage of total revenue	70 %	68 %			

Maintenance and services revenue increased \$5.6 million in the third quarter of fiscal year 2016 as compared to the same quarter last year. Maintenance revenue increased 9% and professional services revenue increased 8% in the third quarter of fiscal year 2016 as compared to the third quarter of fiscal year 2015. Maintenance and services revenue increased \$22.2 million in the first nine months of fiscal year 2016 as compared to the same period last year.

Maintenance revenue increased 13% and professional services revenue increased 6% in the first nine months of fiscal year 2016 as compared to the same period of fiscal year 2015.

The increase in maintenance revenue is primarily due to the impact of the Telerik acquisition during the first quarter of fiscal year 2015. As a result of acquisition accounting, the acquired deferred revenue balance was significantly reduced to reflect its fair value as of the acquisition date. Therefore, the reduction of the acquisition date deferred revenue had a negative impact on revenue in the first nine months of fiscal year 2015. However, in the first nine months of fiscal year 2016 we recognized revenue related to the full value of Telerik deferred revenue that was generated during fiscal years 2015 and 2016. The increase in services revenue in the third quarter and first nine months of fiscal year 2016 was primarily due to higher software-as-a-service (SaaS) revenue generated by our Application Development and Deployment segment compared to the same period last year.

## Revenue by Region

(In thousands)	Three Months Ended		Percentage Change		
	August 31, 2016	August 31, 2015	As Reported	Constant Currency	
North America	\$58,275	\$49,810	17 %	17 %	
As a percentage of total revenue	57 %	53 %			
EMEA	\$32,719	\$30,656	7 %	10 %	
As a percentage of total revenue	32 %	32 %			
Latin America	\$4,667	\$4,621	1 %	2 %	
As a percentage of total revenue	5 %	5 %			
Asia Pacific	\$6,357	\$9,550	(33)%	(34)%	
As a percentage of total revenue	6 %	10 %			

  

(In thousands)	Nine Months Ended		Percentage Change		
	August 31, 2016	August 31, 2015	As Reported	Constant Currency	
North America	\$160,732	\$139,454	15 %	15 %	
As a percentage of total revenue	56 %	53 %			
EMEA	\$95,517	\$89,667	7 %	10 %	
As a percentage of total revenue	33 %	34 %			



Latin America	\$12,749	\$13,977	(9 )%	4 %
As a percentage of total revenue	5	% 5	%	
Asia Pacific	\$18,619	\$21,738	(14)%	(13 )%
As a percentage of total revenue	6	% 8	%	

North America increased \$21.3 million, and total revenue generated outside North America increased \$1.5 million, in the first nine months of fiscal year 2016 as compared to the same period last year. The increases in North America and EMEA were

Table of Contents

primarily due to the impact of the Telerik acquisition, which was completed during the first quarter of fiscal year 2015. As a result of acquisition accounting, the acquired deferred revenue balance was significantly reduced to reflect its fair value as of the acquisition date. Therefore, the reduction of the acquisition date deferred revenue had a negative impact on revenue in the first nine months of fiscal year 2015. However, in the first nine months of fiscal year 2016 we recognized revenue related to the full value of Telerik deferred revenue that was generated during fiscal years 2015 and 2016. The decrease in Latin America in the first nine months of 2016 compared to the same period of 2015 was due to the continuing difficult economic situation in Brazil. The decrease in Asia Pacific in the three and nine months ended August 31, 2016 is due to several large OpenEdge license deals that occurred in the third fiscal quarter of last year.

Total revenue generated in markets outside North America represented 44% of total revenue in the first nine months of fiscal year 2016 and 47% of total revenue in the same period last year. If exchange rates had remained constant in the first nine months of fiscal year 2016 as compared to the exchange rates in effect in the same period of fiscal year 2015, total revenue generated in markets outside North America would have been 45% of total revenue.

## Revenue by Segment

(In thousands)	Three Months Ended		Percentage Change	
	August 31, 2016	August 31, 2015	As Reported	Constant Currency
OpenEdge segment	\$67,534	\$73,398	(8)%	(7)%
Data Connectivity and Integration segment	14,251	8,281	72%	72%
Application Development and Deployment segment	20,233	12,958	56%	56%
Total revenue	\$102,018	\$94,637	8%	9%

  

(In thousands)	Nine Months Ended		Percentage Change	
	August 31, 2016	August 31, 2015	As Reported	Constant Currency
OpenEdge segment	\$198,595	\$214,775	(8)%	(5)%
Data Connectivity and Integration segment	30,852	22,669	36%	36%
Application Development and Deployment segment	58,170	27,392	112%	112%
Total revenue	\$287,617	\$264,836	9%	11%

Revenue in the OpenEdge segment decreased \$5.9 million, or 8%, during the third quarter of fiscal year 2016 as compared to the same quarter last year, primarily due to decreases in sales to OpenEdge customers and in Corticon license sales. Revenue in the OpenEdge segment would have decreased by 7% if exchange rates had been constant in fiscal year 2016 as compared to exchange rates in fiscal year 2015. Data Connectivity and Integration revenue increased \$6.0 million, or 72%, quarter over quarter, primarily in North America, due to higher license revenue resulting from renewals and expansions of distribution agreements with large OEM customers. Application Development and Deployment revenue increased \$7.3 million, or 56%, quarter over quarter as a result of the impact of the Telerik acquisition during the first quarter of fiscal year 2015 as described above.

Revenue in the OpenEdge segment decreased \$16.2 million, or 8%, in the first nine months of fiscal year 2016 as compared to the same period last year. The decrease is primarily due to decreases in sales to OpenEdge customers and in Corticon license sales. Revenue in the OpenEdge segment would have decreased by 5% if exchange rates had been constant in fiscal year 2016 as compared to exchange rates in fiscal year 2015. Data Connectivity and Integration revenue increased \$8.2 million, or 36%, period over period, primarily in North America, due to higher license revenue resulting from renewals and expansions of distribution agreements with large OEM customers. Application

Development and Deployment revenue increased \$30.8 million, or 112%, period over period as a result of the impact of the Telerik acquisition during the first quarter of fiscal year 2015 as described above.

Table of Contents

## Cost of Software Licenses

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Cost of software licenses	\$1,424	\$1,441	(1)%	\$4,139	\$4,526	(9)%
As a percentage of software license revenue	4	% 5	%	5	% 5	%
As a percentage of total revenue	1	% 2	%	1	% 2	%

Cost of software licenses consists primarily of costs of royalties, electronic software distribution, duplication and packaging. Cost of software licenses remained relatively flat in the third quarter of fiscal year 2016 as compared to the same quarter last year, and decreased as a percentage of software license revenue from 5% to 4%. Cost of software licenses decreased \$0.4 million, or 9%, in the first nine months of fiscal year 2016 as compared to the same period last year, and remained flat as a percentage of software license revenue at 5%. Cost of software licenses as a percentage of software license revenue varies from period to period depending upon the relative product mix.

## Cost of Maintenance and Services

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Cost of maintenance and services	\$11,825	\$9,612	23%	\$33,217	\$31,174	7%
As a percentage of maintenance and services revenue	17	% 15	%	17	% 17	%
As a percentage of total revenue	12	% 10	%	12	% 12	%

Cost of maintenance and services consists primarily of costs of providing customer support, consulting and education. Cost of maintenance and services increased \$2.2 million, or 23%, in the third quarter of fiscal year 2016 as compared to the same quarter last year, and increased as a percentage of maintenance and services revenue from 15% to 17%. Cost of maintenance and services increased \$2.0 million, or 7%, in the first nine months of fiscal year 2016 as compared to the same period last year, and remained flat as a percentage of maintenance and services revenue at 17%. The increase in cost of maintenance and services is primarily due to higher compensation-related costs as a result of an increase in headcount as compared to the same period in the prior fiscal year.

## Amortization of Acquired Intangibles

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Amortization of acquired intangibles	\$3,940	\$4,079	(3)%	\$11,818	\$12,805	(8)%
As a percentage of total revenue	4	% 4	%	4	% 5	%

Amortization of acquired intangibles included in costs of revenue primarily represents the amortization of the value assigned to technology-related intangible assets obtained in business combinations. Amortization of acquired intangibles decreased \$0.1 million, or 3%, in the third quarter of fiscal year 2016 as compared to the same quarter last year and decreased \$1.0 million, or 8%, in the first nine months of fiscal year 2016 as compared to the same period last year. The decrease was due to the completion of amortization of certain intangible assets acquired in prior years.



Table of Contents

## Gross Profit

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Gross profit	\$84,829	\$79,505	7 %	\$238,421	\$216,331	10 %
As a percentage of total revenue	83	% 84	%	83 %	81 %	%

Our gross profit increased \$5.3 million, or 7%, in the third quarter of fiscal year 2016 as compared to the same quarter last year and increased \$22.1 million, or 10%, in the first nine months of fiscal year 2016 as compared to the same period last year. Our gross profit as a percentage of total revenue decreased from 84% to 83% and increased from 81% to 83% in the third quarter and first nine months of fiscal year 2016, respectively, compared to the same periods of fiscal year 2015. The dollar increase is primarily related to the increase of maintenance revenue. As a result of acquisition accounting, the deferred revenue balance acquired from Telerik in the first quarter of fiscal year 2015 was significantly reduced to reflect its fair value as of the acquisition date, which impacted the amount of revenue recognized in the quarter and first nine months of 2015. However, we were still incurring the associated costs to fulfill the acquired deferred revenue, which were reflected in our consolidated statement of operations in the third quarter and first nine months of fiscal year 2015. As a result, our expenses as a percentage of total revenue were higher in the third quarter and first nine months of fiscal year 2015.

## Sales and Marketing

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Sales and marketing	\$29,852	\$30,004	(1 )%	\$88,648	\$92,607	(4 )%
As a percentage of total revenue	29	% 32	%	31	% 35	%

Sales and marketing expenses decreased \$0.2 million, or 1%, in the third quarter of fiscal year 2016 as compared to the same quarter last year, and decreased as a percentage of total revenue from 32% to 29%. Sales and marketing expenses decreased \$4.0 million, or 4%, in the first nine months of fiscal year 2016 as compared to the same period last year, and decreased as a percentage of total revenue from 35% to 31%. The decrease in the first nine months of fiscal year 2016 was primarily due to lower outside services costs, largely attributed to our decision to no longer outsource our renewal maintenance business, and lower marketing program costs as compared to the prior year.

## Product Development

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Product development costs	\$21,706	\$20,701	5 %	\$65,800	\$66,858	(2 )%
Capitalized product development costs	—	(279 )	(100 )%	—	(1,325 )	(100 )%
Total product development expense	\$21,706	\$20,422	6 %	\$65,800	\$65,533	— %
As a percentage of total revenue	21	% 22	%	23	% 25	%

Product development expenses increased \$1.3 million, or 6%, in the third quarter of fiscal year 2016 as compared to the same quarter last year, and decreased as a percentage of revenue from 22% to 21%. Product development expenses remained flat in the first nine months of fiscal year 2016 as compared to the same period last year, and decreased as a

percentage of revenue from 25% to 23%. The increase in product development expense during the period is primarily due to higher compensation-related costs, most significantly in stock-based compensation costs, as a result of an increase in headcount as compared to the same period in the prior fiscal year, offset by the elimination of capitalized product development costs primarily as a result of our decision to replace our internally developed cloud-based mobile application development technology with technology acquired in connection with the acquisition of Telerik.

Table of Contents

## General and Administrative

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
General and administrative	\$11,411	\$14,076	(19)%	\$36,055	\$42,065	(14)%
As a percentage of total revenue	11	% 15	%	13	% 16	%

General and administrative expenses include the costs of our finance, human resources, legal, information systems and administrative departments. General and administrative expenses decreased \$2.7 million, or 19%, in the third quarter of fiscal year 2016 as compared to the same quarter in the prior year, and decreased as a percentage of revenue from 15% to 11%. General and administrative expenses decreased \$6.0 million, or 14%, in the first nine months of fiscal year 2016 as compared to the same period in the prior year, and decreased as a percentage of revenue from 16% to 13%. The decrease was primarily due to lower compensation-related costs, most significantly in stock-based compensation costs and salaries, as a result of headcount reduction actions, which occurred in the first half and fourth quarter of fiscal year 2015.

## Amortization of Acquired Intangibles

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Amortization of acquired intangibles	\$3,186	\$3,186	—%	\$9,556	\$9,559	—%
As a percentage of total revenue	3	% 3	%	3	% 4	%

Amortization of acquired intangibles included in operating expenses primarily represents the amortization of value assigned to intangible assets obtained in business combinations other than assets identified as purchased technology. Amortization of acquired intangibles remained flat in the third quarter of fiscal year 2016 as compared to the same quarter last year as well as the first nine months of fiscal year 2016 as compared to the same period in the prior year.

## Impairment of Intangible Assets

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Impairment of intangible assets	\$5,051	\$ —	100%	\$5,051	\$ —	100%
As a percentage of total revenue	5	% —	%	2	% —	%

During the third quarter of fiscal year 2016, we evaluated the ongoing value of the intangible assets associated with the technology obtained in connection with the acquisition of Modulus. As a result of our decision to abandon the related assets due to a change in our expected ability to use the technology internally, we determined that the intangible assets were fully impaired. As a result, we incurred an impairment charge of \$5.1 million in the third quarter of fiscal year 2016.

## Restructuring Expenses

(In thousands)	Three Months Ended		Nine Months Ended	
	Percentage	Percentage	Percentage	Percentage



Edgar Filing: PROGRESS SOFTWARE CORP /MA - Form 10-Q

	August 31, 2016	August 31, 2015	Change	August 31, 2016	August 31, 2015	Percentage Change
Restructuring expenses	\$(36)	\$2,561	(101 )%	\$229	\$8,715	(97 )%
As a percentage of total revenue	—	% 3	%	—	% 3	%

Restructuring expenses recorded in the third quarter and first nine months of fiscal year 2016 relate to the restructuring activities occurring in fiscal years 2015, 2014, 2013 and 2012. See Note 11 to the condensed consolidated financial statements for additional details, including types of expenses incurred and the timing of future expenses and cash payments. See also the

Table of Contents

Liquidity and Capital Resources section of this Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations.

## Acquisition-Related Expenses

(In thousands)	Three Months Ended			Nine Months Ended		
	August 2016	August 31, 2015	Percentage Change	August 2016	August 31, 2015	Percentage Change
Acquisition-related expenses	\$53	\$ 662	(92 )%	\$449	\$3,180	(86 )%
As a percentage of total revenue	— %	1 %		— %	1 %	

Acquisition-related costs are expensed as incurred and include those costs incurred as a result of a business combination. These costs consist of professional service fees, including third-party legal and valuation-related fees, as well as retention fees, including earn-out payments treated as compensation expense. Acquisition-related expenses in the third quarter and first nine months of fiscal year 2016 were minimal. Acquisition-related expenses in the third quarter and first nine months of fiscal year 2015 resulted primarily from expenses related to the Telerik acquisition completed in the first quarter of fiscal year 2015. See Note 6 to the condensed consolidated financial statements for additional details.

## Income (Loss) From Operations

(In thousands)	Three Months Ended			Nine Months Ended		
	August 2016	August 31, 2015	Percentage Change	August 2016	August 31, 2015	Percentage Change
Income (loss) from operations	\$13,606	\$ 8,594	58 %	\$32,655	\$(5,328)	713 %
As a percentage of total revenue	13 %	9 %		11 %	(3 )%	

Income from operations increased \$5.0 million, or 58%, in the third quarter of fiscal year 2016 as compared to the same quarter last year. Income from operations increased \$38.0 million, or 713%, in the first nine months of fiscal year 2016 as compared to the same period last year. As discussed above, the increase was primarily the result of higher revenue during the third quarter and first nine months of fiscal year 2016 compared to the same periods last year, as well as lower expenses during the first nine months of fiscal year 2016 compared to the same period last year.

## Income (Loss) from Operations by Segment

(In thousands)	Three Months Ended			Nine Months Ended		
	August 2016	August 31, 2015	Percentage Change	August 2016	August 31, 2015	Percentage Change
OpenEdge segment	\$49,354	\$ 54,848	(10 )%	\$145,056	\$158,246	(8 )%
Data Connectivity and Integration segment	11,423	5,101	124 %	21,989	13,106	68 %
Application Development and Deployment segment	9,212	3,025	205 %	28,615	(2,777 )	1,130 %
Other unallocated expenses (1)	(56,383 )	(54,380 )	4 %	(163,005 )	(173,903 )	(6 )%
Income (loss) from operations	\$13,606	\$ 8,594	58 %	\$32,655	\$(5,328 )	713 %

(1) Note that the following expenses are not allocated to our segments as we manage and report our business in these functional areas on a consolidated basis only: product development, corporate marketing, general and administration, amortization and impairment of acquired intangibles, stock-based compensation, restructuring, and acquisition-related

expenses.

29

---

Table of Contents

## Other (Expense) Income

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Interest expense	\$(1,174)	\$(987 )	19 %	\$(3,244)	\$(2,808)	16 %
Interest income and other, net	260	450	(42 )%	686	1,153	(41 )%
Foreign currency (loss) gain, net	(374 )	(628 )	(40 )%	(1,916 )	397	(583 )%
Total other (expense) income, net	\$(1,288)	\$(1,165)	11 %	\$(4,474)	\$(1,258)	256 %
As a percentage of total revenue	(1 )%	(1 )%		(2 )%	— %	

Other (expense) income, net increased \$0.1 million in the third quarter of fiscal year 2016 as compared to the same quarter last year primarily due to a decrease to interest income. Other (expense) income, net increased \$3.2 million in the first nine months of fiscal year 2016 as compared to the same period last year primarily due to the foreign currency loss in the first nine months of fiscal year 2016 compared to the foreign currency gain in the first nine months of fiscal year 2015. The change in foreign currency gains/losses is a result of movements in exchange rates and the impact in the first, second and third quarters of fiscal year 2016 on our intercompany receivables and payables denominated in currencies other than local currencies.

## Provision (Benefit) for Income Taxes

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Provision (benefit) for income taxes	\$4,742	\$11,555	(59 )%	\$10,114	\$(7,256)	(239 )%
As a percentage of total revenue	5 %	12 %		4 %	(3 )%	

Our effective income tax rate was 38% in the third quarter of fiscal year 2016 compared to 156% in the third quarter of fiscal year 2015, and 36% in the first nine months of fiscal year 2016 compared to 110% in the same period last year. The decrease in the effective rate is primarily due to the jurisdictional mix of profits as a result of the acquisition of Telerik, where substantial losses were incurred in Bulgaria in fiscal year 2015 and tax effected at a 10% statutory rate and other jurisdictions' earnings, primarily in the United States, were taxed at higher rates. The loss in Bulgaria in fiscal 2015 was primarily due to amortization expense and other purchase accounting adjustments related to the Telerik acquisition. Deferred tax liabilities have been established in purchase accounting for the tax effect of the Telerik amortization expense and other purchase accounting adjustments.

## Net Income (Loss)

(In thousands)	Three Months Ended			Nine Months Ended		
	August 31, 2016	August 31, 2015	Percentage Change	August 31, 2016	August 31, 2015	Percentage Change
Net income (loss)	\$7,576	\$(4,126)	284 %	\$18,067	\$670	2,597 %
As a percentage of total revenue	7 %	(4 )%		6 %	— %	

Table of Contents

## Liquidity and Capital Resources

## Cash, Cash Equivalents and Short-Term Investments

(In thousands)	August 31, November	
	2016	30, 2015
Cash and cash equivalents	\$ 188,084	\$ 212,379
Short-term investments	44,600	28,900
Total cash, cash equivalents and short-term investments	\$ 232,684	\$ 241,279

The decrease in cash, cash equivalents and short-term investments of \$8.6 million from the end of fiscal year 2015 was primarily due to cash outflows for repurchases of common stock of \$71.5 million and payments of debt principal in the amount of \$7.5 million, partially offset by cash inflows from operations of \$68.9 million. Except as described below, there are no limitations on our ability to access our cash, cash equivalents and short-term investments.

As of August 31, 2016, \$30.8 million of our cash, cash equivalents and short-term investments was held by our foreign subsidiaries. This amount is considered to be permanently reinvested; as such, it is not available to fund our domestic operations. If we were to repatriate these funds, they would be subject to taxation in the U.S., but would be offset by foreign tax credits. We do not believe this has a material adverse impact on our liquidity.

## Share Repurchase Program

We repurchased and retired 0.4 million shares of our common stock for \$11.5 million in the three months ended August 31, 2016 and 2.8 million shares for \$71.5 million in the nine months ended August 31, 2016. We did not repurchase shares of our common stock during the three months ended August 31, 2015 and in the nine months ended August 31, 2015, we repurchased and retired 1.3 million shares for \$32.9 million. The shares were repurchased in both periods as part of our Board of Directors authorized share repurchase program.

In March 2016, our Board of Directors authorized a new \$100.0 million share repurchase program, which increased the total authorization to \$202.8 million. As of August 31, 2016, there is \$143.0 million remaining under this current authorization.

## Credit Facility

On December 2, 2014, we entered into a credit agreement (the Credit Agreement) with each of the lenders party thereto (the Lenders), JPMorgan Chase Bank, N.A., as Administrative Agent, Wells Fargo Bank, N.A. and Citizens Bank, N.A., as Syndication Agents, Bank of America, N.A., Citibank, N.A. and Silicon Valley Bank, as Documentation Agents, and J.P. Morgan Securities LLC, as Sole Bookrunner and Sole Lead Arranger, providing for a \$150 million secured term loan and a \$150 million secured revolving credit facility, which may be made available in U.S. Dollars and certain other currencies. The revolving credit facility may be increased by up to an additional \$75 million if the existing or additional lenders are willing to make such increased commitments.

We borrowed the \$150 million term loan included in the Credit Agreement to partially fund our acquisition of Telerik. The revolving credit facility has sublimits for swing line loans up to \$25.0 million and for the issuance of standby letters of credit in a face amount up to \$25.0 million. We expect to use the revolving credit facility for general corporate purposes, including potential acquisitions of other businesses, and may also use it for working capital.

Interest rates for the term loan and revolving credit facility are determined based on an index selected at our option and would range from 1.50% to 2.25% above the Eurodollar rate for Eurodollar-based borrowings or would range

from 0.50% to 1.25% above the defined base rate for base rate borrowings, in each case based upon our leverage ratio. Additionally, we may borrow certain foreign currencies at rates set in the same range above the respective London interbank offered interest rates (LIBOR) for those currencies, based on our leverage ratio. A quarterly commitment fee on the undrawn portion of the revolving credit facility is required, ranging from 0.25% to 0.40% per annum, based upon our leverage ratio. The interest rate of the credit facility as of August 31, 2016 was 2.25%.

The credit facility matures on December 2, 2019, when all amounts outstanding will be due and payable in full. The revolving credit facility does not require amortization of principal. The outstanding balance of the \$150 million term loan as of August 31, 2016 was \$136.9 million, with \$13.1 million due in the next 12 months. The term loan requires repayment of principal at

Table of Contents

the end of each fiscal quarter, beginning with the fiscal quarter ended February 28, 2015. The first eight payments are in the principal amount of \$1.9 million each, the following eight payments are in the principal amount of \$3.8 million each, the following three payments are in the principal amount of \$5.6 million each, and the last payment is of the remaining principal amount. The term loan may be prepaid before maturity in whole or in part at our option without penalty or premium. As of August 31, 2016, the carrying value of the term loan approximates the fair value, based on Level 2 inputs (observable market prices in less than active markets), as the interest rate is variable over the selected interest period and is similar to current rates at which we can borrow funds.

Revolving loans may be borrowed, repaid and reborrowed until December 2, 2019, at which time all amounts outstanding must be repaid. Accrued interest on the loans is payable quarterly in arrears with respect to base rate loans and at the end of each interest rate period (or at each three month interval in the case of loans with interest periods greater than three months) with respect to LIBOR rate loans. We may prepay the loans or terminate or reduce the commitments in whole or in part at any time, without premium or penalty, subject to certain conditions and reimbursement of certain costs in the case of LIBOR rate loans. As of August 31, 2016, there were no amounts outstanding under the revolving line and \$0.5 million of letters of credit.

We are the sole borrower under the credit facility. Our obligations under the Credit Agreement are guaranteed by each of our material domestic subsidiaries and are secured by substantially all of our assets and such material domestic subsidiaries, as well as 100% of the capital stock of our domestic subsidiaries and 65% of the capital stock of our first-tier foreign subsidiaries, in each case, subject to certain exceptions as described in the Credit Agreement. Future material domestic subsidiaries will be required to guaranty our obligations under the Credit Agreement, and to grant security interests in substantially all of their assets to secure such obligations. The Credit Agreement generally prohibits, with certain exceptions, any other liens on our assets, subject to certain exceptions as described in the Credit Agreement.

The credit facility contains customary affirmative and negative covenants, including covenants that limit or restrict our ability to, among other things, grant liens, make investments, make acquisitions, incur indebtedness, merge or consolidate, dispose of assets, pay dividends or make distributions, repurchase stock, change the nature of the business, enter into certain transactions with affiliates and enter into burdensome agreements, in each case subject to customary exceptions for a credit facility of this size and type. We are also required to maintain compliance with a consolidated fixed charge coverage ratio, a consolidated total leverage ratio and a consolidated senior secured leverage ratio. We are in compliance with these covenants as of August 31, 2016.

## Cash Flows from Operating Activities

(In thousands)	Nine Months Ended	
	August 31, 2016	August 31, 2015
Net income	\$18,067	\$ 670
Non-cash reconciling items included in net income	52,585	30,622
Changes in operating assets and liabilities	(1,742 )	45,896
Net cash flows from operating activities	\$68,910	\$ 77,188

The decrease in cash generated from operations in the first nine months of fiscal year 2016 as compared to the first nine months of fiscal year 2015 was primarily due to changes in operating assets and liabilities. Cash flows in the first nine months of fiscal year 2015 were particularly strong due to improvements in working capital driven largely by a shorter collection cycle of Telerik's receivables. In addition, compared to the prior year, the first nine months of fiscal year 2016 was impacted by higher tax payments, the payment of higher variable compensation due to the increase in headcount resulting from the acquisition of Telerik, and the payment of retention bonuses also applicable to the

acquisition of Telerik.

Our gross accounts receivable as of August 31, 2016 decreased by \$11.3 million from the end of fiscal year 2015, which is primarily due to greater collections than billings during the period. Days sales outstanding (DSO) in accounts receivable was 49 days compared to 54 days in the fiscal third quarter of 2015 due to improved collections performance. In addition, our total deferred revenue as of August 31, 2016 increased by \$3.8 million from the end of fiscal year 2015.



Table of Contents

## Cash Flows from Investing Activities

(In thousands)	Nine Months Ended	
	August 31, 2016	August 31, 2015
Net investment activity	\$(16,586)	\$(9,632 )
Purchases of property and equipment	(3,747 )	(6,079 )
Capitalized software development costs	—	(1,661 )
Payments for acquisitions, net of cash acquired	—	(246,275 )
Proceeds from divestitures, net	—	4,500
Net cash flows used in investing activities	\$(20,333)	\$(259,147)

Net cash outflows and inflows of our net investment activity are generally a result of the timing of our purchases and maturities of securities, which are classified as cash equivalents or short-term securities. In addition, we purchased \$3.7 million of property and equipment in the first nine months of fiscal year 2016, as compared to \$6.1 million in the first nine months of fiscal year 2015. Most significantly, however, we acquired Telerik during the first quarter of fiscal year 2015 for a net cash amount of \$246.3 million and did not complete any acquisitions during the first nine months of fiscal year 2016.

## Cash Flows from Financing Activities

(In thousands)	Nine Months Ended	
	August 31, 2016	August 31, 2015
Proceeds from stock-based compensation plans	\$8,166	\$10,459
Repurchases of common stock	(71,507 )	(32,868 )
Net proceeds from the issuance of debt	(7,500 )	142,588
Other financing activities	(2,446 )	(1,952 )
Net cash flows (used in) from financing activities	\$(73,287)	\$118,227

During the first nine months of fiscal year 2016, we received \$8.2 million from the exercise of stock options and the issuance of shares under our employee stock purchase plan as compared to \$10.5 million in the first nine months of fiscal year 2015. In addition, in the first nine months of fiscal year 2016, we repurchased \$71.5 million of our common stock under our share repurchase plan compared to \$32.9 million in the same period of the prior year. Most significantly, during the first nine months of fiscal year 2015, we received net proceeds of \$142.6 million from the issuance of debt, whereas we made principal payments on this debt in the amount of \$7.5 million during the first nine months of fiscal year 2016.

## Indemnification Obligations

We include standard intellectual property indemnification provisions in our licensing agreements in the ordinary course of business. Pursuant to our product license agreements, we will indemnify, hold harmless, and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally business partners or customers, in connection with certain patent, copyright or other intellectual property infringement claims by third parties with respect to our products. Other agreements with our customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by us or our subcontractors. Historically, our costs to defend lawsuits or settle claims relating to such indemnity agreements have been insignificant. Accordingly, the estimated fair value of these indemnification provisions is immaterial.

## Liquidity Outlook

We believe that existing cash balances, together with funds generated from operations and amounts available under our credit facility, will be sufficient to finance our operations and meet our foreseeable cash requirements through at least the next twelve months. We do not contemplate a need for any foreign repatriation of the earnings which are deemed permanently reinvested. Our foreseeable cash needs include our newly announced quarterly cash dividend to Progress shareholders, as well as our planned capital expenditures and share repurchases, lease commitments, restructuring obligations and other long-term obligations.

Table of Contents

## Revenue Backlog

(In thousands)	August 31, 2016	August 31, 2015
Deferred revenue, primarily related to unexpired	\$ 137,883	\$ 130,996
maintenance and support contracts		
Multi-year licensing arrangements <sup>(1)</sup>	31,101	22,791
Total revenue backlog	\$ 168,984	\$ 153,787

Our backlog of orders not included on the balance sheet is not subject to our normal accounting controls for information that is either reported in or derived from our basic financial statements. Note that approximately \$29.4 (1) million of the multi-year licensing arrangements as of August 31, 2016 relate to OEM arrangements in our Data Connectivity and Integration business segment, while the remaining amount relates to arrangements in our OpenEdge business segment.

We typically fulfill most of our software license orders within 30 days of acceptance of a purchase order. Assuming all other revenue recognition criteria have been met, we recognize software license revenue upon shipment of the product, or if delivered electronically, when the customer has the right to access the software. Because there are many elements governing when revenue is recognized, including when orders are shipped, credit approval obtained, completion of internal control processes over revenue recognition and other factors, management has some control in determining the period in which certain revenue is recognized. In addition, there is no industry standard for the definition of backlog and there may be an element of estimation in determining the amount. As such, direct comparisons with other companies may be difficult or potentially misleading.

## Legal and Other Regulatory Matters

See discussion regarding legal and other regulatory matters in Part II, Item 1. Legal Proceedings.

## Off-Balance Sheet Arrangements

Our only significant off-balance sheet commitments relate to operating lease obligations. Future annual minimum rental lease payments are detailed in Note 10 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015. We have no “off-balance sheet arrangements” within the meaning of Item 303(a)(4) of Regulation S-K.

## Contractual Obligations

There have been no material changes to our contractual obligations disclosed in tabular format in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015.

## Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-15, Classification of Certain Cash Receipts and Cash Payments (ASU 2016-15). ASU 2016-15 is intended to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows

and to eliminate the diversity in practice related to such classifications. The guidance in ASU 2016-15 is required for annual reporting periods beginning after December 15, 2017, with early adoption permitted. We are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated statement of cash flows.

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). ASU 2016-09 is intended to simplify various aspects of the accounting for employee share-based payment transactions, including accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The guidance in ASU 2016-09 is required for annual reporting periods beginning after December 15, 2016, with early adoption permitted. We are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated financial position and results of operations.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (ASU 2016-02), which requires lessees to record most leases on their balance sheets, recognizing a lease liability for the obligation to make lease payments and a right-to-use asset for the right to use the underlying asset for the lease term. The guidance in ASU 2016-02 is required for annual

## Table of Contents

reporting periods beginning after December 15, 2018, with early adoption permitted. We currently expect that most of our operating lease commitments will be subject to the update and recognized as operating lease liabilities and right-of-use assets upon adoption. However, we are currently evaluating the effect that implementation of this update will have upon adoption on our consolidated financial position and results of operations.

In April 2015, the FASB issued Accounting Standards Update No. 2015-03, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03). ASU 2015-03 requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability, consistent with the presentation of a debt discount. The guidance in ASU 2015-03 is required for annual reporting periods beginning after December 15, 2015, including interim periods within the reporting period. Early adoption is permitted for financial statements that have not been previously issued. We estimate that the impact on our consolidated balance sheets will be a reclassification of up to \$1.1 million from other assets to long-term debt as of December 1, 2016.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09). ASU 2014-09 outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This new guidance is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. Early adoption is not permitted. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance. In July 2015, the FASB voted to defer the effective date of this ASU by one year for reporting periods beginning after December 15, 2017, with early adoption permitted as of the original effective date. As a result, the new effective date for the Company will be December 1, 2018. This update will impact the timing and amounts of revenue recognized. Management is currently assessing the impact the adoption of this ASU will have on the Company's consolidated financial statements.

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

During the third quarter of fiscal year 2016, there were no significant changes to our quantitative and qualitative disclosures about market risk. Please refer to Part II, Item 7A. Quantitative and Qualitative Disclosures about Market Risk included in our Annual Report on Form 10-K for our fiscal year ended November 30, 2015 for a more complete discussion of the market risks we encounter.

### Item 4. Controls and Procedures

#### (a) Evaluation of disclosure controls and procedures

Our management maintains disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended (the "Exchange Act") that are designed to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively), as appropriate, to allow for timely decisions regarding required disclosure.

Our management, including the Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective to ensure that the information required to be disclosed in the reports filed or submitted by us under the Securities Exchange Act of 1934 was recorded, processed, summarized and reported within the requisite

time periods and that such information was accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting

Our management, including our Chief Executive Officer and Chief Financial Officer, evaluated our “internal control over financial reporting” as defined in Exchange Act Rule 13a-15(f) to determine whether any changes in our internal control over financial reporting occurred during the fiscal quarter ended August 31, 2016 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on that evaluation, there were no changes in our internal control over financial reporting during the fiscal quarter ended August 31, 2016 that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these legal matters will have a material effect on our financial position, results of operations or cash flows.

Item 1A. Risk Factors

We operate in a rapidly changing environment that involves certain risks and uncertainties, some of which are beyond our control. There have been no material changes in our assessment of our risk factors from those set forth in our Annual Report on Form 10-K for the fiscal year ended November 30, 2015, except for the addition of a risk factor relating to the Referendum of the United Kingdom's Membership of the European Union. For convenience, all of our risk factors are included below. The risks discussed below could materially affect our business, financial condition and future results. The risks described below are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be insignificant also may materially and adversely affect our business, financial condition or operating results in the future.

Our revenue and quarterly results may fluctuate, which could adversely affect our stock price. We have experienced, and may in the future experience, significant fluctuations in our quarterly operating results that may be caused by many factors. These factors include:

- changes in demand for our products;
- introduction, enhancement or announcement of products by us or our competitors;
- market acceptance of our new products;
- the growth rates of certain market segments in which we compete;
- size and timing of significant orders;
- a high percentage of our revenue is generated in the third month of each fiscal quarter and any failure to receive, complete or process orders at the end of any quarter could cause us to fall short of our revenue targets;
- budgeting cycles of customers;
- mix of distribution channels;
- mix of products and services sold;
  - mix of international and North American revenues;
- fluctuations in currency exchange rates;
- changes in the level of operating expenses;
- the amount of our stock-based compensation;
- changes in management;
- restructuring programs;
- changes in our sales force;
- completion or announcement of acquisitions by us or our competitors;
- customer order deferrals in anticipation of new products announced by us or our competitors; and
- general economic conditions in regions in which we conduct business.

Revenue forecasting is uncertain, and the failure to meet our forecasts could result in a decline in our stock price. Our revenues, particularly new software license revenues, are difficult to forecast. We use a pipeline system to forecast revenues and trends in our business. Our pipeline estimates may prove to be unreliable either in a particular quarter or

over a longer period of time, in part because the conversion rate of the pipeline into contracts can be difficult to estimate and requires management judgment. A variation in the conversion rate could cause us to plan or budget incorrectly and materially adversely impact our business or our planned results of operations. Furthermore, most of our expenses are relatively fixed, including costs of personnel and facilities, and are not easily reduced. Thus, an unexpected reduction in our revenue, or failure to achieve the anticipated rate of growth, would have a material adverse effect on our profitability. If our operating results do not meet our publicly stated guidance or the expectations of investors, our stock price may decline.

The addition of a subscription model to augment our traditional perpetual licensing model may negatively impact our license growth in the near term. Under a subscription model, downturns or upturns in sales may not be immediately reflected in our results of operations. Subscription pricing allows customers to use our products at a lower initial cost when compared to the sale of a perpetual license. Although the subscription model is designed to increase the number of customers who purchase our products and services and create a recurring revenue stream that is more predictable, it creates certain risks related to the timing of revenue recognition and reduced cash flows. A decline in new or renewed subscriptions in any period may not be



## Table of Contents

immediately reflected in our results for that period, but may result in a decline in our revenue in future quarters. If we were to experience significant downturns in subscription sales and renewal rates, our results of operations might not reflect such downturns until future periods. Further, any increases in sales under our subscription sales model could result in decreased revenues over the short term if they are offset by a decline in sales from perpetual license customers.

We recognize a substantial portion of our revenue from sales made through third parties, including our application partners, distributors/resellers, and OEMs, and adverse developments in the businesses of these third parties or in our relationships with them could harm our revenues and results of operations. Our future results depend upon our continued successful distribution of our products through our application partner, distributor/reseller, and OEM channels. The activities of these third parties are not within our direct control. Our failure to manage our relationships with these third parties effectively could impair the success of our sales, marketing and support activities. A reduction in the sales efforts, technical capabilities or financial viability of these parties, a misalignment of interest between us and them, or a termination of our relationship with a major application partner, distributor/reseller, or OEM could have a negative effect on our sales and financial results. Any adverse effect on the application partners', distributors'/resellers', or OEMs' businesses related to competition, pricing and other factors could also have a material adverse effect on our business, financial condition and operating results.

Weakness in the U.S. and international economies may result in fewer sales of our products and may otherwise harm our business. We are subject to the risks arising from adverse changes in global economic conditions, especially those in the U.S., Europe and Latin America. The past five years have been characterized by weak global economic conditions, tightening of credit markets and instability in the financial markets. If these conditions continue or worsen, customers may delay, reduce or forego technology purchases, both directly and through our application partners and OEMs. This could result in reductions in sales of our products, longer sales cycles, slower adoption of new technologies and increased price competition. Further, deteriorating economic conditions could adversely affect our customers and their ability to pay amounts owed to us. Any of these events would likely harm our business, results of operations, financial condition or cash flows.

Our international operations expose us to additional risks, and changes in global economic and political conditions could adversely affect our international operations, our revenue and our net income. Approximately 45% of our total revenue is generated from sales outside North America. Political and/or financial instability, oil price shocks and armed conflict in various regions of the world can lead to economic uncertainty and may adversely impact our business. If customers' buying patterns, decision-making processes, timing of expected deliveries and timing of new projects unfavorably change due to economic or political conditions, there would be a material adverse effect on our business, financial condition and operating results.

Other potential risks inherent in our international business include:

- longer payment cycles;
- credit risk and higher levels of payment fraud;
- greater difficulties in accounts receivable collection;
- varying regulatory requirements;
- compliance with international and local trade, labor and export control laws;
- compliance with U.S. laws such as the Foreign Corrupt Practices Act, and local laws prohibiting bribery and corrupt payments to government officials;
- restrictions on the transfer of funds;
- difficulties in developing, staffing, and simultaneously managing a large number of varying foreign operations as a result of distance, language, and cultural differences;
- reduced or minimal protection of intellectual property rights in some countries;

laws and business practices that favor local competitors or prohibit foreign ownership of certain businesses;  
seasonal reductions in business activity during the summer months in Europe and certain other parts of the world;  
economic instability in emerging markets; and  
potentially adverse tax consequences.

Any one or more of these factors could have a material adverse effect on our international operations, and, consequently, on our business, financial condition and operating results.

Risk Relating to the Referendum of the United Kingdom's Membership of the European Union. The announcement of the Referendum of the United Kingdom's (or the U.K.) Membership of the European Union (E.U.) (referred to as Brexit), advising for the exit of the United Kingdom from the European Union, has resulted in significant volatility in global stock markets and currency exchange rate fluctuations that resulted in the strengthening of the U.S. dollar against foreign currencies in which we conduct business. As described elsewhere in this 10-Q, we translate revenue denominated in foreign currency into U.S. dollars for our financial statements. During periods of a strengthening dollar, our reported international revenue is reduced because

## Table of Contents

foreign currencies translate into fewer U.S. dollars. The announcement of Brexit may also create global economic uncertainty, which may cause our customers to closely monitor their costs and reduce their spending budget on our products and services.

If the Referendum is passed into law, negotiations would commence to determine the future terms of the U.K.'s relationship with the E.U., including the terms of trade between the U.K. and the E.U. The effects of Brexit will depend on any agreements the U.K. makes to retain access to E.U. markets either during a transitional period or more permanently. The measures could potentially disrupt the markets we serve and may cause us to lose customers, and employees. In addition, Brexit could lead to legal uncertainty and potentially divergent national laws and regulations as the U.K. determines which E.U. laws to replace or replicate.

Any of these effects of Brexit, among others, could materially adversely affect our business, results of operations and financial condition.

Fluctuations in foreign currency exchange rates could have an adverse impact on our financial condition and results of operations. Changes in the value of foreign currencies relative to the U.S. dollar has adversely affected our results of operations and financial position. For example, during the second half of 2014 and early 2015, the value of the U.S. dollar strengthened in comparison to certain foreign currencies, including in Europe, Brazil and Australia. As approximately one-third of our revenue is denominated in foreign currency, our fiscal year 2015 and fiscal first, second, and third quarters of 2016 revenue results were impacted, and we expect will continue to be impacted, by fluctuations in foreign currency exchange rates.

We seek to reduce our exposure to fluctuations in exchange rates by entering into foreign exchange forward contracts to hedge certain actual and forecasted transactions of selected currencies (mainly in Europe, Brazil, India and Australia). Our currency hedging transactions may not be effective in reducing any adverse impact of fluctuations in foreign currency exchange rates. Further, the imposition of exchange or price controls or other restrictions on the conversion of foreign currencies could have a material adverse effect on our business.

Technology and customer requirements evolve rapidly in our industry, and if we do not continue to develop new products and enhance our existing products in response to these changes, our business could be harmed. Ongoing enhancements to our product sets will be required to enable us to maintain our competitive position. We may not be successful in developing and marketing enhancements to our products on a timely basis, and any enhancements we develop may not adequately address the changing needs of the marketplace. Overlaying the risks associated with our existing products and enhancements are ongoing technological developments and rapid changes in customer requirements. Our future success will depend upon our ability to develop and introduce in a timely manner new products that take advantage of technological advances and respond to new customer requirements. We may not be successful in developing new products incorporating new technology on a timely basis, and any new products may not adequately address the changing needs of the marketplace. Failure to develop new products and product enhancements that meet market needs in a timely manner could have a material adverse effect on our business, financial condition and operating results.

We are substantially dependent on our Progress OpenEdge products. We derive a significant portion of our revenue from software license and maintenance revenue attributable to our Progress OpenEdge product set. Accordingly, our future results depend on continued market acceptance of OpenEdge. If new technologies emerge that are superior to, or more responsive to customer requirements, than OpenEdge such that we are unable to maintain OpenEdge's competitive position within its marketplace, this will have a material adverse effect on our business, financial condition and operating results.

The increased emphasis on a cloud strategy may give rise to risks that could harm our business. We are devoting significant resources to the development of cloud-based technologies and service offerings where we have a limited operating history. Our cloud strategy requires continued investment in product development and cloud operations as well as a change in the way we price and deliver our products. Many of our competitors may have advantages over us due to their larger presence, larger developer network, deeper experience in the cloud-based computing market, and greater sales and marketing resources. It is uncertain whether these strategies will prove successful or whether we will be able to develop the infrastructure and business models more quickly than our competitors. Our cloud strategy may give rise to a number of risks, including the following:

- if new or current customers desire only perpetual licenses, we may not be successful in selling subscriptions; although we intend to support our perpetual license business, the increased emphasis on a cloud strategy may raise concerns among our installed customer base;
- we may be unsuccessful in achieving our target pricing;
- our revenues might decline over the short or long term as a result of this strategy;
- our relationships with existing partners that resell perpetual licenses may be damaged; and
- we may incur costs at a higher than forecasted rate as we enhance and expand our cloud operations.

Table of Contents

We may make additional acquisitions or investments in new businesses, products or technologies that involve additional risks, which could disrupt our business or harm our financial condition, results of operations or cash flows. We may make acquisitions of businesses or investments in companies that offer complementary products, services and technologies. Any acquisitions that we do complete involve a number of risks, including the risks of assimilating the operations and personnel of acquired companies, realizing the value of the acquired assets relative to the price paid, distraction of management from our ongoing businesses and potential product disruptions associated with the sale of the acquired company's products. In addition, an acquisition may not further our business strategy as we expected, we may not integrate an acquired company or technology as successfully as we expected or we may overpay for, or otherwise not realize the expected return on, our investments, which could adversely affect our business or operating results and potentially cause impairment to assets that we recorded as a part of an acquisition including intangible assets and goodwill. These factors could have a material adverse effect on our business, financial condition, operating results and cash flows. The consideration we pay for any future acquisitions could include our stock. As a result, future acquisitions could cause dilution to existing shareholders and to earnings per share.

If our goodwill or amortizable intangible assets become impaired we may be required to record a significant charge to earnings. We acquire other companies and intangible assets and may not realize all the economic benefit from those acquisitions, which could cause an impairment of goodwill or intangibles. We review our amortizable intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. We test goodwill for impairment at least annually. Factors that may be a change in circumstances, indicating that the carrying value of our goodwill or amortizable intangible assets may not be recoverable, include a decline in our stock price and market capitalization, reduced future cash flow estimates, and slower growth rates in industry segments in which we participate. We may be required to record a significant charge in our consolidated financial statements during the period in which any impairment of our goodwill or amortizable intangible assets is determined, negatively affecting our results of operations.

We are investing significantly in development, sales and marketing resources in furtherance of our cloud-based offerings, and we may experience decreased profitability or losses if our cloud-based offerings do not gain market acceptance. We are increasing our investment in development, sales and marketing resources in furtherance of our cloud-based offerings. These investments have resulted in increased costs. If demand for our cloud-based offerings does not materialize or increase, we could experience decreased profitability or losses as a result of these increased costs.

The segments of the software industry in which we participate are intensely competitive, and our inability to compete effectively could harm our business. We experience significant competition from a variety of sources with respect to the marketing and distribution of our products. Many of our competitors have greater financial, marketing or technical resources than we do and may be able to adapt more quickly to new or emerging technologies and changes in customer requirements or to devote greater resources to the promotion and sale of their products than we can. Increased competition could make it more difficult for us to maintain our market presence or lead to downward pricing pressure.

In addition, the marketplace for new products is intensely competitive and characterized by low barriers to entry. For example, an increase in market acceptance of open source software may cause downward pricing pressures. As a result, new competitors possessing technological, marketing or other competitive advantages may emerge and rapidly acquire market share. In addition, current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third parties, thereby increasing their ability to deliver products that better address the needs of our prospective customers. Current and potential competitors may also be more successful than we are in having their products or technologies widely accepted. We may be unable to compete successfully against current and future competitors, and our failure to do so could have a material adverse effect on

our business, prospects, financial condition and operating results.

We rely on the experience and expertise of our executives and skilled employees, and must continue to attract and retain qualified executive, technical, marketing and managerial personnel in order to succeed. Our future success will depend in a large part upon our ability to attract and retain highly skilled executive, technical, managerial, sales and marketing personnel. There is significant competition for such personnel in the software industry. We may not continue to be successful in attracting and retaining the personnel we require to develop new and enhanced products and to continue to grow and operate profitably.

The loss of technology licensed from third parties could adversely affect our ability to deliver our products. We utilize certain technology that we license from third parties, including software that is integrated with internally developed software and used in our products to perform key functions. This technology, or functionally similar technology, may not continue to be available on commercially reasonable terms in the future, or at all. The loss of any significant third-party technology license could cause delays in our ability to deliver our products or services until equivalent technology is developed internally or equivalent third-party technology, if available, is identified, licensed and integrated.

Table of Contents

Privacy concerns and laws, evolving regulation of cloud computing, cross-border data transfer restrictions and other domestic or foreign regulations may limit the use and adoption of our products and solutions and adversely affect our business. Regulation related to the provision of services on the Internet is increasing, as federal, state and foreign governments continue to adopt new laws and regulations addressing data privacy and the collection, processing, storage and use of personal information. In some cases, foreign data privacy laws and regulations, such as the European Union's Data Protection Directive, and the country-specific laws and regulations that implement that directive, also govern the processing of personal information. Further, laws are increasingly aimed at the use of personal information for marketing purposes, such as the European Union's e-Privacy Directive, and the country-specific regulations that implement that directive. Such laws and regulations are subject to new and differing interpretations and may be inconsistent among jurisdictions. These and other requirements could reduce demand for our products and solutions or restrict our ability to store and process data or, in some cases, impact our ability to offer our products and solutions in certain locations or our customers' ability to deploy our solutions globally.

For example, the European Court of Justice recently invalidated the U.S.-EU Safe Harbor framework that had been in place since 2000, which allowed companies to meet certain European legal requirements for the transfer of personal data from the European Economic Area to the United States. While other adequate legal mechanisms to lawfully transfer such data remain, the invalidation of the U.S.-EU Safe Harbor framework may result in different European data protection regulators applying differing standards for the transfer of personal data, which could result in increased regulation, cost of compliance and limitations on data transfer for us and our customers. The costs of compliance with and other burdens imposed by laws, regulations and standards may limit the use and adoption of our services, reduce overall demand for our services, lead to significant fines, penalties or liabilities for noncompliance, or slow the pace at which we close sales transactions, any of which could harm our business.

Furthermore, concerns regarding data privacy may cause our customers' customers to resist providing the data necessary to allow our customers to use our products and solutions effectively. Even the perception that the privacy of personal information is not satisfactorily protected or does not meet regulatory requirements could inhibit sales of our products or solutions, and could limit adoption of our cloud-based solutions.

If our products contain software defects or security flaws, it could harm our revenues and expose us to litigation. Our products, despite extensive testing and quality control, may contain defects or security flaws, especially when we first introduce them or when new versions are released. We may need to issue corrective releases of our software products to fix any defects or errors. The detection and correction of any security flaws can be time consuming and costly. Errors in our software products could affect the ability of our products to work with other hardware or software products, delay the development or release of new products or new versions of products, adversely affect market acceptance of our products and expose us to potential litigation. If we experience errors or delays in releasing new products or new versions of products, such errors or delays could have a material adverse effect on our revenue.

We could incur substantial cost in protecting our proprietary software technology or if we fail to protect our technology, which would harm our business. We rely principally on a combination of contract provisions and copyright, trademark, patent and trade secret laws to protect our proprietary technology. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary. Policing unauthorized use of our products is difficult. Litigation may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. This litigation could result in substantial costs and diversion of resources, whether or not we ultimately prevail on the merits. The steps we take to protect our proprietary rights may be inadequate to prevent misappropriation of our technology; moreover, others could independently develop similar technology.

We could be subject to claims that we infringe intellectual property rights of others, which could harm our business, financial condition, results of operations or cash flows. Third parties could assert infringement claims in the future with respect to our products and technology, and such claims might be successful. This litigation could result in substantial costs and diversion of resources, whether or not we ultimately prevail on the merits. This litigation could also lead to our being prohibited from selling one or more of our products, cause reluctance by potential customers to purchase our products, or result in liability to our customers and could have a material adverse effect on our business, financial condition, operating results and cash flows.

If our security measures are breached, our products and services may be perceived as not being secure, customers may curtail or stop using our products and services, and we may incur significant legal and financial exposure. Our products and services involve the storage and transmission of our customers' proprietary information, and security breaches could expose us to a risk of loss of this information, litigation, and potential liability. Our security measures may be breached due to the actions of outside parties, employee error, malfeasance, or otherwise, and, as a result, an unauthorized party may obtain access to our



Table of Contents

data or our customers' data. Any such breach or unauthorized access could result in significant legal and financial exposure, increased costs to defend litigation or damage to our reputation, and a loss of confidence in the security of our products and services that could potentially have an adverse effect on our business. Because the techniques used to obtain unauthorized access, disable or degrade service, or sabotage systems change frequently and often are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose customers.

We may have exposure to additional tax liabilities. As a multinational corporation, we are subject to income taxes in the U.S. and various foreign jurisdictions. Significant judgment is required in determining our global provision for income taxes and other tax liabilities. In the ordinary course of a global business, there are many intercompany transactions and calculations where the ultimate tax determination is uncertain. Our income tax returns are routinely subject to audits by tax authorities. Although we regularly assess the likelihood of adverse outcomes resulting from these examinations to determine our tax estimates, a final determination of tax audits or tax disputes could have an adverse effect on our financial condition, results of operations and cash flows.

We are also subject to non-income taxes, such as payroll, sales, use, value-added, net worth, property and goods and services taxes in the U.S. and various foreign jurisdictions. We are regularly under audit by tax authorities with respect to these non-income taxes and may have exposure to additional non-income tax liabilities, which could have an adverse effect on our results of operations, financial condition and cash flows.

In addition, our future effective tax rates could be favorably or unfavorably affected by changes in tax rates, changes in the valuation of our deferred tax assets or liabilities, or changes in tax laws or their interpretation. Such changes could have a material adverse impact on our financial results.

We are required to comply with certain financial and operating covenants under our credit facility and to make scheduled debt payments as they become due; any failure to comply with those covenants or to make scheduled payments could cause amounts borrowed under the facility to become immediately due and payable or prevent us from borrowing under the facility. In December 2014, we entered into a new credit facility, which consists of a \$150 million term loan and a \$150 million revolving loan (and may be increased by an additional \$75 million in the form of revolving loans or term loans, or a combination thereof if the existing or additional lenders are willing to make such increased commitments). This facility matures in December 2019, at which time any amounts outstanding will be due and payable in full. We may wish to borrow additional amounts under the facility in the future to support our operations, including for strategic acquisitions and share repurchases.

We are required to comply with specified financial and operating covenants and to make scheduled repayments of our term loan, which limits our ability to operate our business as we otherwise might operate it. Our failure to comply with any of these covenants or to meet any payment obligations under the facility could result in an event of default which, if not cured or waived, would result in any amounts outstanding, including any accrued interest and unpaid fees, becoming immediately due and payable. We might not have sufficient working capital or liquidity to satisfy any repayment obligations in the event of an acceleration of those obligations. In addition, if we are not in compliance with the financial and operating covenants at the time we wish to borrow funds, we will be unable to borrow funds.

Our common stock price may continue to be volatile, which could result in losses for investors. The market price of our common stock, like that of other technology companies, is volatile and is subject to wide fluctuations in response to quarterly variations in operating results, announcements of technological innovations or new products by us or our competitors, changes in financial estimates by securities analysts or other events or factors. Our stock price may also be affected by broader market trends unrelated to our performance. As a result, purchasers of our common stock may be unable at any given time to sell their shares at or above the price they paid for them.



Table of Contents

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

Items 2(a) and 2(b) are not applicable.

## (c) Stock Repurchases

Information related to the repurchases of our common stock by month in the third quarter of fiscal year 2016 is as follows (in thousands, except per share and share data):

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs
June 2016	442,846	\$ 25.89	442,846	\$ 143,021
July 2016	—	—	—	143,021
August 2016	—	—	—	143,021
Total	442,846	\$ 25.89	442,846	\$ 143,021

## Item 5. Other Matters

On September 28, 2016, we announced the appointment of Kurt J. Abkemeier as our new chief financial officer. As CFO, Mr. Abkemeier will oversee the company's global finance and accounting operations and be a member of the company's executive leadership team, reporting to Phil Pead, president and chief executive officer. Mr. Abkemeier succeeds Chris E. Perkins, who informed the company in March 2016 that he would retire as CFO upon the appointment of his successor. Mr. Abkemeier began as CFO at Progress on September 28, 2016.

## Item 6. Exhibits

The following exhibits are filed or furnished as part of this Quarterly Report on Form 10-Q:

Exhibit No.	Description
31.1*	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act – Philip M. Pead
31.2*	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act – Kurt J. Abkemeier
32.1**	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act
101	The following materials from Progress Software Corporation's Quarterly Report on Form 10-Q for the three and nine months ended August 31, 2016, formatted in XBRL (eXtensible Business Reporting Language):

(i) Condensed Consolidated Balance Sheets as of August 31, 2016 and November 30, 2015; (ii) Condensed Consolidated Statements of Income for the three and nine months ended August 31, 2016 and 2015; (iii) Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended August 31, 2016 and 2015; (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended August 31, 2016 and 2015; and (v) Notes to Condensed Consolidated Financial Statements.

\* Filed herewith

\*\*Furnished herewith

Table of Contents

SIGNATURES

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

PROGRESS SOFTWARE CORPORATION  
(Registrant)

Dated: October 7, 2016 /s/ PHILIP M. PEAD  
Philip M. Pead  
President and Chief Executive Officer  
(Principal Executive Officer)

Dated: October 7, 2016 /s/ KURT J. ABKEMEIER  
Kurt J. Abkemeier  
Chief Financial Officer  
(Principal Financial Officer)

Dated: October 7, 2016 /s/ PAUL A. JALBERT  
Paul A. Jalbert  
Vice President, Corporate Controller and Chief Accounting Officer  
(Principal Accounting Officer)

Table of Contents

EXHIBIT INDEX

Exhibit No. Description

31.1\* Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act – Philip M. Pead

31.2\* Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act – Kurt J. Abkemeier

32.1\*\* Certification Pursuant to Section 906 of the Sarbanes-Oxley Act

The following materials from Progress Software Corporation’s Quarterly Report on Form 10-Q for the three and nine months ended August 31, 2016, formatted in XBRL (eXtensible Business Reporting Language):

101 (i) Condensed Consolidated Balance Sheets as of August 31, 2016 and November 30, 2015; (ii) Condensed Consolidated Statements of Income for the three and nine months ended August 31, 2016 and 2015; (iii) Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended August 31, 2016 and 2015; (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended August 31, 2016 and 2015; and (v) Notes to Condensed Consolidated Financial Statements.

\* Filed herewith

\*\*Furnished herewith