

WAGWORKS, INC.
Form 424B4
October 04, 2012
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Filed Pursuant to Rule 424(b)(4)
Registration No. 333-183889

Prospectus

6,000,000 Shares

Common Stock

WageWorks, Inc. is selling 1,000,000 shares of common stock in this offering. The selling stockholders are selling 5,000,000 shares of common stock in this offering, including 338,566 shares of common stock which will be issued upon the exercise of outstanding warrants. We will not receive any proceeds from the sale of shares to be offered by the selling stockholders other than \$1,550,633 representing the exercise price of the warrants to be exercised in connection herewith.

Our common stock is listed on the New York Stock Exchange under the symbol WAGE. On October 3, 2012, the last reported sale price on the New York Stock Exchange was \$18.24 per share.

The underwriters have an option to purchase a maximum of 900,000 additional shares from the selling stockholders identified in this prospectus to cover overallotments of shares, including 31,313 shares of common stock which will be issued upon the exercise of outstanding warrants in connection herewith.

We are an emerging growth company as defined under the federal securities laws and, as such, may elect to comply with certain reduced public company reporting requirements. Investing in our common stock involves risks. See Risk Factors on page 10 of this prospectus.

	Per Share	Total
Public Offering Price	\$17.50	\$105,000,000
Discounts and commissions to underwriters	\$1.05	\$6,300,000
Offering proceeds to WageWorks, Inc., before expenses	\$16.45	\$16,450,000
Offering proceeds to selling stockholders, before expenses	\$16.45	\$82,250,000(1)

(1) Includes \$1,550,633 to be paid to us representing the exercise price of the warrants to be exercised in connection herewith. Delivery of the shares of common stock will be made on or about October 9, 2012.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Joint Book-Running Managers

William Blair

Stifel Nicolaus Weisel

JMP Securities

Needham & Company

The date of this prospectus is October 3, 2012.

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You should rely only on the information contained in this prospectus or contained in any related free writing prospectus filed by us with the Securities and Exchange Commission. We, the underwriters and the selling stockholders have not authorized anyone to provide you with additional information or information that is different from that contained in this prospectus or contained in any related free writing prospectus filed by us with the Securities and Exchange Commission. This document may only be used where it is legal to sell these securities. The information in this document may only be accurate on the date of this document.

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PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus and does not contain all of the information you should consider in making your investment decision. You should read this entire prospectus carefully, especially the risks of investing in our common stock discussed under Risk Factors and the consolidated financial statements and related notes included elsewhere in this prospectus, before making an investment decision.

Company Overview

We are a leading on-demand provider of tax-advantaged programs for consumer-directed health, commuter and other employee spending account benefits, or CDBs, in the United States. We administer and operate a broad array of CDBs, including spending account management programs, such as health and dependent care Flexible Spending Accounts, or FSAs, Health Savings Accounts, or HSAs, Health Reimbursement Arrangements, or HRAs, and commuter benefits, such as transit and parking programs.

We deliver our CDB programs through a highly scalable Benefits-as-a-Service, or BaaS, delivery model that employer clients and their employee participants may access through a standard web browser on any internet-enabled device, including computers, smart phones and other mobile devices, such as tablet computers. Our on-demand delivery model eliminates the need for our employer clients to install and maintain hardware and software in order to support CDB programs and enables us to rapidly implement product enhancements across our entire user base.

Our CDB programs enable employees and their families to save money by using pre-tax dollars to pay for certain of their healthcare and commuter expenses. Employers financially benefit from our programs through reduced payroll taxes, even after factoring in our fees. Under our FSA, HSA and commuter programs, employee participants contribute funds from their pre-tax income to pay for qualified out-of-pocket healthcare expenses not fully covered by insurance, such as co-pays, deductibles and over-the-counter medical products or for commuting costs.

These employee contributions result in savings to both employees and employers. As an example, based on our average employee participant's annual FSA contribution of approximately \$1,400 and an assumed personal combined federal and state income tax rate of 35%, an employee participant will reduce his or her taxes by approximately \$490 per year by participating in an FSA. Our employer clients also realize payroll tax (i.e., FICA and Medicare) savings on the pre-tax contributions made by their employees. In the above FSA example, an employer client would save approximately \$64 per participant per year, even after the payment of our fees.

Under our HRA programs, employer clients provide their employee participants with a specified amount of available reimbursement funds to help their employee participants defray out-of-pocket medical expenses, such as deductibles, co-insurance and co-payments. All amounts paid by the employer into HRAs are deductible by the employer as an ordinary business expense and are tax-free to the employee.

Our clients include many of the Fortune 100 and Fortune 500 and approximately 3,200 small-and-medium-sized business, or SMB, clients. At January 31, 2012, we had approximately 2.0 million employee participants from approximately 5,000 employer clients. We believe that January 31 is the most appropriate point-in-time measurement date for annual plan metrics. Although plan changes and the entry and exit of employers and participants from our programs are usually decided late in the calendar year during open enrollment to be effective on January 1, it is not unusual for employers to still be submitting updated files of participants in early January. While updates can be delayed past January, any changes from such late updates are usually minimal. Consequently, we believe the January 31 point-in-time measurement date is the most appropriate date to use as a

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baseline. In 2011, employee participants used over two million WageWorks prepaid debit cards. Our revenues are highly diversified, as our largest client represented only 3.0% of our 2011 revenues and our top 10 clients represented only 14.4% of our 2011 revenues. None of the data included in this paragraph reflects the two transactions that we have made in 2012.

Through a combination of the acquisition and integration of smaller third party administrators, or TPAs, which we refer to as portfolio purchases, and organic growth, we grew our revenue from \$108.5 million in 2009 to \$115.0 million in 2010 and to \$135.6 million in 2011. Our revenue increased from \$69.2 million for the first six months ended June 30, 2011 to \$88.1 million for the first six months ended June 30, 2012. In each period, our healthcare revenue growth resulted primarily from portfolio purchases. Our commuter revenue growth in the first six months of 2012 primarily resulted from our acquisition of TransitChek, or TC, on February 1, 2012. For each of 2009, 2010 and 2011, clients that accounted for more than 90% of our revenues (excluding interchange fees and vendor commissions) during the year remained under contract with us in the succeeding year. Our net loss was \$0.6 million and \$17.3 million in the years 2009 and 2010, respectively, and our net income was \$33.3 million in 2011. Our net income decreased from \$6.9 million for the first six months of 2011 to \$5.2 million for the first six months of 2012 primarily due to an increase in tax expense as a result of providing for taxes in the first six months of 2012 without a corresponding and offsetting valuation allowance, since we released the remaining valuation allowance through earnings in December 2011. Our Adjusted EBITDA grew from \$15.9 million in 2009 to \$22.4 million in 2010 and to \$30.3 million in 2011, increases of 40% and 36%, respectively. Adjusted EBITDA increased from \$15.7 million for the first six months of 2011 to \$20.3 million for the first six months of 2012. For a discussion of Adjusted EBITDA and a reconciliation of net income (loss) to Adjusted EBITDA, see footnote 1 to *Selected Consolidated Financial Information*.

Industry Overview

Healthcare costs for both employers and employees continue to increase dramatically. To mitigate the continuing rise in healthcare costs, employers are more frequently passing these costs on to employees by increasing deductibles, out-of-pocket limits and non-network provider cost sharing, and by migrating to co-insurance models systems where employees pay a percentage of the out-of-pocket costs for each healthcare service. As a result, according to a 2011 Hewitt Associates report, average employee out-of-pocket healthcare costs are expected to increase 13.4% from 2011 to 2012.

In addition, rising transportation costs and increasing corporate social responsibility have led to the creation of a variety of programs that are aimed at helping employees understand and reduce their carbon footprint by encouraging alternatives to driving to work. These alternatives include carpooling, cycling and use of public transportation. According to a 2011 American Public Transportation Association report, public transportation is twice as fuel efficient as private automobiles at reducing annual fuel consumption.

CDBs have emerged as an attractive way for employers to offer structured benefit plans to their employees that lessen overall healthcare and transportation costs through the use of tax-advantaged spending accounts.

Employee-funded tax-advantaged spending accounts include:

FSAAs, which allow employees to set aside a portion of earnings on a pre-tax basis to pay for certain expenses primarily related to healthcare, but also cover dependent care, vision and dental expenses;

HSAs, which allow employees to set aside pre-tax earnings for similar expenses, but are available only to individuals who are enrolled in a qualified High Deductible Health Plan; and

Commuter accounts, which allow employee participants to set aside earnings on a pre-tax basis to cover commuter rail, subway, bus, commuter-related parking and eligible vanpool expenses.

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Employer-funded tax-advantaged spending accounts include:

HRAs, which allow employer clients to provide their employee participants with a specified amount of available reimbursement funds to help their employee participants defray out-of-pocket medical expenses, such as deductibles, co-insurance and co-payments. All amounts paid by the employer into HRAs are deductible by the employer as an ordinary business expense and are tax-free to the employee.

Our CDB Programs

We focus on providing CDB programs to employer clients of any size. We provide marketing programs that are designed to increase employee participation in our employer clients' CDB offerings. We believe our employer clients and their employee participants benefit from our superior customer service, efficient workflow processes and advanced monitoring applications. The quality of our customer support has resulted in high levels of client satisfaction and service level performance. We employ a wide range of sophisticated tools to communicate available benefit options to employees and measure the effectiveness of CDB program performance.

We deliver our CDB programs through a BaaS model under which we host and maintain the benefits programs that we provide to our employer clients. Our on-demand delivery model enables employer clients and their employee participants to implement, access and use our proprietary software remotely through a standard web browser on any internet-enabled device, including computers, smart phones and other mobile devices, such as tablet computers. We believe that our on-demand model requires less up-front investment by our employer clients than required by traditional third-party software and hardware options, as well as less personnel resources and implementation services.

Key Business Attributes

Key attributes of our business include the following:

Our revenue is derived almost entirely from recurring monthly fees paid by our employer clients.

Our focus is to consistently deliver the highest quality service to our employer clients and their employee participants, which primarily means providing employee participants with timely and accurate responses to their inquiries, claims submissions and other account transactions.

Our CDB programs employ an easy-to-use website interface that provides our employer clients with robust data and reporting capabilities and provides employee participants with direct access to their accounts, claims history and balance information.

We have historically successfully identified and executed portfolio purchases and integrated the operations of these complementary businesses to expand our employer client base. While we have encountered some challenges in integrating accounting functions in connection with certain of these portfolio purchases, we have leveraged the efficiencies afforded by our on-demand software platform to cross-sell additional CDB products and services to acquired employer clients. We expect to experience similar effects from our acquisition that we completed in early 2012.

Our senior management team has significant operating and service delivery experience with industry-leading businesses.

We have a large and highly diversified employer client base.

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Our core business is providing a comprehensive array of full-featured CDB programs to employers.

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Our Strategy

Our objective is to enhance our position as a leading provider of CDB account management programs. The key elements of our growth strategy are to:

increase employee participation levels within our existing employer client base;

cross-sell additional CDB programs to our existing employer clients;

broaden our employer client base through portfolio purchases;

gain market share with both Fortune 1000 companies and SMBs by leveraging our multiple sales channels; and

continually enhance our products and develop new products and functionality.

Risks Affecting Us

Our business is subject to a number of risks that you should understand before making an investment decision. These risks are discussed more fully in *Risk Factors* following this prospectus summary. Some of these risks include the following:

any diminution in, elimination of, or change in the availability of, tax-advantaged consumer-directed benefits to employees would materially adversely affect our results of operations, financial condition, business and prospects;

our ability to grow our business could be materially adversely affected if we fail to successfully identify, acquire or integrate additional portfolio purchase or acquisition targets;

our business may not grow if our marketing efforts do not successfully raise awareness among employers and employees about the advantages of adopting and participating in CDB programs;

our results of operations, financial condition, business and prospects would be materially adversely affected if we are unable to retain and expand our employer client base;

our business may not grow if a greater percentage of employees do not participate in our employer clients' CDB programs;

our business and prospects may be materially adversely affected if we are unable to cross-sell our products and services;

we may be unable to compete effectively against our current and future competitors; and

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we may not accurately estimate the impact of the development and introduction of new products and services on our business.

Risks Related to this Offering and Ownership of Our Common Stock

There are risks related to this offering and the ownership of our common stock that you should understand before making an investment decision, including that, following the completion of this offering and assuming no exercise by the underwriters of their overallotment option, VantagePoint Capital Partners will hold approximately 34.5% of the outstanding shares of our common stock and will have the right to designate two members of our board of directors, as well as other rights, which may limit the ability of our public stockholders to affect significant corporate actions. These risks are discussed more fully in **Risk Factors** following this prospectus summary.

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Corporate Information

We were incorporated in Delaware in 2000. Our principal executive offices are located at 1100 Park Place, 4th Floor, San Mateo, CA 94403, U.S.A., and our telephone number is 1 (650) 577-5200. Our website address is www.wageworks.com. Information contained on our website is not incorporated by reference into this prospectus, and should not be considered to be part of this prospectus.

WageWorks, Commuter Express, WinFlexOne, Fringe Benefits Management Company, Choice Strategies, TransitChek and other trademarks or trade names of WageWorks appearing in this prospectus are the property of WageWorks, Inc. Other service marks, trademarks and trade names referred to in this prospectus are the property of their respective owners.

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The Offering

Common stock offered by us	1,000,000 shares
Common stock offered by the selling stockholders	5,000,000 shares, which includes 338,566 shares to be issued concurrently with the consummation of this offering upon the exercise of outstanding warrants.
Common stock to be outstanding after this offering	27,713,354 shares
Overallotment option	The underwriters have an option to purchase a maximum of 900,000 additional shares of common stock, including 31,313 shares of common stock to be issued upon the exercise of outstanding warrants, from the selling stockholders to cover overallotments. The underwriters could exercise this option at any time within 30 days from the date of the prospectus.
Use of proceeds	The principal purposes of this offering are to facilitate an orderly distribution of shares for the selling stockholders, to increase our public float and to raise additional capital. We intend to use the net proceeds received by us from this offering for working capital and general corporate purposes, including further expansion of our sales and marketing efforts, continued investments in technology and development and for capital expenditures. In addition, we may use a portion of the proceeds we receive from this offering for portfolio purchases or purchases of technologies or assets to expand our employer client base. However, we do not have agreements for any portfolio purchases at this time. We will not receive any proceeds from the sale of shares of common stock by the selling stockholders, other than \$1,550,633 representing the exercise price of the warrants to be exercised in connection herewith. See <i>Use of Proceeds</i> .
NYSE trading symbol	WAGE
The number of shares of common stock that will be outstanding after this offering is based on the number of shares outstanding as of June 30, 2012 and excludes:	
	5,242,621 shares of common stock issuable upon the exercise of options outstanding as of June 30, 2012, at a weighted average exercise price of \$7.68 per share;
	75,000 shares of common stock issuable upon the exercise of a warrant outstanding as of June 30, 2012 to purchase common stock, at an exercise price of \$8.20 per share;
	4,578,567 shares of common stock issuable upon the exercise of warrants outstanding as of June 30, 2012 to purchase common stock, at a weighted average exercise price of \$4.76 per share (including 338,566 shares of common stock that we expect to be sold in this offering upon the exercise of outstanding warrants concurrently with the consummation of this offering); and

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195,048 shares of common stock reserved for future issuance under our 2010 Equity Incentive Plan as of June 30, 2012. Unless otherwise indicated, all information in this prospectus assumes:

no exercise of options outstanding as of June 30, 2012; and

no exercise by the underwriters of their right to purchase up to an additional 900,000 shares of common stock from the selling stockholders.

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The information set forth below should be read together with *Capitalization, Selected Consolidated Financial Information, Management's Discussion and Analysis of Financial Condition and Results of Operations* and our consolidated financial statements and related notes included elsewhere in this prospectus.

The summary consolidated statements of operations data for the years ended December 31, 2009, 2010 and 2011 have been derived from our audited consolidated financial statements, which are included elsewhere in this prospectus. The unaudited consolidated statement of operations data for the six months ended June 30, 2011 and 2012, as well as the unaudited consolidated balance sheet data as of June 30, 2012, are derived from our unaudited interim consolidated financial statements included elsewhere in this prospectus. The unaudited interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and, in our opinion, reflect all adjustments necessary for the fair presentation of the financial information set forth in those statements. Historical results are not necessarily indicative of the results to be expected in the future and our interim results are not necessarily indicative of the results to be expected for the full fiscal year or for any other period.

Summary Consolidated Financial Information

(in thousands, except per share data)

	Year Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012
				(unaudited)	
Consolidated Statement of Operations Data:					
Revenues	\$ 108,461	\$ 115,047	\$ 135,637	\$ 69,185	\$ 88,087
Operating expenses	107,992	107,013	122,077	61,648	79,450
Income from operations	469	8,034	13,560	7,537	8,637
Interest and other expense, net	(608)	(26,488)	(107)	(236)	(430)
Income (loss) before taxes	(139)	(18,454)	13,453	7,301	8,207
Income tax (provision) benefit	(495)	1,204	19,868	(401)	(2,973)
Net income (loss)	(634)	(17,250)	33,321	6,900	5,234
Accretion of redemption premium (expense) benefit	1,037	(6,740)	(6,209)	(5,692)	(2,301)
Net income (loss) attributable to common stockholders	\$ 403	\$ (23,990)	\$ 27,112	\$ 1,208	\$ 2,933
Net income (loss) per share attributable to common stockholders:					
Basic	\$ 0.25	\$ (15.70)	\$ 17.65	\$ 0.79	\$ 0.37
Diluted	\$ (0.04)	\$ (15.70)	\$ 1.43	\$ 0.07	\$ 0.13
Weighted Average Shares:					
Basic	1,606	1,528	1,536	1,534	7,907
Diluted	16,864	1,528	20,086	16,376	20,683

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	2009	At December 31, 2010	2011	At June 30, 2012 (unaudited)
Consolidated Balance Sheet Data:				
Cash and cash equivalents	\$ 93,261	\$ 104,280	\$ 154,621	\$ 261,340
Total current assets	108,515	124,337	179,829	294,730
Total assets	171,478	206,831	278,696	442,201
Total current liabilities	153,303	167,648	215,645	308,006
Total liabilities	167,430	182,254	218,584	317,430
Total redeemable convertible preferred stock	48,043	75,960	82,169	
Total stockholders' equity (deficit)	(43,995)	(51,383)	(22,057)	124,771

	Years Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012
Non-GAAP Financial Data:					
Adjusted EBITDA (unaudited)	\$ 15,941	\$ 22,366	\$ 30,330	\$ 15,655	\$ 20,316

Notes to Summary Balance Sheet Data and Other Data**Definition of Adjusted EBITDA**

Adjusted EBITDA is a performance measure that is not calculated in accordance with GAAP. The table immediately following this discussion provides a reconciliation of net income (loss) to Adjusted EBITDA, which is the most directly comparable GAAP measure. Adjusted EBITDA should not be considered as an alternative to net income, income from operations or any other measure of financial performance calculated and presented in accordance with GAAP. Our Adjusted EBITDA may not be comparable to similarly titled measures of other companies because other companies may not calculate Adjusted EBITDA or similarly titled measures in the same manner that we do. We prepare Adjusted EBITDA to eliminate the impact of items that we do not consider indicative of our core operating performance. We encourage you to evaluate these adjustments, the reasons we consider them appropriate and the material limitations of Adjusted EBITDA as described in footnote 1 to Selected Consolidated Financial Information.

Our management uses Adjusted EBITDA:

as a measure of operating performance;

as a factor when determining management's compensation;

for planning purposes, including the preparation of our annual operating budget;

to allocate resources of our business; and

to evaluate the effectiveness of our business strategies.

We believe that the use of Adjusted EBITDA provides consistency and comparability with our past financial performance and facilitates period-to-period comparisons of our operating results by management and investors. Although calculation of Adjusted EBITDA may vary from company-to-company, our detailed presentation may facilitate analysis and comparison of our operating results by management and investors with other peer companies, many of which use similar non-GAAP financial measures to supplement their GAAP results in their public disclosures.

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The following provides a reconciliation of net income (loss) to Adjusted EBITDA:

	Year Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011 (unaudited)	2011	2012
Net income (loss)	\$ (634)	\$ (17,250)	\$ 33,321	\$ 6,900	\$ 5,234
Depreciation	4,564	4,164	3,199	1,744	1,446
Amortization and change in contingent consideration	8,398	7,764	11,327	5,175	8,532
Stock-based compensation expense	2,510	2,404	2,244	1,199	1,674
Interest income	(851)	(220)	(36)	(20)	(19)
Interest expense	1,102	188	494	197	857
Interest expense: amortization of convertible debt discount	71	21,107			
Income tax provision (benefit)	495	(1,204)	(19,868)	401	2,973
Loss (gain) on revaluation of warrants	(70)	5,413	(351)	59	(381)
Loss on extinguishment of debt	356				
Adjusted EBITDA	\$ 15,941	\$ 22,366	\$ 30,330	\$ 15,655	\$ 20,316

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RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information in this prospectus, including our consolidated financial statements and related notes included elsewhere in this prospectus, before making an investment decision. If any of the following risks is realized, our business, financial condition, results of operations and prospects could be materially and adversely affected. In that event, the trading price of our common stock could decline and you could lose part or all of your investment.

Risks Related to Our Business and Industry

Our business is dependent upon the availability of tax-advantaged consumer-directed benefits to employers and employees and any diminution in, elimination of, or change in the availability of, these benefits would materially adversely affect our results of operations, financial condition, business and prospects.

Our business fundamentally depends on employer and employee demand for tax-advantaged consumer-directed health, commuter and other employee spending plan benefits, or CDBs. We are not aware of any reliable statistics on the growth of CDB programs and cannot assure you that participation in CDB programs will grow. Any diminution in or elimination of the availability of CDBs for employees would materially adversely affect our results of operations, financial condition, business and prospects. In addition, incentives for employers to offer CDBs may also be reduced or eliminated by changes in laws that result in employers no longer realizing financial gain from the implementation of these benefits. If employers cease to offer CDB programs or reduce the number of programs they offer to their employees, our results of operations, financial condition, business and prospects would also be materially adversely affected.

In addition, if the payroll tax savings employers currently realize from their employees' utilization of CDBs become reduced or unavailable, employers may be less inclined to offer these programs to their employees. If the tax savings currently realized by employee participants by utilizing CDBs were reduced or unavailable, we expect employees would correspondingly reduce or eliminate their participation in such CDB plans. Any such reduction in employer or employee incentives would materially adversely affect our results of operations, financial condition, business and prospects.

Future portfolio purchases and acquisitions are an important aspect of our growth strategy, and any failure to successfully identify, acquire or integrate acquisitions or additional portfolio targets could materially adversely affect our ability to grow our business. In addition, costs of integrating acquisitions and portfolio purchases may adversely affect our results of operations in the short term.

Our recent growth has been, and our future growth will be, substantially dependent on our ability to continue to make and integrate acquisitions and complementary portfolio purchases to expand our employer client base and service offerings. Since 2007, we have completed five portfolio purchases and one acquisition, including one portfolio purchase and one acquisition in 2012. The successful integration of these portfolio purchases and acquisitions into our operations on a cost-effective basis is also critical to our future financial performance. While we believe that there are numerous potential portfolio purchases that would add to our employer client base and service offerings, we cannot assure you that we will be able to successfully make a sufficient number of such portfolio purchases in a timely and effective manner in order to support our growth objectives. In addition, the process of integrating portfolio purchases and our most recent acquisition may create unforeseen difficulties and expenditures. We face various risks in making portfolio purchases and any acquisition, including:

our ability to retain acquired employer clients and their associated revenues;

diversion of management's time and focus from operating our business to address integration challenges;

our ability to retain or replace key employees from acquisitions and portfolios we acquire;

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cultural and logistical challenges associated with integrating employees from acquired portfolios into our organization;

our ability to integrate the combined products, services and technology;

the migration of acquired employer clients to our technology platforms;

our ability to cross-sell additional CDB programs to acquired employer clients;

our ability to realize expected synergies;

the need to implement or improve internal controls, procedures and policies appropriate for a public company at businesses that, prior to the portfolio purchase or acquisition, may have lacked effective controls, procedures and policies, including, but not limited to, processes required for the effective and timely reporting of the financial condition and results of operations of the acquired business, both for historical periods prior to the acquisition and on a forward-looking basis following the acquisition;

possible write-offs or impairment charges that result from acquisitions and portfolio purchases;

unanticipated or unknown liabilities that relate to purchased businesses;

the need to integrate purchased businesses' accounting, management information, human resources, and other administrative systems to permit effective management; and

any change in one of the many complex federal or state laws or regulations that govern any aspect of the financial or business operations of our business and businesses we acquire, such as state escheatment laws.

Portfolio purchases and acquisitions may have a short-term material adverse impact on our results of operations, including a potential material adverse impact on our cost of revenues, as we seek to migrate acquired employer clients to our proprietary technology platforms, typically over the succeeding 12 to 24 months, in order to achieve additional operating efficiencies. For example, our cost of revenues in the six months ended June 30, 2012 included additional expenses of \$4.3 million due to the purchases of TC and The Choice Care Card, LLC, also known as Choice Strategies, or CS, a third party administrator of predominantly SMB HRA accounts, based in Vermont.

Our business may not grow if our marketing efforts do not successfully raise awareness among employers and employees about the advantages of adopting and participating in CDB programs.

Our revenue model is substantially based on the number of employee participants enrolled in the CDB programs that we administer. We devote significant resources to educating both employers and their employees on the potential cost savings available to them from utilizing CDB programs. We have created various marketing, educational and awareness tools to inform employers about the benefits of offering CDB programs to their employees and how our services allow them to offer these benefits in an efficient and cost effective manner. We also provide marketing information to employees that informs them about the potential tax savings they can achieve by utilizing CDB programs to pay for their healthcare, commuter and other benefit needs. However, if more employers and employees do not both become aware of or understand these potential cost savings and choose to adopt CDB programs, our results of operations, financial condition, business and prospects may be materially adversely affected.

If we are unable to retain and expand our employer client base and establish new channel partnerships, our results of operations, financial condition, business and prospects would be materially adversely affected.

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Most of our revenue is derived from the long term, multi-year agreements that we typically enter into with our employer clients. The initial subscription period is typically three years for our larger employer clients, which we refer to as enterprise clients, and one year for our small- and medium-sized business, or SMB, clients. We also derive revenue from our channel partner agreement with American Family Life Assurance Company, or

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Aflac, and we may in the future establish new channel partnerships with other companies. Our employer clients, however, have no obligation to renew their agreements with us after the initial term and we cannot assure you that our employer clients will continue to renew their agreements at the same rate, if at all. Moreover, most of our employer clients have the right to cancel their agreements for convenience, subject to certain notice requirements. While few employer clients have terminated their agreements with us for convenience, some of our employer clients have elected not to renew their agreements with us. Our employer clients' renewal rates may decline or fluctuate as a result of a number of factors, including the prices of competing products or services or reductions in our employer clients' spending levels. Channel partners are independent and typically offer products of competing companies. They require that we provide competitive prices, products and services which may require a significant amount of investment on our part without a guarantee of a return on our investment. Our ability to grow our business will therefore depend to a degree upon our ability to maintain our existing channel partner relationships and develop new relationships. No assurance can be given that new channel partners will be found, that any such new relationships will be successful when they are in place, or that business with our current channel partners will increase. If our employer clients or channel partners do not renew their agreements with us, and we are unable to attract new employer clients or channel partners, our revenue may decline and our results of operations, financial condition, business and prospects may be materially adversely affected.

Our business may not grow if a greater percentage of employees do not participate in our employer clients' CDB programs.

Our revenue depends on the number of employees who participate in the CDB programs that we sell to our employer clients. If more employees do not participate in these benefit programs for various reasons, including a lack of information about the tax-related advantages of doing so, insufficient funds to set aside pre-tax income into such programs, concerns about forfeiting contributions due to forfeiture provisions in FSA benefit programs, or otherwise, our business may not grow as we anticipate and that may materially adversely affect our results of operations, financial condition, business and prospects.

Our business and prospects may be materially adversely affected if we are unable to cross-sell our products and services.

A significant component of our growth strategy is the increased cross-selling of products and services to current and future employer clients. In particular, we expect our ability to cross-sell our commuter programs to our healthcare program clients and our healthcare programs to our commuter employer clients to be an important part of this strategy. We may not be successful in cross-selling our products and services if our employer clients find our additional products and services to be unnecessary or unattractive. Any failure to sell additional products and services to current and future clients could materially adversely affect our results of operations, financial condition, business and prospects.

We may be unable to compete effectively against our current and future competitors.

The market for our products and services is highly competitive, rapidly evolving and fragmented. We have numerous competitors, including health insurance carriers, such as Aetna and UHC, human resources consultants and outsourcers, such as Aon Hewitt, payroll providers, such as ADP and Ceridian, national CDB specialists, such as TASC, and regional third party administrators and commercial banks, such as Bank of America. Many of our competitors, including health insurance carriers, have longer operating histories and significantly greater financial, technical, marketing and other resources than we have. As a result, some of these competitors may be in a position to devote greater resources to the development, promotion, sale and support of their products and services.

In addition, if one or more of our competitors were to merge or partner with another of our competitors, the change in the competitive landscape could materially adversely affect our ability to compete effectively. Our

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competitors may also establish or strengthen cooperative relationships with our current or future strategic brokers, insurance carriers, payroll services companies, third party advisors or other parties with which we have relationships, thereby limiting our ability to promote our CDB programs with these parties and limiting the number of brokers available to sell or market our programs. If we are unable to compete effectively with our competitors for any of the foregoing reasons or for any other reasons, our results of operations, financial condition, business and prospects could be materially adversely affected.

We plan to extend and expand our products and services and introduce new products and services, and we may not accurately estimate the impact of developing and introducing these products and services on our business.

We intend to continue to invest in technology and development to create new and enhanced products and services to offer our employer clients and their participating employees. For example, in 2011, we deployed a mobile application that enables employee participants to access their accounts and submit healthcare and dependent care claims as well as healthcare debit card receipts. Employee participants can securely send digital photos of their receipts to verify expenses and debit card transactions directly from their iPhone®, iPad®, Android and Blackberry® devices. We have limited experience in these areas, however, and we may not be able to anticipate or manage new risks and obligations or legal, compliance or other requirements that may arise. In addition, the anticipated benefits of these expanded products and services may not outweigh the costs and resources associated with their development.

Our ability to attract and retain new employer clients and increase revenue from existing employer clients will depend in large part on our ability to enhance and improve our existing products and services and to introduce new products and services. The success of any enhancement or new product or service depends on several factors, including the timely completion, introduction and market acceptance of the enhancement or new product or service. Any new product or service we develop or acquire may not be introduced in a timely or cost-effective manner and may not achieve the broad market acceptance necessary to generate significant revenue. If we are unable to successfully develop or acquire new products or services or enhance our existing products or services to meet client requirements, our results of operations, financial condition, business or prospects may be materially adversely affected.

If the market for our services does not grow as we anticipate, our results of operations, financial condition, business and prospects may be materially adversely affected.

Our future success depends on increasing the number of employer clients and their employee participants to whom we provide our services. However, there is no guarantee that the market for our services will grow as we expect. For example, the value of our services is directly related to the complexity of administering CDB programs and government action that significantly reduces or simplifies these requirements could reduce demand or pricing for our services. If the market for our services declines or develops more slowly than we expect, or the number of employer clients that select us to provide CDB programs to their employee participants declines or fails to increase as we expect, our revenue, results of operations, financial condition, business and prospects could be materially adversely affected.

General economic and other conditions may adversely affect trends in employment and hiring patterns, which could result in lower employee participation in CDB programs, which would materially adversely affect our results of operations, financial condition, business and prospects.

Our revenue is attributable to the number of employee participants at each of our employer clients, which in turn is influenced by the employment and hiring patterns of our employer clients. To the extent that weak economic conditions cause our employer clients to freeze or reduce their headcount or wages paid, demand for our programs may decrease, which could materially adversely affect our results of operations, financial condition, business and prospects. Similarly, our revenue growth opportunities may be negatively affected by such headcount or wage reductions by our potential employer clients.

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Our business and prospects may be materially adversely affected if we are unable to maintain high levels of service while reducing operating costs.

One of the key attributes of our business is providing high quality service to our employer clients and their employee participants. While we have exceeded contractual service levels to our enterprise employer clients each month since May 2007, as our business grows and we service increasing numbers of employer clients and their employee participants, we may be unable to sustain these same levels of service, which could have a material adverse effect on our business. Alternatively, we may only be able to sustain high levels of service by significantly increasing our operating costs, which would materially adversely affect our operating results. If we are unable to maintain these high levels of service performance, our brand and reputation could suffer and our results of operations, financial condition, business and prospects would be materially adversely affected.

Failure to effectively develop and expand our direct and indirect sales channels may materially adversely affect our results of operations, financial condition, business and prospects and reduce our growth.

We will need to continue to expand our sales and marketing infrastructure in order to grow our employer client base and our business. We rely on our enterprise sales force to target new Fortune 1000 client accounts, as well as to cross-sell additional products and services to our existing enterprise clients. Effectively training our sales personnel requires significant time, expense and attention. In addition, we utilize various channel brokers, including insurance agents, benefits consultants, regional and national insurance carriers, health plans, payroll companies, banks and regional TPAs, to sell and market our programs to SMB employers. If we are unable to develop and expand our direct sales teams or these indirect sales channels, our ability to attract new employer clients and cross-sell our programs may be negatively impacted and our growth opportunities will be reduced, each of which would materially adversely affect our results of operations, financial condition, business and prospects.

If our efforts to develop and expand our direct and indirect sales channels do not generate a corresponding increase in revenue, our business may be materially adversely affected. In particular, if we are unable to effectively train our sales personnel or if our direct sales personnel are unable to achieve expected productivity levels in a reasonable period of time, we may not be able to increase our revenue and grow our business.

Long sales cycles make the timing of our long-term revenues difficult to predict.

Our sales cycle generally varies in length between two and nine months and, in some cases, even longer depending on the size of the potential client. Factors that may influence the length of our sales cycle include:

the need to educate potential employer clients about the uses and benefits of our CDB programs;

the relatively long duration of the commitment clients make in their agreements with us or with pre-existing plan administrators;

the discretionary nature of potential employer clients' purchasing and budget cycles and decisions;

the competitive nature of potential employer clients' evaluation and purchasing processes;

fluctuations in the CDB program needs of potential employer clients; and

lengthy purchasing approval processes of potential employer clients.

The fluctuations that result from the length of our sales cycle may be magnified for large- and mid-sized potential employer clients. If we are unable to close an expected significant transaction with one or more of these potential clients in the anticipated period, our operating results for that period, and for any future periods in which revenue from such transaction would otherwise have been recognized, would be harmed.

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Our business and operational results are subject to seasonality as a result of open enrollment for CDB programs and decreased use of commuter program offerings during typical vacation months.

The number of accounts that generate revenue is typically greatest during our first calendar quarter due primarily to three factors. First, new employer clients and their employee participants typically begin service on January 1. Second, during the first calendar quarter, we are also servicing the end of plan year activity for existing clients and employee participants who do not continue participation into the next plan year. Third, we receive the majority of cash for pre-funded accounts from our employer clients in late December or early January, which results in higher cash balances during our first quarter.

Generally, in comparison to other quarters, our revenue is highest in the first quarter and lowest in the second and third quarters. Thereafter, our revenue generally grows gradually in the fourth quarter as our employer clients hire new employees who then elect to participate in our programs, thereby increasing our monthly minimum billing amount. The minimum billing amount is not, however, generally subject to downward revision when employees leave their employers because we continue to administer those former employee participants' accounts for the remainder of the plan year. Revenue from commuter programs may vary from month-to-month because employees may elect to participate in our commuter programs at any time during the year and may change their election to participate or the amount of their contribution on a monthly basis; however, participation rates in our commuter business typically slow during the summer as people take vacations and do not purchase transit passes or parking passes during that time.

Our operating expenses increase during the fourth quarter because we increase our customer support center capacity to answer questions from employee participants during the open enrollment periods related to their CDB participation decisions. The cost of providing services peaks in the first quarter as new employee participants contact us for information about their CDBs, and as terminating employee participants submit their final claims for reimbursement.

If employee participants do not continue to utilize our prepaid debit cards, our results of operations, business and prospects could be materially adversely affected.

We derive a portion of our revenue from interchange fees that are paid to us when employee participants utilize our prepaid debit cards to pay for certain healthcare and commuter expenses under CDB programs. These fees represent a percentage of the expenses transacted on each debit card. If our employer clients do not adopt these prepaid debit cards as part of the benefits programs they offer, if the employee participants do not use them at the rate we expect, or if other alternatives to prepaid tax-advantaged benefit cards develop, our results of operations, business and prospects could be materially adversely affected.

If we are unable to maintain and enhance our brand and reputation, our ability to sustain and grow our business may be materially adversely affected.

Maintaining and strengthening our brand is critical to attracting new clients and growing our business. Our ability to maintain and strengthen our brand and reputation will depend heavily on our capacity to continue to provide high levels of customer service to our employer clients and their employee participants at cost effective and competitive prices, which we may not do successfully. In addition, our continued success depends, in part, on our reputation as an industry leader in promoting awareness and understanding of the positive impact of CDBs among employers and employees. If we fail to successfully maintain and strengthen our brand, our results of operations, financial condition, business and prospects will be materially adversely affected.

Some plan providers with which we have relationships also provide, or may provide, competing services.

We face competitive risks in situations where some of our strategic partners are also current or potential competitors. For example, certain of the banks we utilize as custodians for our prepaid debit card funds also offer

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their own HSA products. To the extent that these partners choose to offer competing products and services that they have developed or in which they have an interest to our current or potential clients, our results of operations, business and prospects could be materially adversely affected.

We are subject to complex regulation, and any compliance failures or regulatory action could materially adversely affect our business.

The plans we administer and, as a result, our business are subject to extensive, complex and continually changing federal and state laws and regulations, including IRS regulations, ERISA, privacy and HIPAA regulations and Department of Labor regulations, all of which are further described in Business Government Regulation below. If we fail to comply with any applicable law, rule or regulation, we could be subject to fines and penalties, indemnification claims by our clients, or become the subject of a Department of Labor enforcement action, each of which would materially adversely affect our business and reputation.

We may also become subject to additional regulatory and compliance requirements as a result of changes in laws or regulations, or as a result of any expansion or enhancement of our existing products and services or any new products or services we may offer in the future. For example, if we expand our product and service offerings into the health insurance market in the future, we would become subject to state Department of Insurance regulations. Compliance with any new regulatory requirements may divert internal resources and take significant time and effort.

Any claims of noncompliance brought against us, regardless of merit or ultimate outcome, could subject us to investigation by the Department of Labor, the Internal Revenue Service, the Centers for Medicare and Medicaid Services, the Treasury Department or other federal and state regulatory authorities, which could result in substantial costs to us and divert management's attention and other resources away from our operations. In addition, investor perceptions of us may suffer and could cause a decline in the market price of our common stock. Our compliance processes may not be sufficient to prevent assertions that we failed to comply with any applicable law, rule or regulation.

Changes in healthcare laws and other regulations applicable to our business may constrain our ability to offer our products and services.

Changes in healthcare or other laws and regulations applicable to our business may occur that could increase our compliance and other costs of doing business, require significant systems enhancement, or render our products or services less profitable or obsolete, any of which could have a material adverse effect on our results of operations. For instance, when the new debit card network exclusivity restrictions set forth in the Durbin Amendment to the Electronic Fund Transfer Act are implemented in April 2013, we will be required to use at least two unaffiliated networks for our prepaid debit cards and the card issuers and networks may pass a portion of the implementation costs of such changes to us. While we do not currently expect that this will have, or is reasonably likely to have, a material adverse impact on our financial condition or operating results, we will need to continue to monitor the status of this rule as well as other potential changes in laws or regulations that may impact our business as such changes could potentially adversely affect our business, prospects and results of operations.

There has been an increasing political and regulatory focus on healthcare laws in recent years. While legislation such as the Patient Protection and Affordable Care Act has been signed into law, many of the details necessary to implement the legislation have yet to be defined. For example, any new laws that increase reporting and compliance burdens on employers may make them less likely to offer CDBs to their employees and instead offer employees benefit coverage through state run health insurance exchanges. If employers are less incentivized to offer our CDB programs to employees because of increased regulatory burdens or otherwise, our results of operations and financial condition could be materially adversely affected.

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Failure to ensure and protect the confidentiality of participant data could lead to legal liability, adversely affect our reputation and have a material adverse effect on our results of operations, business or financial condition.

We must collect, store and use employee participants' confidential information, including the transmission of that data to third parties, to provide our services. For example, we collect names, addresses, social security numbers and other personally identifiable information from employee participants. In addition, we facilitate the issuance and funding of prepaid debit cards and, in some cases, collect bank routing information, account numbers and personal credit card information for purposes of funding an account or issuing a reimbursement. We have invested significantly in preserving the security of this data.

In addition, we outsource customer support center services and claims processing services to third-party subcontractors to whom we transmit certain confidential information of our employee participants. We have security measures in place with each of these subcontractors to protect this confidential information, including written agreements that outline how protected health information will be handled and shared. However, there are no assurances that these measures, or any additional security measures that our subcontractors may have in place, will be sufficient to protect this outsourced confidential information from unauthorized security breaches.

We cannot assure you that, despite the implementation of these security measures, we will not be subject to a security breach or that this data will not be compromised. We may be required to expend significant capital and other resources to protect against security breaches or to alleviate problems caused by security breaches. Despite our implementation of security measures, techniques used to obtain unauthorized access or to sabotage systems change frequently. As a result, we may be unable to anticipate these techniques or implement adequate preventative measures to protect this data. Any compromise or perceived compromise of our security could damage our reputation with our clients and brokers, and could subject us to significant liability, as well as regulatory action, which would materially adversely affect our brand, results of operations, financial condition, business and prospects.

Privacy concerns could require us to modify our operations.

As part of our business, we collect employee participants' personal data for the sole purpose of processing their benefits. For privacy or security reasons, privacy groups, governmental agencies and individuals may seek to restrict or prevent our use of this data. We have incurred, and will continue to incur, expenses to comply with privacy and security standards and protocols imposed by law, regulation, industry standards or contractual obligations. Increased domestic or international regulation of data utilization and distribution practices, including self-regulation, could require us to modify our operations and incur significant additional expense, which could have a material adverse effect on our results of operations, financial condition, business and prospects.

If we fail to effectively upgrade our information technology systems, our business and operations could be disrupted.

As part of our efforts to continue the improvement of our enterprise resource planning, we plan to upgrade our existing information technology systems in order to automate several controls that are currently performed manually. We may experience difficulties in transitioning to these upgraded systems, including loss of data and decreases in productivity as personnel work to become familiar with these new systems. In addition, our management information systems will require modification and refinement as we grow and as our business needs change, which could prolong difficulties we experience with systems transitions, and we may not always employ the most effective systems for our purposes. If we experience difficulties in implementing new or upgraded information systems or experience significant system failures, or if we are unable to successfully modify our management information systems or respond to changes in our business needs, we may not be able to effectively manage our business and we may fail to meet our reporting obligations.

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Our future success depends on our ability to recruit and retain qualified employees, including our executive officers.

Our success is substantially dependent upon the performance of our senior management, such as our chief executive officer. Our management and employees may terminate their employment at any time, and the loss of the services of any of our executive officers could materially adversely affect our business. Our success is also substantially dependent upon our ability to attract additional personnel for all areas of our organization. Competition for qualified personnel is intense, and we may not be successful in attracting and retaining such personnel on a timely basis, on competitive terms or at all. If we are unable to attract and retain the necessary personnel, our results of operations, financial condition, business and prospects would be materially adversely affected.

We might require additional capital to support business growth in the future, and this capital might not be available on acceptable terms, if at all.

We believe that our existing cash and cash equivalents, combined with our credit line, expected cash flow from operations and net proceeds of this offering, will be sufficient to meet our operating and capital requirements, as well as anticipated requirements for potential additional portfolio purchases, for at least the next 12 months. Our business and operations may, however, consume resources faster than we currently anticipate. We intend to continue to make investments to support our business growth, including through additional portfolio purchases of complementary businesses, and may require additional funds in the future to respond to business challenges, including the need to develop new features and platforms, enhance our existing programs or improve our operating infrastructure. Accordingly, we may seek to sell additional equity or debt securities or obtain additional debt financing. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing secured by us in the future could involve restrictive covenants relating to our capital-raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential portfolio purchases. We have not made arrangements to obtain additional financing and there can be no assurances that financing, if required, will be available in amounts or on terms acceptable to us, if at all.

Changes in credit card association or other network rules or standards set by Visa or MasterCard, or changes in card association and debit network fees or products or interchange rates, could materially adversely affect our results of operations, business and financial position.

We, and the banks that issue our prepaid debit cards, are subject to Visa and MasterCard association rules that could subject us to a variety of fines or penalties that may be levied by the card associations or networks for acts or omissions by us or businesses that work with us, including card processors, such as Fidelity National Information Services. The termination of the card association registrations held by us or any of the banks that issue our cards, or any changes in card association or other debit network rules or standards, including interpretation and implementation of existing rules or standards that increase the cost of doing business or limit our ability to provide our products and services, could have a material adverse effect on our results of operations, financial condition, business and prospects. In addition, from time-to-time, card associations increase the organization or processing fees that they charge, which could increase our operating expenses, reduce our profit margin and materially adversely affect our results of operations, financial condition, business and prospects.

Our operating results can fluctuate from period-to-period, which could cause our share price to fluctuate.

Our quarterly operating results may fluctuate as a result of a variety of factors, including fluctuations in our operating expenses during the year for items such as printing and temporary labor expenses. Fluctuations in our quarterly operating results could cause our stock price to decline rapidly, may lead analysts to change their long-term models for valuing our common stock, could cause short-term liquidity issues, may impact our ability to

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retain or attract key personnel or cause other unanticipated issues. If our quarterly operating results or guidance fall below the expectations of research analysts or investors, the price of our common stock could decline substantially.

Our quarterly operating expenses and operating results may vary significantly in the future and period-to-period comparisons of our operating results may not be meaningful. You should not rely on the results of one quarter as an indication of future performance.

Our results of operations, financial condition, business and prospects could be materially adversely affected if we experience unanticipated delays in rollouts by our employer clients of services to their employee participants.

We generally do not earn fees from our employer clients until our services are available to their employee participants. If our infrastructure capacity is insufficient to meet our needs, we may experience delays in deploying our programs to new employer clients, or expanding the services we offer to existing employer clients, and on-boarding their employee participants. If the rollout of our services to our employer clients and, subsequently, their employee participants is delayed, our results of operations, financial condition, business and prospects could be materially adversely affected.

If we fail to manage future growth effectively, we may not be able to market and sell our products and services successfully.

We have expanded our operations significantly in recent years and anticipate that further expansion will be required in order for us to grow our business. If we do not effectively manage our growth, the quality of our services could suffer, which could materially adversely affect our results of operations, financial condition, business and prospects, and damage our reputation among existing and prospective clients. In order to manage our future growth, we will need to hire, integrate and retain highly skilled and motivated employees. We will also be required to continue to improve our existing systems for operational and financial information management, including our reporting systems, procedures and controls and regulatory compliance processes. These improvements may require significant capital expenditures and will place increasing demands on our management. We may not be successful in managing or expanding our operations, or in maintaining adequate operating and financial information systems and controls. If we are not successful in implementing improvements in these areas, our results of operations, financial condition, business and prospects would be materially adversely affected.

We have entered into outsourcing and other agreements with third parties related to certain of our business operations, and any difficulties experienced in these arrangements could result in additional expense, loss of revenue or an interruption of our services.

We have entered into outsourcing agreements with third parties to provide certain customer service and related support functions to our employer clients and their participant employees. As a result, we rely on third parties over which we have limited control to perform certain of our operations. If these third parties are unable to perform to our requirements or to provide the level of service required or expected by our employer clients and their employee participants, our operating results, financial condition, business, prospects and reputation may be materially harmed and we may be forced to pursue alternative strategies to provide these services, which could result in delays, interruptions, additional expenses and loss of clients and related revenues.

If our intellectual property and technology are not adequately protected to prevent use or appropriation by our competitors, our business and competitive position could be materially adversely affected.

We rely on a combination of copyright, trademark and trade secret laws, as well as confidentiality procedures and contractual provisions, to establish and protect our intellectual property rights in the United States.

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The efforts we have taken to protect our intellectual property may not be sufficient or effective, and our trademarks and copyrights may be held invalid or unenforceable. We may not be effective in policing unauthorized use of our intellectual property, and even if we do detect violations, litigation may be necessary to enforce our intellectual property rights. Any enforcement efforts we undertake, including litigation, could be time consuming and expensive, could divert our management's attention and may result in a court determining that our intellectual property rights are unenforceable. If we are not successful in cost-effectively protecting our intellectual property rights, our results of operations, financial condition, business and prospects could be materially adversely affected.

Our ability to use net operating loss carryforwards to offset future taxable income may be limited.

As of December 31, 2011, we had \$47.9 million of federal and \$38.9 million of state net operating loss carryforwards available to offset future taxable income. These net operating loss carryforwards will expire beginning in 2023 through 2029 for U.S. federal income tax purposes and beginning in 2012 through 2031 for state income tax purposes, if not fully utilized. In addition, we have federal and state research and development credit carryforwards of \$2.6 million and \$1.1 million respectively. The federal research credit carryforwards expire beginning in the years 2022 through 2031, if not fully utilized. The California research credit carries forward indefinitely. Our ability to utilize net operating loss and tax credit carryforwards in the future may be subject to substantial restriction under applicable law, including in the event of past or future ownership changes as defined in Section 382 of the Internal Revenue Code of 1986, as amended and similar state law (including in connection with this offering), which ownership changes may be outside of our control.

If one or more jurisdictions successfully assert that we should have collected or in the future should collect additional sales and use taxes on our fees, we could be subject to additional liability with respect to past or future sales and the results of our operations could be adversely affected.

We do not collect sales and use taxes in all jurisdictions in which our employer clients are located, based on our belief that such taxes are not applicable. Sales and use tax laws and rates vary by jurisdiction and such laws are subject to interpretation. Jurisdictions in which we do not collect sales and use taxes may assert that such taxes are applicable, which could result in the assessment of such taxes, interest and penalties, and we could be required to collect such taxes in the future. This additional sales and use tax liability could adversely affect the results of our operations.

Third parties may assert intellectual property infringement claims against us, or our services may infringe the intellectual property rights of third parties, which may subject us to legal liability and materially adversely affect our reputation.

Assertion of intellectual property infringement claims against us could result in litigation. We might not prevail in any such litigation or be able to obtain a license for the use of any infringed intellectual property from a third party on commercially reasonable terms, or at all. Even if obtained, we may be unable to protect such licenses from infringement or misuse, or prevent infringement claims against us in connection with our licensing efforts. Any such claims, regardless of their merit or ultimate outcome, could result in substantial cost to us, divert management's attention and our resources away from our operations and otherwise adversely affect our reputation. Our process for controlling our own employees' use of third-party proprietary information may not be sufficient to prevent assertions of intellectual property infringement claims against us.

We rely on insurance to mitigate some risks of our business and, to the extent the cost of insurance increases or we maintain insufficient coverage, our results of operations, business and financial condition may be materially adversely affected.

We contract for insurance to cover a portion of our potential business risks and liabilities. In the current environment, insurance companies are increasingly specific about what they will and will not insure. It is

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possible that we may not be able to obtain sufficient insurance to meet our needs, may have to pay very high prices for the coverage we do obtain or may not acquire any insurance for certain types of business risk. This could leave us exposed, and to the extent we incur liabilities and expenses for which we are not adequately insured, our results of operations, business and financial condition could be materially adversely affected. Also, to the extent the cost of maintaining insurance increases, our operating expenses will rise, which could materially adversely affect our results of operations, financial condition, business and prospects.

Risks Related to this Offering and Ownership of Our Common Stock

VantagePoint Capital Partners holds a high percentage of our common stock, which may limit the ability of our public stockholders to affect significant corporate actions.

After this offering, funds affiliated with VantagePoint Capital Partners, or VantagePoint, will hold approximately 34.5% of our outstanding common stock, assuming no exercise by the underwriters of their overallotment option. In addition, we and VantagePoint are parties to a stockholder agreement related to a number of board of directors, stockholder and related governance matters.

The stockholder agreement provides that the following actions by us require the approval of VantagePoint for so long as VantagePoint owns 25% or more of our outstanding shares of common stock:

any amendment of our bylaws;

the issuance of any securities with economic rights senior to our common stock or with voting rights different than our common stock, subject to certain exceptions;

the incurrence or guarantee of any debt in excess of \$20.0 million;

the issuance of equity or debt, or any securities convertible into equity or debt, for consideration in excess of 12.5% of our market capitalization;

the acquisition or disposition of stock or assets, including through a license or lease, for consideration in excess of 12.5% of our market capitalization;

the adoption of a stockholder rights plan;

the approval of any golden parachute or other compensatory plan contingent upon a change in control of us for any of our executive officers valued in excess of \$1 million for an individual officer or \$5 million for a group of officers, at the time such compensatory arrangement is adopted; or

any change in the number of authorized directors.

Accordingly, our ability to engage in significant transactions, such as a merger, acquisition or liquidation, is limited without the consent of VantagePoint. Conflicts of interest could arise between us and VantagePoint, and any conflict of interest may be resolved in a manner that does not favor us. VantagePoint may decide not to consent to a transaction in which you would receive consideration for your common shares that is higher than the cost to you or the then-current market price of those shares. Any decision that VantagePoint may make at some future time regarding their ownership of us will be in their absolute discretion.

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In addition, our stockholder agreement with VantagePoint and our amended and restated certificate of incorporation and amended and restated bylaws provide the following additional rights to VantagePoint:

so long as VantagePoint owns more than 30% of our outstanding voting stock, a special meeting of our stockholders may be called by either VantagePoint or any two members of our board of directors, whether or not VantagePoint designees;

so long as VantagePoint owns more than 40% of our outstanding voting stock, our stockholders may act by written consent to change the number of authorized directors, remove a director without cause or fill a vacancy on our board of directors (following this offering, VantagePoint will own approximately 34.5% of our outstanding common stock);

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we may not amend any provision of our certificate of incorporation or bylaws relating to VantagePoint's rights without VantagePoint's consent; and

VantagePoint and its representatives will have access to our books and records, subject to customary confidentiality and non-disclosure provisions.

VantagePoint has the right to designate (and remove or replace) three of the members of our board of directors if VantagePoint owns at least 50% or more of our outstanding shares, two members of our board of directors if VantagePoint owns between 20% and 50% of our outstanding shares, and one member of our board of directors if VantagePoint owns between 10% and 20% of our outstanding shares (following this offering, VantagePoint will own approximately 34.5% of our outstanding common stock). VantagePoint also has the right to select one of its board designees to serve on our compensation committee, our nominating and corporate governance committee and any other special committee of our board of directors, so long as it continues to hold at least 10% of our outstanding shares.

VantagePoint is not prohibited from selling its interest in us to a third party.

We will continue to incur increased costs and demands upon management as a result of complying with the laws and regulations that affect public companies, which could materially adversely affect our results of operations, financial condition, business and prospects.

As a public company and particularly after we cease to be an emerging growth company, we will continue to incur significant legal, accounting and other expenses that we did not incur as a private company, including costs associated with public company reporting and corporate governance requirements. These requirements include compliance with Section 404 and other provisions of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, as well as rules implemented by the SEC and the NYSE. In addition, our management team will also have to continue to adapt to the requirements of being a public company. We expect that compliance with these rules and regulations will substantially increase our legal and financial compliance costs and will make some activities more time-consuming and costly.

The increased costs associated with operating as a public company will decrease our net income or increase our net loss, and may require us to reduce costs in other areas of our business or increase the prices of our products or services. Additionally, if these requirements divert our management's attention from other business concerns, they could have a material adverse effect on our results of operations, financial condition, business and prospects.

However, for as long as we remain an emerging growth company as defined in the Jumpstart our Business Startups Act of 2012, or JOBS Act, we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. We may take advantage of these reporting exemptions until we are no longer an emerging growth company.

We will remain an emerging growth company for up to five years from the date of our initial public offering, although if the market value of our common stock that is held by non-affiliates exceeds \$700 million as of any June 30 before that time, we would cease to be an emerging growth company as of the following December 31, or if we issue more than \$1 billion in non-convertible debt in a three-year period, we would cease to be an emerging growth company immediately.

As a public company, we also expect that it may be more difficult and expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur

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substantially higher costs to obtain the same or similar coverage. As a result, it may be more difficult for us to attract and retain qualified individuals to serve on our board of directors or as our executive officers.

As a public company, we are required to maintain a system of effective control over financial reporting. It was determined in connection with the audit of our 2010 financial results that we had significant deficiencies with respect to instances of lack of timely financial reporting and reliable financial statements, inability to timely integrate the accounting function of certain of our portfolio purchases and inconsistencies and omissions in key documents and that in connection with the audit of our 2011 financial results that we still had a significant deficiency regarding our inability to timely integrate the accounting function of certain of our portfolio purchases. If we do not remediate this significant deficiency and develop effective controls, our impaired ability to produce accurate and timely financial reports could cause our stock price to decline.

We have, in the past, experienced issues with our internal control over financial reporting. For example, three significant deficiencies were identified in internal controls in connection with the preparation of our financial statements and the audit of our financial results for 2010. We had significant deficiencies relating to: the completion of our financial reporting cycle within the expected period and our ability to produce reliable financial statements in the period that would normally be expected of a public company; our ability to timely integrate accounting functions of certain of our portfolio purchases; and certain inconsistencies and omissions in some of our key documents and agreements. The lack of timely financial reporting involved adjustments of a bonus accrual that was not timely made and the number of errors, missing disclosures and incorrect numbers in the financial statements we delivered to our independent registered public accounts for audit. The inability to timely integrate the accounting function of portfolio purchases related to our inability through March 2011 to reconcile an opening balance sheet for our PBS acquisition on August 31, 2010. The inconsistencies and omissions in key documents related to certain agreements that were not appropriately documented or referred to other agreements that did not exist, including agreements relating to our acquisition of the CDB assets of FBM.

In connection with the preparation of our financial statements and the audit of our financial results for 2011, it was determined that we remediated the significant deficiency relating to lack of timely financial reporting and reliable financial statements by the hiring of additional qualified accounting personnel. Hires to date include an SEC reporting manager, an internal auditor who will also address Sarbanes-Oxley issues, an accounting manager, a general ledger accountant, a financial analyst and a treasury analyst. It was also determined that we remediated the significant deficiency related to inconsistencies and omissions in some of our key documents and agreements. Since we did not complete any portfolio purchases in 2011, we were unable to remediate the significant deficiency with respect to timely integration of the accounting function of portfolio purchases. However, we intend to do so by earlier assessment of the accounting function at the company from which the portfolio is purchased and allocation of needed resources, including the hiring of consultants, to assure timely integration. For example, for the acquisition and portfolio purchase that we have completed in 2012, we have assigned a full-time accounting resource and a consultant to lead the accounting integration of CS and TC.

We cannot assure that these actions will entirely remediate this significant deficiency or that other material weaknesses or significant deficiencies will not be discovered.

We will not be required to comply with certain provisions of the Sarbanes-Oxley Act for as long as we remain an emerging growth company.

As long as we remain an emerging growth company, we will not be required to comply with certain of the SEC rules that implement Section 404 of the Sarbanes-Oxley Act, and require us to make a formal assessment of the effectiveness of our internal control over financial reporting. Though we will be required to disclose changes made in our internal control procedures on a quarterly basis, we will not be required to make our first annual assessment of our internal control over financial reporting pursuant to Section 404 until the later of the year following our first annual report required to be filed with the SEC, or the date we are no longer an emerging growth company as defined in the JOBS Act. We will remain an emerging growth company for up to five years, although if the market value of our common stock that is held by non-affiliates exceeds \$700 million as of

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any June 30 before that time, we would cease to be an emerging growth company as of the following December 31, or if we issue more than \$1 billion in non-convertible debt in a three-year period, we would cease to be an emerging growth company immediately.

Our independent registered public accounting firm is not required to formally attest to the effectiveness of our internal control over financial reporting until the later of the year following our first annual report required to be filed with the SEC, or the date we are no longer an emerging growth company. At such time, our independent registered public accounting firm may issue a report that is adverse in the event it is not satisfied with the level at which our controls are documented, designed or operating.

We are an emerging growth company and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an emerging growth company, as defined in the JOBS Act, and we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. We cannot predict whether investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

In addition, Section 107 of the JOBS Act also provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act for complying with new or revised accounting standards. An emerging growth company can therefore delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we are choosing to opt out of such extended transition period, and as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

Our stock price has been volatile, may continue to be and may decline regardless of our financial performance.

The market price of our common stock has fluctuated and may continue to fluctuate significantly in response to numerous factors, many of which are beyond our control, including:

actual or anticipated fluctuations in our financial results;

the financial projections we provide to the public, any changes in these projections or our failure to meet these projections;

failure of securities analysts to initiate or maintain coverage of our company, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;

ratings changes by any securities analysts who follow our company;

announcements by us or our competitors of significant technical innovations, acquisitions, strategic partnerships, joint ventures or capital commitments;

changes in operating performance and stock market valuations of other newly public companies generally, or those in our industry in particular;

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price and volume fluctuations in the overall stock market, including as a result of trends in the global economy;

any major change in our board of directors or management;

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lawsuits threatened or filed against us; and

other events or factors, including those resulting from war, incidents of terrorism or responses to these events.

In addition, the stock market in general, and the market for newly public companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may seriously affect the market price of companies' stock, including ours, regardless of actual operating performance. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against such a company. If securities class action litigation is instituted against us, it could result in substantial costs and a diversion of our management's attention and resources and could materially adversely affect our operating results.

A total of 13,705,829 shares, or 49.5%, of our total outstanding shares after this offering are restricted from immediate resale, but may be sold on the NYSE in the near future. The large number of shares eligible for public sale or subject to rights requiring us to register them for public sale could depress the market price of our common stock.

The market price of our common stock could decline as a result of sales of a large number of shares of our common stock in the market after this offering, and the perception that these sales could occur may also depress the market price of our common stock. Based on shares outstanding as of June 30, 2012, we will have 27,713,354 shares of common stock outstanding after this offering. Of these shares, the common stock sold in our initial public offering and the common stock sold in this offering will be freely tradable in the United States, except for any shares purchased by our affiliates as defined in Rule 144 under the Securities Act of 1933, as amended. The holders of 883,290 shares of outstanding common stock have agreed with us or the underwriters, subject to certain exceptions, not to dispose of or hedge any of their common stock during the 180-day period beginning on the date of our initial public offering prospectus, except with the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated. After the expiration of the 180-day restricted period, these shares may be sold in the public market in the United States, subject to prior registration in the United States, if required, or reliance upon an exemption from U.S. registration, including, in the case of shares held by affiliates or control persons, compliance with the volume restrictions of Rule 144. In addition, the holders of 12,822,539 shares of outstanding common stock have agreed with us or the underwriters, subject to certain exceptions, not to dispose of or hedge any of their common stock during the 90-day period beginning on the date of this prospectus, except with the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated. After the expiration of the 90-day restricted period, these shares may be sold in the public market in the United States, subject to prior registration in the United States, if required, or reliance upon an exemption from U.S. registration, including, in the case of shares held by affiliates or control persons, compliance with the volume restrictions of Rule 144.

Number of Shares**and % of Total****Outstanding****Date Available for Sale into Public Markets**

14,007,525 or 50.5%

Immediately after this offering.

883,290 or 3.2%

November 6, 2012, which is the day after 180 days following the date of our initial public offering prospectus, due to contractual obligations and lock-up agreements between the holders of these shares and us or the underwriters. However, the underwriters may waive the provisions of these lock-up agreements and allow these stockholders to sell their shares at any time, provided their respective six-month holding periods under Rule 144 have expired.

12,822,539 or 46.3%

90 days after the date of this prospectus due to contractual obligations and lock-up agreements between the holders of these shares and us or the underwriters. However, the underwriters may waive the provisions of these lock-up agreements and allow these stockholders to sell their shares at any time, provided their respective six-month holding periods under Rule 144 have expired.

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Upon completion of this offering, stockholders owning an aggregate of 17,240,809 shares (including shares issuable upon the exercise of all warrants) will be entitled, under agreements providing for registration rights, to require us to register shares of our common stock owned by them for public sale in the United States. In addition, we filed a registration statement to register approximately 6,029,556 shares reserved for future issuance under our equity compensation plans. Subject to the satisfaction of applicable exercise periods and, in certain cases, lock-up agreements with the representatives of the underwriters referred to above, the shares of common stock issued upon exercise of outstanding options became available for immediate resale in the United States in the open market.

Sales of our common stock, as restrictions end or pursuant to registration rights, may make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. These sales also could cause our stock price to fall and make it more difficult for you to sell shares of our common stock.

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

Our amended and restated certificate of incorporation, amended and restated bylaws and Delaware law contain provisions that could have the effect of delaying, preventing or rendering more difficult an acquisition of us if such acquisition is deemed undesirable by our board of directors. Our corporate governance documents include provisions that:

create a classified board of directors whose members serve staggered three-year terms;

authorize blank check preferred stock, which could be issued by the board of directors without stockholder approval and may contain voting, liquidation, dividend and other rights superior to our common stock;

limit the ability of our stockholders to call and bring business before special meetings;

limit the ability of stockholders to act by written consent to such periods during which VantagePoint Capital Partners and its affiliates hold 40% or more of our outstanding common stock;

require advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;

control the procedures for the conduct and scheduling of board of directors and stockholder meetings; and

provide the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

These provisions, alone or together, could delay or prevent unsolicited takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock.

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

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

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

Our management will have broad discretion over the use of the proceeds we receive in this offering and might not apply the proceeds in ways that increase the value of your investment.

Our management will have broad discretion in the application of the net proceeds of this offering. We cannot specify with certainty the uses to which we will apply these net proceeds. The failure by our management to apply these funds effectively could adversely affect our ability to continue to maintain and expand our business and adversely affect the price of our common stock.

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

We do not anticipate declaring any cash dividends to holders of our common stock in the foreseeable future. In addition, our existing credit facility prohibits us from paying cash dividends, and any future financing agreements may prohibit us from paying any type of dividends. Consequently, investors may need to rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investment. Investors seeking cash dividends should not purchase our common stock.

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INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This prospectus includes forward-looking statements that relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Words such as, but not limited to, believe, expect, anticipate, estimate, intend, plan, targets, likely, will, would, could, and phrases, or the negative of those expressions or phrases, identify forward-looking statements.

Although we believe that we have a reasonable basis for each forward-looking statement contained in this prospectus, we caution you that these statements are based on our projections of the future that are subject to known and unknown risks and uncertainties and other factors that may cause our actual results, level of activity, performance or achievements expressed or implied by these forward-looking statements, to differ. The sections in this prospectus entitled *Risk Factors*, *Management's Discussion and Analysis of Financial Condition and Results of Operations* and *Business*, as well as other sections in this prospectus, discuss some of the factors that could contribute to these differences.

Other unknown or unpredictable factors could also harm our results. Consequently, actual results or developments anticipated by us may not be realized or, even if substantially realized, may not have the expected consequences to, or effects on, us. Given these uncertainties, prospective investors are cautioned not to place undue reliance on such forward-looking statements. Except as required by law, we undertake no obligation to update or revise publicly any of the forward-looking statements after the date of this prospectus.

You may rely only on the information contained in this prospectus. Neither we nor any of the underwriters have authorized anyone to provide information different from that contained in this prospectus. Neither the delivery of this prospectus, nor sale of common stock, means that information contained in this prospectus is correct after the date of this prospectus. This prospectus is not an offer to sell or solicitation of an offer to buy shares of common stock in any circumstances under which the offer or solicitation is unlawful.

MARKET, INDUSTRY AND OTHER DATA

Unless otherwise indicated, information contained in this prospectus concerning our industry and the markets in which we operate, including our general expectations and market position, market opportunity and market size, is based on information from various sources, on assumptions that we have made that are based on those data and other similar sources and on our knowledge of the markets for our services. These data involve a number of assumptions and limitations. We have not independently verified the accuracy of any third party information. In addition, projections, assumptions and estimates of our future performance and the future performance of the industry in which we operate is necessarily subject to a high degree of uncertainty and risk due to a variety of factors, including those described in *Risk Factors* and elsewhere in this prospectus. These and other factors could cause results to differ materially from those expressed in the estimates made by the independent parties and by us.

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USE OF PROCEEDS

We estimate that our net proceeds from the sale of shares of our common stock in this offering will be approximately \$15,765,752, based on the public offering price of \$17.50 per share, and after deducting underwriting discounts and commissions and estimated offering expenses that we must pay in connection with this offering. We will not receive any proceeds from the sale of shares of common stock by the selling stockholders, other than \$1,550,633 representing the exercise price of the warrants in connection herewith. We will bear the costs, other than the underwriting discounts and commissions, associated with the sale of shares of common stock by the selling stockholders.

The principal purposes of this offering are to facilitate an orderly distribution of shares for the selling stockholders, to increase our public float and to raise additional capital.

We cannot specify with certainty the particular uses for the net proceeds to be received by us from this offering. Accordingly, our management team will have broad discretion in using the net proceeds to be received by us from this offering. We currently intend to use the net proceeds received by us from this offering for working capital and general corporate purposes, including further expansion of our sales and marketing efforts, continued investments in technology and development and for capital expenditures. Specifically, we intend to hire additional personnel to support the growth in our business. In addition, we may use a portion of the proceeds received by us from this offering for portfolio purchases of complementary businesses, technologies or assets to expand our employer client base. We have no agreements with respect to any portfolio purchases at this time.

Pending such uses, we plan to invest the net proceeds in short- and intermediate-term, interest-bearing obligations, investment-grade instruments, certificates of deposit or direct or guaranteed obligations of the U.S. government.

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MARKET PRICE OF COMMON STOCK

Our common stock has been listed on the New York Stock Exchange, or the NYSE, under the symbol WAGE since May 10, 2012. Prior to that date, there was no public trading market for our common stock. The following table sets forth for the periods indicated the high and low sales prices per share of our common stock as reported on the NYSE:

	High	Low
Second Quarter (from May 10, 2012)	\$ 15.40	\$ 9.75
Third Quarter	\$ 18.87	\$ 12.36
Fourth Quarter (through October 3, 2012)	\$ 18.69	\$ 17.24

On October 3, 2012, the last reported sale price of our common stock on the NYSE was \$18.24 per share. As of June 30, 2012, we had 109 holders of record of our common stock. The actual number of stockholders is greater than this number of record holders, and includes stockholders who are beneficial owners, but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

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DIVIDEND POLICY

We have never declared or paid any cash dividend on our capital stock. We currently intend to retain any future earnings and do not expect to pay any dividends in the foreseeable future. Any determination to pay dividends in the future will be at the discretion of our board of directors and will be dependent on a number of factors, including our earnings, capital requirements and overall financial conditions. Currently, our credit facility with Union Bank, N.A. prohibits our payment of any dividends without obtaining its prior written consent, other than dividends payable solely in our common stock.

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The table below sets forth our cash and cash equivalents and capitalization as of June 30, 2012 on:

an unaudited actual basis; and

an as adjusted basis, after giving effect to the sale by us of 1,000,000 shares of common stock in this offering based on the public offering price of \$17.50 per share, after deducting the underwriting discounts and commissions and estimated offering expenses payable by us, and the sale of shares of common stock by the selling stockholders (including \$1,550,633 representing the exercise price of the warrants that we expect to be exercised concurrently with the consummation of this offering).

You should read this table together with our consolidated financial statements and the related notes thereto, as well as the information under *Management's Discussion and Analysis of Financial Conditions and Results of Operations*.

	As of June 30, 2012	
	Actual (unaudited) (in thousands, except share and per share data)	Adjusted (unaudited)
Cash and cash equivalents	\$ 261,340	\$ 278,656
Bank borrowings	44,560	44,560
Stockholders' equity:		
Common stock, \$0.001 par value; authorized 1,000,000,000 shares, actual and as adjusted; issued, 26,713,354 shares actual; issued, 27,713,354 shares as adjusted	27	28
Treasury stock	(463)	(463)
Additional paid-in capital	194,593	211,908
Accumulated deficit	(69,386)	(69,386)
Total stockholders' equity	124,771	142,087
Total capitalization	\$ 169,331	\$ 186,647

The outstanding share information in the capitalization table above is based on the number of shares outstanding as of June 30, 2012, and excludes:

5,242,621 shares of common stock issuable upon the exercise of options outstanding as of June 30, 2012, at a weighted average exercise price of \$7.68 per share;

75,000 shares of common stock issuable upon the exercise of a warrant outstanding as of June 30, 2012 to purchase common stock, at an exercise price of \$8.20 per share;

4,578,567 shares of common stock issuable upon the exercise of warrants outstanding as of June 30, 2012 to purchase common stock, at a weighted average exercise price of \$4.76 per share (including 338,566 shares of common stock that we expect to be sold in this offering upon the exercise of outstanding warrants); and

195,048 shares of common stock reserved for future issuance under our 2010 Equity Incentive Plan as of June 30, 2012.

Table of Contents**SELECTED CONSOLIDATED FINANCIAL INFORMATION**

The following selected consolidated financial data should be read together with *Management's Discussion and Analysis of Financial Condition and Results of Operations* and our audited consolidated financial statements and related notes included elsewhere in this prospectus. The selected consolidated balance sheet data as of December 31, 2010 and 2011, and the selected consolidated statements of operations data for each of 2009, 2010 and 2011 have been derived from our audited consolidated financial statements, which are included elsewhere in this prospectus. The selected consolidated balance sheet data as of December 31, 2007, 2008 and 2009 and the selected consolidated statements of operations data for each of 2007 and 2008 have been derived from our audited consolidated financial statements not included in this prospectus. The unaudited selected consolidated balance sheet data as of June 30, 2012 and the unaudited selected consolidated statement of operations data for the six months ended June 30, 2011 and 2012 are derived from our unaudited interim consolidated financial statements included elsewhere in this prospectus. The unaudited interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and, in our opinion, reflect all adjustments necessary for the fair presentation of the financial information set forth in those statements. Historical results are not necessarily indicative of the results to be expected in the future and our interim results are not necessarily indicative of the results to be expected for the full fiscal year or any other period.

	2007	Year Ended December 31,				Six Months Ended June 30,	
	2008	2009	2010	2011	2011	2012	
	(in thousands, except per share data)						
	(unaudited)						
Consolidated Statement of Operations Data:							
Revenues	\$ 89,765	\$ 103,273	\$ 108,461	\$ 115,047	\$ 135,637	\$ 69,185	\$ 88,087
Operating expenses:							
Cost of revenues (excluding amortization of internal use software)	48,459	49,298	46,802	50,205	55,651	28,610	32,677
Sales and marketing, technology and development and general and administration	36,115	49,552	52,792	49,044	55,099	27,863	38,241
Amortization and change in contingent consideration	6,867	7,987	8,398	7,764	11,327	5,175	8,532
Total operating expense	91,441	106,837	107,992	107,013	122,077	61,648	79,450
Income (loss) from operations	(1,676)	(3,564)	469	8,034	13,560	7,537	8,637
Other income (expense):							
Interest income	1,403	1,368	851	220	36	20	19
Interest expense	(2,189)	(1,570)	(1,102)	(188)	(494)	(197)	(857)
Interest expense: amortization of convertible debt			(71)	(21,107)			
Other, net	(643)	(72)	(286)	(5,413)	351	(59)	408
Income (loss) before income taxes	(3,105)	(3,838)	(139)	(18,454)	13,453	7,301	8,207
Income tax (provision) benefit	(315)	(487)	(495)	1,204	19,868	(401)	(2,973)
Net income (loss)	(3,420)	(4,325)	(634)	(17,250)	33,321	6,900	5,234
Accretion of redemption premium (expense) benefit	(3,837)	(3,130)	1,037	(6,740)	(6,209)	(5,692)	(2,301)
Net income (loss) attributable to common stockholders	\$ (7,257)	\$ (7,455)	\$ 403	\$ (23,990)	\$ 27,112	\$ 1,208	\$ 2,933
Net income (loss) per share attributable to common stockholders:							
Basic	\$ (4.82)	\$ (4.45)	\$ 0.25	\$ (15.70)	\$ 17.65	\$ 0.79	\$ 0.37
Diluted	\$ (4.82)	\$ (4.45)	\$ (0.04)	\$ (15.70)	\$ 1.43	\$ 0.07	\$ 0.13
Weighted average shares:							
Basic	1,505	1,674	1,606	1,528	1,536	1,534	7,907
Diluted	1,505	1,674	16,864	1,528	20,086	16,376	20,683

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	2007	2008	At December 31,		2011	At June 30,
			2009	2010		2012
			(in thousands)			(unaudited)
Consolidated Balance Sheet Data:						
Cash and cash equivalents	\$ 49,978	\$ 72,102	\$ 93,261	\$ 104,280	\$ 154,621	\$ 261,340
Total current assets	72,657	90,704	108,515	124,337	179,829	294,730
Total assets	138,144	159,615	171,478	206,831	278,696	442,201
Total current liabilities	120,763	145,004	153,303	167,648	215,645	308,006
Total liabilities	143,869	167,892	167,430	182,254	218,584	317,430
Total redeemable convertible preferred stock	45,950	49,080	48,043	75,960	82,169	
Total stockholders' equity (deficit)	(51,675)	(57,357)	(43,995)	(51,383)	(22,057)	124,771

	2007	Year Ended December 31,				Six Months Ended	
		2008	2009	2010	2011	2011	June 30,
							2012
			(in thousands)				
Non-GAAP Financial Data:							
Adjusted EBITDA(1) (unaudited)	\$ 8,867	\$ 10,752	\$ 15,941	\$ 22,366	\$ 30,330	\$ 15,655	\$ 20,316

- (1) We define Adjusted EBITDA as net income (loss), calculated in accordance with GAAP, plus: (i) depreciation; (ii) amortization and change in contingent consideration; (iii) stock-based compensation expense; (iv) interest expense (income), net; (v) income tax (benefit) provision; (vi) interest expense: amortization of convertible debt discounts; (vii) loss (gain) on revaluation of warrants; and (viii) loss on extinguishment of debt.

Adjusted EBITDA is not a recognized presentation in accordance with GAAP. An explanation of the elements of Adjusted EBITDA, a full reconciliation of net income (loss), which is the most directly comparable GAAP measure to Adjusted EBITDA, and the material limitations of Adjusted EBITDA are set forth below. Adjusted EBITDA should not be considered as an alternative to net income, income from operations or any other measure of financial performance calculated and presented in accordance with GAAP. Our Adjusted EBITDA may not be comparable to similarly titled measures of other companies because other companies may not calculate Adjusted EBITDA or similarly titled measures in the same manner that we do. We prepare Adjusted EBITDA to eliminate the impact of items that we do not consider indicative of our core operating performance. We encourage you to evaluate these adjustments and the reasons we consider them appropriate.

Our management uses Adjusted EBITDA:

as a measure of operating performance;

as a factor when determining management's compensation;

for planning purposes, including the preparation of our annual operating budget;

to allocate resources of our business; and

to evaluate the effectiveness of our business strategies.

We believe that the use of Adjusted EBITDA as an operational performance metric provides greater consistency and comparability with our past financial performance and facilitates period-to-period comparisons of our operating results by management and investors. Although calculation of Adjusted EBITDA may vary from company-to-company, our presentation of Adjusted EBITDA may facilitate analysis and comparison of our operating results by management and investors with other peer companies that may use similar non-GAAP financial measures to supplement their GAAP results in their public disclosures. While we believe Adjusted EBITDA is a useful measure for our management and investors in

evaluating our operating performance and business trends, there are material limitations to the use of Adjusted EBITDA. For a further discussion of these limitations, see below in this footnote.

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We believe that it is useful to exclude non-cash charges for depreciation, amortization and change in contingent consideration, amortization of convertible debt discounts, loss (gain) on revaluation of warrants, losses associated with the extinguishment of debt and stock-based compensation from Adjusted EBITDA because (i) the amount of such non-cash expenses in any specific period may not directly correlate to the underlying operational performance of our business and (ii) such expenses can vary significantly between periods as a result of new acquisitions, full amortization of previously acquired intangible assets, full amortization of convertible debt discounts or the timing of new stock-based awards.

Depreciation, amortization and change in contingent consideration. We believe that it is useful to exclude depreciation, amortization and change in contingent consideration from Adjusted EBITDA because depreciation is a function of our capital expenditures, while amortization and change in contingent consideration reflect other asset acquisitions and their associated costs made at a prior point or points in time. In analyzing the performance of our business currently, management believes it is helpful to also consider the business without taking into account costs or benefits accruing from historical decisions on infrastructure and capacity. While these expense and related investments affect the overall financial health of our company, they are separately evaluated and relate to historic decisions. Further, depreciation and amortization do not result in ongoing cash expenditures. Investors should note that the use of assets being depreciated or amortized contributed to revenues earned during the periods presented and will continue to contribute to future period revenues. This depreciation and amortization expense will recur in future periods for GAAP purposes.

Losses (gains) associated with the revaluation of warrants. We believe that it is useful to exclude losses (gains) associated with the revaluation of warrants from Adjusted EBITDA. These items vary significantly in size and amount and are excluded by our management when evaluating and predicting earnings trends because these charges are based on many subjective inputs at a point in time and many of these inputs are not necessarily directly related to the performance of our business. Due to subjective assumptions that underlie valuation methodologies used in the calculation, as well as the impact of non-operational factors such as our share price, on the magnitude of this expense, management excludes these gains or losses when evaluating the ongoing performance of our business.

Losses associated with the extinguishment of debt and amortization of convertible debt discount. We believe that it is useful to exclude losses associated with the extinguishment of debt and amortization of convertible debt discount from Adjusted EBITDA. These items vary significantly in size and amount and are excluded by our management when evaluating and predicting earnings trends because these charges are unique to specific financings. We, therefore, exclude these cash and non-cash charges when presenting Adjusted EBITDA.

Stock-based compensation expense. We believe that it is useful in evaluating our financial performance to exclude stock-based compensation expense from Adjusted EBITDA because non-cash equity grants made at various points in time based on the value of our stock do not necessarily reflect how our business is performing at any particular time. While we believe that investors should have information about any dilutive effect of outstanding options and the cost of that compensation, we also believe that investors should have the ability to view Adjusted EBITDA as a non-GAAP financial measure that excludes these costs. The determination of stock-based compensation expense is based on many subjective inputs at a point in time and many of these inputs are not necessarily directly related to the performance of our business. Due to subjective assumptions that underlie valuation methodologies used in the calculation of this expense and the variety of stock award types that companies employ, as well as the impact of non-operational factors, such as our share price, on the magnitude of this expense, management believes that providing Adjusted EBITDA as a non-GAAP financial measure that excludes this stock-based compensation expense allows investors to make meaningful comparisons between our operating results and those of other companies.

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Although Adjusted EBITDA measures are frequently used by investors and securities analysts in their evaluations of companies, Adjusted EBITDA measures each have limitations as an analytical tool, and you should not consider them in isolation or as a substitute for analysis of our results of operations as reported under GAAP.

A number of the material limitations of our use and presentation of Adjusted EBITDA include:

Adjusted EBITDA does not reflect our future requirements for contractual commitments and capital expenditures;

Adjusted EBITDA does not reflect cash interest income or expense;

Adjusted EBITDA does not reflect cash outflows for income taxes;

Adjusted EBITDA does not reflect the stock-based component of employee compensation;

although depreciation and amortization are non-cash charges that are excluded from Adjusted EBITDA, the assets being depreciated or amortized will often have to be replaced in the future, and Adjusted EBITDA does not reflect any current cash requirements for these replacements; and

other companies in our industry may calculate Adjusted EBITDA or similarly titled measures differently from the manner in which we do, limiting their usefulness as comparative measures by our management or investors.

Management addresses the inherent limitations associated with using the Adjusted EBITDA measure through disclosure of such limitations, presentation of our financial statements in accordance with GAAP and reconciliation of the most directly comparable GAAP measure, net income (loss) to Adjusted EBITDA. Further, management also reviews GAAP measures, and evaluates individual measures that are not included in Adjusted EBITDA such as our level of capital expenditures and interest expense, among other items.

The following provides a reconciliation of net income (loss) to Adjusted EBITDA:

	Year Ended December 31,					Six Months Ended	
	2007	2008	2009	2010	2011	2011	2012
	(in thousands, unaudited)						
Net income (loss)	\$ (3,420)	\$ (4,325)	\$ (634)	\$ (17,250)	\$ 33,321	\$ 6,900	\$ 5,234
Depreciation	3,729	4,559	4,564	4,164	3,199	1,744	1,446
Amortization and change in contingent consideration	6,867	7,987	8,398	7,764	11,327	5,175	8,532
Stock-based compensation expense	610	1,770	2,510	2,404	2,244	1,199	1,674
Interest income	(1,403)	(1,368)	(851)	(220)	(36)	(20)	(19)
Interest expense	2,189	1,570	1,102	188	494	197	857
Interest expense: amortization of convertible debt discount			71	21,107			
Income tax provision (benefit)	315	487	495	(1,204)	(19,868)	401	2,973
Loss (gain) on revaluation of warrants	(360)	72	(70)	5,413	(351)	59	(381)
Loss on extinguishment of debt	340		356				
Adjusted EBITDA	\$ 8,867	\$ 10,752	\$ 15,941	\$ 22,366	\$ 30,330	\$ 15,655	\$ 20,316

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**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition and results of operations should be read together with Selected Consolidated Financial Information and our consolidated financial statements and related notes appearing elsewhere in this prospectus. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of a variety of factors, including but not limited to, those set forth under Risk Factors and elsewhere in this prospectus.

Overview

We are a leading on-demand provider of tax-advantaged programs for consumer-directed health, commuter and other employee spending account benefits, or CDBs, in the United States. We administer and operate a broad array of CDBs, including spending account management programs such as health and dependent care Flexible Spending Accounts, or FSAs, Health Savings Accounts, or HSAs, Health Reimbursement Arrangements, or HRAs, and commuter benefits, such as transit and parking programs.

We deliver our CDB programs through a highly scalable Benefits-as-a-Service, or BaaS, delivery model that employer clients and their employee participants may access through a standard web browser on any internet-enabled device including computers, smart phones and other mobile devices, such as tablet computers. Our on-demand delivery model eliminates the need for our employer clients to install and maintain hardware and software in order to support CDB programs and enables us to rapidly implement product enhancements across our entire user base.

Our CDB programs enable employees and their families to save money by using pre-tax dollars to pay for certain of their healthcare and commuter expenses. Employers financially benefit from our programs through reduced payroll taxes, even after factoring in our fees. Under our FSA, HSA and commuter programs, employee participants contribute funds from their pre-tax income to pay for qualified out-of-pocket healthcare expenses not fully covered by insurance, such as co-pays, deductibles and over-the-counter medical products or for commuting costs.

These employee contributions result in savings to both employees and employers. As an example, based on our average employee participant's annual FSA contribution of approximately \$1,400 and an assumed personal combined federal and state income tax rate of 35%, an employee participant will reduce his or her taxes by approximately \$490 per year by participating in an FSA. Our employer clients also realize payroll tax (i.e., FICA and Medicare) savings on the pre-tax contributions made by their employees. In the above FSA example, an employer client would save approximately \$64 per participant per year, even after the payment of our fees.

Under our HRA programs, employer clients provide their employee participants with a specified amount of available reimbursement funds to help their employee participants defray out-of-pocket medical expenses such as deductibles, co-insurance and co-payments. All amounts paid by the employer into HRAs are deductible by the employer as an ordinary business expense and are tax-free to the employee.

Our company was founded in 2000 to provide the administration of tax-free commuter benefits. In early 2003, we expanded our business to include the administration of tax-advantaged healthcare programs with our FSA program. As a result of subsequent portfolio purchases made through 2006, we have broadened our CDB offerings to include HRA, HSA and Consolidated Omnibus Budget Reconciliation Act, or COBRA, programs. In 2007 we purchased MHM Resources, or MHM. The MHM small- and medium-sized business, or SMB, portfolio expanded our existing client base and the MHM technology platform enhanced our service offering to SMBs. Between 2008 and 2010, we made three portfolio purchases that have added to our client base and broadened our opportunities with public sector employers. We completed an additional portfolio purchase in January 2012 and also completed an acquisition in February 2012.

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We market and sell our CDB programs through multiple channels, including direct sales to large enterprises, direct sales and through brokers to SMBs, and direct sales to industry purchasing and affiliate groups. Our enterprise sales force targets Fortune 1000 companies and generates new large account relationships through employer prospecting, consultant relationships and strategic partnerships. Our SMB distribution channel complements our enterprise sales channel. It consists of third-party advisors and institutional brokers that sell our CDB programs along with their own complementary products to SMBs. We also sell our services through group purchasing organizations of industry-specific employers with which we negotiate a standard service contract that covers their member entities. Our sales cycle ranges from two months for SMBs to six to nine months for our large institutional clients.

Our CDB agreements with our larger employer clients, which we refer to as enterprise clients, are typically for three-year terms and provide for monthly fees based on the number of employee participants enrolled in our programs. We price our services based on the estimated number and types of claims, whether payment processing and client support activities will be provided within or outside of the United States, the estimated number of calls to our customer support center and any specific client requirements. Almost all of the healthcare benefit plans we service on behalf of our enterprise clients are subject to contractual minimum monthly billing amounts. Generally, such minimum billing amounts are subject to upward revision on a monthly basis as our employer clients hire new employees who elect to participate in our programs, but generally are not subject to downward revision when employees leave their employers because we continue to administer those former employee participants' accounts for the remainder of the plan year. For our SMB clients, our agreements are typically for one year and the monthly fee remains constant for the year unless there is a 10% or greater increase in the number of employee participants in which case it is subject to upward revision.

Benefit plan years customarily run concurrently with the calendar year and have an open enrollment period that typically occurs at benefit plan year-end during the fourth quarter of the calendar year. Most of our healthcare CDB agreements are executed in the last quarter of the calendar year. Because the signing of our contract often coincides with open enrollment, employer clients are able to offer our CDB programs to their employees during open enrollment for the upcoming benefit year. As a result of this timing, we are able to obtain significant visibility into our healthcare-related revenue early on in each plan year because healthcare benefit plans are administered on an annual basis, contractual revenue is based on the number of participants enrolled in our CDB programs on a per month basis and the minimum number of enrolled participants for the plan year is usually established at the close of the open enrollment period. In contrast to healthcare CDB programs, enrollment in commuter programs occurs on a monthly basis. Therefore, there is less visibility and some variability in commuter revenue from month-to-month, particularly during the summer vacation period when employee participants are less likely to participate in commuter programs for those months.

We offer prepaid debit cards for use in conjunction with almost all of the plans that we administer. These prepaid debit cards are offered in coordination with commercial banks and card associations. We receive interchange fees from employee participants' prepaid debit card transactions, which are calculated as a percentage of the expenses transacted on each card. These interchange fees are exempt from the Durbin Amendment since there is an exception for general purpose reloadable cards and some of such cards also fall outside the definitions that establish the scope of coverage. In addition to interchange fees, we also derive revenue through our wholesale card program from fees we charge to assist third party administrators, or TPAs, in issuing our prepaid debit cards to their employee participant groups and in selling their administrative services utilizing our prepaid debit cards to new employee participants. We have historically experienced seasonality in healthcare interchange revenue, which is typically the highest during the first quarter of the year because participants are either using their newly available balances for the current plan year or spending any remaining funds available from the prior plan year during the prior plan year's grace period. A grace period is generally established by employer clients as January 1 through March 15 of the succeeding plan year and is the period during which employee participants can access funds from the prior plan year's FSA account. Healthcare interchange revenue generally declines through the second and third quarters and is subject to a small increase in December as some employee participants strive to use their remaining account balances before the end of the plan year.

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We also offer transit passes from various transit agencies, which we purchase on behalf of employee participants. Due to our significant volume, we receive commissions on these passes which we recognize as vendor commission revenue.

Our cost of revenues typically varies with our revenue and is, therefore, impacted by the seasonality of our business. We incur higher expenses in the first quarter associated with increased headcount in the form of temporary workers, consultants and other outsourced services that are required to cover the increased call volume and activity associated with the commencement of the new plan year. The need for these resources diminishes in the second and third quarters, but increases again in the fourth quarter when we provide services to our employer clients during their open enrollment periods.

At the beginning of a plan year, most of our enterprise clients provide us with prefunds for their FSA programs based on a percentage of projected elections by the employee participants for the plan year ahead. This prefunding activity covers our estimate of approximately one week of spending on behalf of the employer client's employee participants. During the plan year, we process employee participants' FSA claims as they are submitted and typically seek reimbursement from our employer clients within one week after settling the claim. Employer clients generally set a time after the close of a plan year when employee participants in FSA programs are allowed to continue submitting claims for the preceding plan year, which we refer to as a run-out period. At the end of the plan year and following the grace period and run-out period, as applicable, we reconcile all claims paid against the FSA prefund and return any unused funds to the employer. Prior to that point we will have already received an entirely new FSA prefund from a continuing employer client for the new plan year.

Our growth strategy includes acquiring and integrating smaller TPAs to expand our employer client base. We refer to these acquisitions as portfolio purchases.

Consistent with this acquisition strategy, we have made five portfolio purchases since 2007, which include MHM in September 2007, Creative Benefits, or CB, in September 2008, Planned Benefit Systems, or PBS, in August 2010, the CDB assets of a division of Fringe Benefits Management Company, or FBM, in November 2010, and the assets of The Choice Care Card, LLC, also known as Choice Strategies, or CS, in January 2012. In addition, we completed one acquisition, in which we acquired the operating assets of TransitCenter, Inc. (a business we refer to as TransitChek or TC) in February 2012. These portfolio purchases have enabled us to expand our employer client base, particularly in the SMB and public sector markets, and provided an opportunity to cross-sell additional CDB services to our newly acquired employer clients. The purchases of CB and PBS increased our COBRA service offerings, and the purchase of the FBM portfolio expanded our service capabilities to public sector clients. Our model for these portfolio purchases generally involves a payment at closing of the transaction and contingent payments based on retention of the acquired client accounts and achievement of revenue growth targets. Portfolio purchases may have a material adverse impact on our results of operations, including a potential material adverse impact on our cost of revenues in the short term as we seek to migrate acquired clients to our proprietary technology platforms, typically over the succeeding 12 to 24 months, in order to achieve additional operating efficiencies. There are several hundred regional TPA portfolios that we continually monitor and evaluate in order to maintain a robust pipeline of potential candidates for purchase and we intend to continue executing our focused strategy of portfolio purchases to broaden our employer client base. The acquisition of TC enabled us to further expand our commuter tax-advantaged benefit offerings in the SMB market with products tailored to SMB needs. We believe this acquisition will help solidify our position as a leading provider of commuter-related CDBs.

We monitor our operating results and take steps to improve, redirect and consolidate our operations. In April 2009, we reorganized a number of operational areas to enable key personnel to focus solely on supporting either our healthcare or commuter programs. In addition, we reduced and reorganized our client services team to focus on specific regions. We also took actions to reduce our fixed personnel costs and increase our variable outsourcing costs. These activities have provided us with increased resource flexibility during our seasonal peaks in service delivery. In the first quarter of 2012, we closed our Troy, Michigan facility and consolidated redundant activities within our operations, which resulted in the elimination of certain personnel. The expenses related to these actions were approximately \$0.5 million.

Table of Contents**Adjusted EBITDA**

In addition to traditional financial measures, we monitor our Adjusted EBITDA to help us evaluate the effectiveness and efficiency of our operations. Adjusted EBITDA is not a recognized presentation in accordance with generally accepted accounting principles in the United States, or GAAP. The table immediately following this discussion provides a reconciliation of net income (loss), which is the most directly comparable GAAP measure, to this non-GAAP measure. Adjusted EBITDA should not be considered as an alternative to net income, income from operations or any other measure of financial performance calculated and presented in accordance with GAAP. Our Adjusted EBITDA may not be comparable to similarly titled measures of other companies because other companies may not calculate Adjusted EBITDA or similarly titled measures in the same manner that we do. We prepare Adjusted EBITDA to eliminate the impact of items that we do not consider indicative of our core operating performance. For further discussion on Adjusted EBITDA, see footnote 1 to Selected Consolidated Financial Information.

The following provides a reconciliation of net income (loss) to Adjusted EBITDA:

	Year Ended December 31,			Six Months Ended	
	2009	2010	2011	2011	2012
	(in thousands)				
	(unaudited)				
Net income (loss)	\$ (634)	\$ (17,250)	\$ 33,321	\$ 6,900	\$ 5,234
Depreciation	4,564	4,164	3,199	1,744	1,446
Amortization and change in contingent consideration	8,398	7,764	11,327	5,175	8,532
Stock-based compensation expense	2,510	2,404	2,244	1,199	1,674
Interest income	(851)	(220)	(36)	(20)	(19)
Interest expense	1,102	188	494	197	857
Interest expense: amortization of convertible debt discount	71	21,107			
Income tax provision (benefit)	495	(1,204)	(19,868)	401	2,973
Loss (gain) on revaluation of warrants	(70)	5,413	(351)	59	(381)
Loss on extinguishment of debt	356				
Adjusted EBITDA	\$ 15,941	\$ 22,366	\$ 30,330	\$ 15,655	\$ 20,316

Key Components of Our Results of Operations**Revenue**

We generate revenue from three major sources: healthcare solutions, commuter solutions and other services.

Healthcare Revenue

We derive our healthcare revenue from the service fees paid by our employer clients for the administration services we provide in connection with their employee participants' healthcare FSA, dependent care FSA, HRA and HSA tax-advantaged accounts. Our fee is generally fixed for the duration of the written agreement with our employer client, which is typically three years for our enterprise clients and one year for our SMB clients. These fees are paid to us on a monthly basis by our employer clients, and the related services are made available to employee participants pursuant to written agreements between us and each employer client. Almost all of the healthcare benefit plans we service on behalf of our enterprise employer clients are subject to contractual minimum monthly billing amounts. Generally, such minimum billing amounts are subject to upward revision on a monthly basis as our employer clients hire new employees who elect to participate in our programs, but generally are not subject to downward revision when employees leave their employers because we continue to

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administer those former employee participants' accounts for the remainder of the plan year. For SMB employer clients, the monthly fee remains constant for the plan year unless there is a 10% or greater increase in the number of employee participants in which case it is subject to upward revision. Revenue is recognized monthly as services are rendered under our written service agreements.

We also earn interchange revenue from debit cards used by employee participants in connection with all of our healthcare programs and through our wholesale card program, which we recognize monthly based on reports received from third parties.

Commuter Revenue

We derive our commuter revenue from monthly service fees paid by our employer clients, interchange revenue that we receive from debit cards used by employee participants in connection with our commuter solutions and revenue from the sale of transit passes used in our commuter solutions. Our fees from employer clients are normally paid monthly in arrears based on the number of employee participants enrolled for the month. Most agreements have volume tiers that adjust the per participant price based upon the number of participants enrolled during that month. Revenue is recognized monthly as services are rendered under these written service agreements. We earn interchange revenue from the debit cards used by employee participants in connection with our commuter programs, which we recognize monthly based on reports received from third parties. We also receive commissions from transit passes, which we purchase from various transit agencies on behalf of employee participants. Due to our significant volume, we receive commissions on these passes which we recognize as vendor commission revenue. Commission revenue is recognized on a monthly basis as transactions are placed under written purchase agreements having stipulated terms and conditions, which do not require management to make any significant judgments or assumptions regarding any potential uncertainties.

Revenue from our TC operations is derived from two programs that are similar in size: Basic and Premium. Revenue from the Basic program is based on a percentage of the face value of the transit and parking passes ordered by employer clients and revenue from the Premium program is derived from monthly service fees paid by employer clients. In addition, revenue is recognized on our estimate of passes that will expire unused over the estimated useful life of the passes, as the amounts paid for these passes are nonrefundable to both the employer client and the employee participant.

Other Revenue

We derive other revenue primarily from our provision of COBRA administration services to employer clients for continuation of coverage for participants who are no longer eligible for the employer's health benefits, such as medical, dental, vision, and for the continued administration of the employee participants' HRAs and certain healthcare FSAs. Our agreements to provide COBRA services are not consistently structured and we receive fees based on a variety of methodologies. Other services also include enrollment and eligibility services, employee account administration (i.e., tuition and health club reimbursements) and project-related professional fees. Other services revenue is recognized as services are rendered under our written service agreements.

Costs and Expenses

Cost of Revenues (excluding the amortization of internal use software)

Cost of revenues includes the costs of providing services to our employer clients' employee participants.

The primary component of cost of revenues is personnel and the expenses related to our claims processing, product support and customer service personnel. Cost of revenues includes outsourced and temporary help costs, check/ACH payment processing services, debit card processing services, shipping and handling costs for cards and passes and employee participant communications costs.

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Cost of revenues also includes the losses or gains associated with processing our large volume of transactions, which we refer to as net processing losses or gains. In the normal course of our business, we make administrative and processing errors that we cannot bill to our employer clients. For example, we may over-reimburse employee participants for claims they submit or incur the cost of replacing commuter passes that are not received by employee participants. Upon identifying such an error, we record the expense as a processing loss. In certain circumstances, we experience recoveries with respect to these amounts which are recorded as processing gains.

Cost of revenues does not include amortization of internal use software, which is included in amortization, or the cost of operating on-demand technology infrastructure, which is included in technology and development expenses.

Technology and Development

Technology and development expenses include personnel and related expenses for our technology operations and development personnel as well as outsourced programming services, the costs of operating our on-demand technology infrastructure, depreciation of equipment and software licensing expenses. During the planning and post-implementation phases of development, we expense, as incurred, all internal use software and website development expenses associated with our proprietary scalable delivery model. During the development phase, costs incurred for internal use software are capitalized and subsequently amortized once the software is available for its intended use. See *Amortization and Change in Contingent Consideration* below. Expenses associated with the platform content or the repair or maintenance of the existing platforms are expensed as incurred.

Sales and Marketing

Sales and marketing expenses consist primarily of personnel and related expenses for our sales, client services and marketing staff, including sales commissions for our direct sales force, as well as communication, promotional, public relations and other marketing expenses.

General and Administration

General and administration expenses include personnel and related expenses of and professional fees incurred by our executive, finance, legal, human resources and facilities departments.

Amortization and Change in Contingent Consideration

Amortization and change in contingent consideration expense includes amortization of internal use software, amortization of acquired intangible assets and changes in contingent consideration in connection with portfolio purchases and acquisitions.

We capitalize internal use software and website development costs incurred during the development phase and we amortize these costs over the technology's estimated useful life, which is generally four years. These capitalized costs include personnel costs and fees for outsourced programming and consulting services.

We also amortize acquired intangible assets consisting primarily of employer client agreements and relationships and broker relationships. Employer client agreements and relationships and broker relationships are amortized on a straight-line basis over an average estimated life that ranges from one to eleven years.

We measure acquired contingent consideration payable each reporting period at fair value and recognize changes in fair value in our consolidated statement of operations each period, until the final amount payable is determined. Increases or decreases in the fair value of the contingent consideration payable can result from changes in revenue forecasts and risk and probability assumptions. Significant judgment is employed in determining the appropriateness of these assumptions in each period.

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Other Income (Expense)

Other income (expense) primarily consists of (i) interest income; (ii) interest expense; and (iii) gain (loss) on revaluation of warrants.

Interest Expense: Amortization of Convertible Debt Discount

On December 28, 2009, we entered into a convertible note agreement with several of our existing preferred stockholders. This transaction resulted in a debt discount of \$20.0 million that was fully amortized during 2010. Amortization of convertible debt discount also includes accrued interest on our promissory notes that were converted in July 2010.

Gain (Loss) on Revaluation of Warrants

Preferred warrant liabilities are the result of warrants issued in connection with previous debt financings. We account for freestanding warrants that are exercisable into shares of potentially redeemable preferred stock as liabilities by marking-to-market those warrants at each reporting period from the warrant issuance date until their exercise date or expiration. The changes resulting from marking-to-market are presented in our consolidated statements of operations as gain (loss) on revaluation of warrants. Warrants issued in connection with our 2009 debt financing were modified on July 30, 2010 to be exercisable for Series E-1 preferred shares that are not redeemable. Accordingly, these warrants were reclassified at that date from debt to equity and were no longer subject to mark-to-market changes. Upon the automatic conversion of our preferred stock into common stock in connection with the closing of our initial public offering in May 2012, the warrants became exercisable for shares of common stock. As the warrant is no longer exercisable into shares of redeemable preferred stock, we will no longer record any mark-to-market changes in the fair value of the warrant in the statements of operations.

Provision for Income Taxes

We are subject to taxation in the United States. In 2011, our effective tax rate differed from the statutory rate primarily due to the 2011 release of our valuation allowance on our net deferred tax assets, state taxes and the increases in the contingent payments related to our PBS and FBM acquisitions, which increases are not deductible for tax purposes. Prior to 2011, our effective tax rate differed from the statutory rate primarily due to the valuation allowance on the majority of our net deferred tax assets. For future periods, we expect our effective tax rate to approximate the U.S. federal statutory tax rates before adjusting for the effects of credits and state taxes.

As of December 31, 2011, we had \$47.9 million of federal and \$38.9 million of state net operating loss carryforwards available to offset future taxable income. If not fully utilized, these net operating loss carryforwards will expire beginning in 2023 through 2029 for U.S. federal income tax purposes, and beginning in 2012 through 2031 for state income tax purposes. In addition, we have federal and state research and development credit carryforwards of \$2.6 million and \$1.1 million, respectively. The federal research credit carryforwards expire beginning in the years 2022 through 2031, if not fully utilized. The California research credit carries forward indefinitely. Our ability to utilize net operating loss and tax credit carryforwards in the future may be subject to substantial restriction under applicable law, including in the event of past or future ownership changes as defined in Section 382 of the Internal Revenue Code of 1986, as amended, and similar state law (including in connection with this offering), which ownership changes may be outside of our control.

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. As of June 30, 2012, we remain in a net deferred tax asset position. Valuation allowances are established when necessary to reduce net deferred tax assets to the amount expected to be realized.

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We make estimates and judgments about our future taxable income that are based on assumptions that are consistent with our plans and estimates. Should the actual amounts differ from our estimates, our provision for income taxes could be materially affected.

Accretion of Redemption Premium

We accounted for redemption premium by recording accretion charges reflecting the changes in the redemption value of certain of our series of redeemable preferred stock over the period from the date of issuance to the earliest redemption date. Upon the completion of our initial public offering in May 2012, the redeemable preferred shares converted to common shares that are not redeemable. We performed the final re-measurement of the redeemable preferred stock at the date when redemption was no longer probable and the preferred stock was then reclassified from the mezzanine to equity. We no longer record accretion of redeemable preferred shares.

Critical Accounting Policies and Significant Management Estimates

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles, or GAAP, in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many instances, we could have reasonably used different accounting estimates, and in other instances, changes in the accounting estimates are reasonably likely to occur from period-to-period. Accordingly, actual results could differ significantly from the estimates made by our management. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP and does not require management's judgment in its application, while in other cases, management's judgment is required in selecting among available alternative accounting standards that allow different accounting treatment for similar transactions. We believe that there are several accounting policies that are critical to understanding our business and prospects for future performance, as these policies affect the reported amounts of revenue and other significant areas that involve management's judgment and estimates. These significant policies and our procedures related to these policies are described in detail below. In addition, please refer to the *Notes to Consolidated Financial Statements* for further discussion of our accounting policies.

Revenue Recognition

We report revenue for the following programs: healthcare, commuter and other services.

Healthcare and commuter programs include revenues generated from benefit service fees based on employee participant levels, interchange and other commission fees.

Most of our employee participants utilize prepaid debit cards to pay for their qualified healthcare and commuter expenses and we receive fees, known as interchange, that represent a percentage of the expenses transacted on each card. We also receive commissions from transit passes that we purchase from various transit agencies on behalf of employee participants. Due to our significant volume, we receive commissions on these passes which we recognize as vendor commission revenue. In addition, we recognize revenue on our estimate of passes that will expire unused over the estimated useful life of the passes, as the amounts paid for these passes are nonrefundable to both the employer client and the employee participant.

We recognize revenue when the following criteria are met: collectability is reasonably assured, delivery has occurred, persuasive evidence of an arrangement exists and there is a fixed or determinable fee. These criteria are generally met each month as we deliver services to our employer clients and their employee participants.

Table of Contents***Valuation of Long-Lived Assets***

Long-lived assets, such as property, equipment, acquired intangibles and capitalized internal use software subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable such as: (i) a significant adverse change in the extent or manner in which it is being used or in its physical condition, (ii) a significant adverse change in legal factors or in the business climate that could affect its value, or (iii) a current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with its use.

Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset group to estimated undiscounted future cash flows expected to be generated by the asset group. An asset group is the lowest level at which cash flows can be identified that are largely independent of the cash flows of other asset groups. If the carrying amount of an asset group exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset group exceeds the fair value of the asset group. With the exception of MHM, we have determined that the entity level is the lowest level at which cash flows can be identified that are largely independent of the cash flows of other assets and liabilities as our revenue is interdependent on the revenue-producing activities and significant shared operating activities of all long-lived assets. The entity level is the aggregation of our three revenue streams arising from the administration of employer client sponsored healthcare programs, commuter programs and other programs. In addition to the undiscounted future cash flows expected to be generated at an entity level, we also consider other available information such as our total enterprise value determined for the purpose of estimating the fair value of our common stock, as further discussed below, in assessing the fair value of the entity level asset group. We have identified the long-lived assets of MHM as a separate asset group because we believe that the financial information available is sufficient to determine the cash inflows and outflows of certain MHM assets. Management evaluates the remaining useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets. We recorded impairment adjustments of \$345,000, \$120,000 and \$116,000 in 2009, 2010 and 2011, respectively, and no impairment adjustments in the three and six months ended June 30, 2011 or 2012, related to software development costs.

We perform an annual goodwill impairment test on December 31st and more frequently if events and circumstances indicate that the asset might be impaired. The impairment tests are performed in accordance with FASB ASC 350, *Intangibles - Goodwill and Other*, or ASC 350. An impairment loss is recognized to the extent that the carrying amount exceeds the reporting unit's fair value. The goodwill impairment analysis is a two-step process: First, the reporting unit's estimated fair value is compared to its carrying value, including goodwill. If we determine that the estimated fair value of the reporting unit is less than its carrying value, we move to the second step to determine the implied fair value of the reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill in a manner similar to a purchase price allocation.

When reviewing goodwill for impairment, we assess whether goodwill should be allocated to operating levels lower than our single operating segment for which discrete financial information is available and reviewed for decision-making purposes. These lower levels are referred to as reporting units. Currently, we aggregate the following three revenue streams, healthcare, commuter and other into a single reporting unit in accordance with ASC 350.

The fair value of our reporting unit was determined using the market approach. In the application of the market approach, we are required to make estimates of future operating trends and judgments on discount rates and other variables. Actual future results related to assumed variables could differ from these estimates. Discount rates are based on a weighted average cost of capital, which represents the average rate a business must pay its

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providers of debt and equity capital. We used discount rates that are the representative weighted average cost of capital for our reporting unit in comparison with peer companies, with consideration given to the current condition of the global economy. We determine projected income based on our best estimate of near term revenue and Earnings before Interest, Income Taxes, Depreciation and Amortization, or EBITDA, expectations and long-term projections. Estimated Adjusted EBITDA for 2011 increased as compared to 2010. As a sensitivity analysis, a 100 basis point reduction in the assumed net sales growth beginning in 2012 would decrease minimally the overall valuation but it would not cause a change in the results of our impairment testing that indicated no impairment of goodwill.

As of the end of our fourth quarter of 2011, the period of our last annual impairment test, the fair value of our reporting unit determined under the market approach exceeded our aggregate carrying value by a significant amount. To date, we have not made any impairment adjustments to goodwill as the fair value of our reporting unit has always exceeded our carrying value.

Income Taxes

We are subject to income taxes in the United States. Significant judgments are required in determining the consolidated provision for income taxes.

We use the asset and liability method to account for income taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and net operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. We record a valuation allowance to reduce deferred tax assets to an amount whose realization is more likely than not.

During the ordinary course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. As a result, we recognize tax liabilities based on estimates of whether additional taxes and interest will be due. These tax liabilities are recognized when, despite the belief that our tax return positions are supportable, we believe that certain positions may not be more likely than not of being sustained upon review by tax authorities. As of December 31, 2011, our unrecognized tax benefits approximated \$2.3 million, and we have no uncertain tax positions that would be reduced as a result of a lapse of the applicable statute of limitations. We believe that our accruals for tax liabilities are adequate for all open audit years based on our assessment of many factors, including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events. We do not anticipate any adjustments would result in a material change to our financial position. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact income tax expense in the period in which such determination is made. We recognize accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense.

Management periodically evaluates if it is more likely than not that some or all of the deferred tax assets will be realized. In making such determination, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial performance. In order to support a conclusion that a valuation allowance is not needed, positive evidence of sufficient quantity and quality (objective compared to subjective) is necessary to overcome negative evidence. During 2009 and 2010, management determined there was significant negative evidence and concluded that it was more likely than not that the net deferred tax assets would not be realized and accordingly established a valuation allowance on our deferred tax asset balance. The last two quarters of 2010 were profitable, but the lack of profitability in prior years is a significant piece of negative evidence and generally

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precludes management's estimate of forecasted future taxable income as positive evidence in its assessment. As a result, a valuation allowance on our deferred tax asset balance was recognized for the net deferred tax assets as of December 31, 2010.

In the fourth quarter of 2011, we determined that the positive evidence of taxable income coupled with our forecasted profitability outweighed the negative evidence of prior losses. We deferred action on the release of the valuation allowance until later in the fourth quarter of 2011 when we had visibility into our 2012 enrollment levels, including enrollment and a full year of results from our 2010 portfolio purchases. We believe this information provides the basis for reliable forecasts of our 2012 pre-tax income due to the fixed monthly fees that form the majority of our revenue. Accordingly, in the fourth quarter of 2011, we released the valuation allowance on our deferred tax assets of \$25.9 million, primarily related to our federal deferred tax assets.

In the future, if there is a significant negative change in our operating results or the other factors that were considered in making this determination, we could be required to record a valuation allowance against our deferred tax assets. Any subsequent increases in the valuation allowance will be recognized as an increase in deferred tax expense. Any decreases in the valuation allowance will be recorded either as a reduction of the income tax provision or as a credit to paid-in capital if the associated deferred tax asset relates to windfall stock option deductions on the exercise of stock options.

Stock-Based Compensation

Stock-based compensation for stock awards is estimated at the grant date based on the award's fair value as calculated by the Black-Scholes option pricing model and is recognized as an expense over the requisite service period. The determination of the fair value of stock-based awards on the date of grant using an option pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables. These variables include our expected stock price and related volatility over the expected term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate, estimated forfeitures and expected dividends. The following table sets forth the assumptions made with respect to these issues during 2009, 2010 and 2011 and the first six months of 2012.

	2009	December 31, 2010	2011	June 30, 2012 (unaudited)
Expected term (in years)	4.95-6.06	5.26-8.50	5.47-6.08	5.27-8.50
Risk-free interest rate	2.13-2.72%	1.13-3.12%	2.18-2.72%	0.94-1.74%
Expected volatility	47.0%	46.0-50.9%	54.72-56.09%	54.63-56.14%
Dividend yield	0.00%	0.00%	0.00%	0.00%

We changed our method of estimating expected term in 2010 from using historical and observed exercises to using the simplified method as an estimate of expected term. We based the risk-free interest rate on zero-coupon yields implied from U.S. Treasury issues with remaining terms similar to the expected term on the options. We estimate expected volatility based on the historical volatility of comparable companies from a representative peer-group. We do not anticipate paying any cash dividends in the foreseeable future, and therefore, used an expected dividend yield of zero in the option pricing model. We are required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. We true-up our forfeitures monthly to vested amounts. If we use different assumptions for estimating stock-based compensation expense in future periods, or if actual forfeitures differ materially from our estimated forfeitures, future stock-based compensation expense may differ significantly from what we have recorded in the current period and could materially affect our income (loss) from operations, net income (loss) and net income (loss) per share.

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Since the completion of our initial public offering in May 2012, we have determined our stock price based on the closing price at the date of grant. Prior to the completion of our initial public offering, our stock price at any given time was determined by our board of directors, which considered numerous objective and subjective factors at each option grant date, including the following:

contemporaneous valuations performed by an independent valuation firm, generally as of specified dates;

prices for our preferred stock sold to outside investors in arms-length transactions, and the rights, preferences and privileges of our preferred stock and our common stock;

secondary sales of shares of our common stock, if any;

our actual financial condition and results of operations relative to our operating plan during the relevant period;

forecasts of our financial results and overall market conditions; and

the likelihood of achieving a liquidity event for the shares of common stock underlying the options such as an initial public offering or sale of the company, or remaining a private company, given prevailing market conditions at the time of grant.

Our board of directors believes that the judgment required in such efforts necessarily involves an element of subjectivity.

Valuations performed by the independent valuation firm were conducted in accordance with methods specified by the AICPA Practice Aid on *Valuation of Privately-Held Company Equity Securities Issued as Compensation*. The valuations performed by the independent valuation firm used the Probability Weighted Expected Result Method, or PWERM, to arrive at a weighted equity value. The PWERM methodology requires the consideration of various liquidity scenarios, including an initial public offering and a sale of our company, as well as continuing as a standalone privately-held company, and takes into account potential timing and the relative probability of each possible outcome. The probabilities for each outcome were based on discussions with management. The PWERM was also used to allocate the value among the various issues of preferred shares and considered differences between our preferred and common stock with respect to liquidation preferences, conversion rights, voting rights and other features. The valuations used in the PWERM allocation primarily considered the public company market multiple method. The public company market multiple method focuses on comparing our company to similar publicly traded entities. The valuations for June 30, 2010 and prior also used the income approach as a weighted factor in valuing the standalone scenario. The income approach involves applying appropriate risk-adjusted discount rates to estimated debt-free cash flows, based on forecasted revenues and costs. The discount rate applied to our cash flows was based on a weighted average cost of capital, which represents the blended, after-tax costs of debt and equity. The projections used in connection with these valuations were based on our expected operating performance over the forecast period. Beginning with its December 31, 2010 valuation report, our independent valuation appraiser noted that the use of the market approach was a more appropriate valuation methodology than the income approach based on the anticipated timing of our planned initial public offering. The valuation appraiser determined that the increased probability of an initial public offering scenario in the relatively near term was indicative of our anticipated time to exit being substantially less than the period used for a discounted cash flow analysis under the income approach. The market approach was corroborated by the implied enterprise value from the PWERM.

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We considered appropriate adjustments in light of the lack of marketability of shares of our common stock and calculated our results based upon variables for cost of capital (20-25%). The following table summarizes the concluded discount for lack of marketability as of the valuation dates noted:

Valuation Date	Discount for Lack of Marketability	Value per Share of Common Stock
As of December 31, 2008	15.0%	\$ 6.14
As of June 30, 2009	15.0	7.42
As of December 31, 2009	11.7	5.32
As of June 30, 2010	9.6	6.18
As of December 31, 2010	12.4	10.98
As of March 31, 2011	9.5	12.10
As of June 30, 2011	7.0	12.84
As of December 31, 2011	10.1	9.59
As of March 31, 2012	8.1	10.53

No other discounts were applied to arrive at the fair value amount, other than the lack of marketability discount discussed above.

The following table summarizes the number of options granted and the value of the common stock at each grant date:

Grant Date	Number of Shares Underlying Options Granted	Exercise Price per Share	Common Stock Fair Value per share at Grant Date	Intrinsic Value per Share at Grant Date	Weighted Average Stock Option Fair Value at Grant Date
May 7, 2009	155,250	\$ 6.14	\$ 6.14		\$ 2.64
May 29, 2009	592,875	6.14	6.14		2.66
November 4, 2009	68,750	7.42	7.42		3.58
December 15, 2009	107,500	7.42	7.42		3.58
April 1, 2010	39,375	5.32	5.32		2.62
May 6, 2010	757,375	5.32	5.32		2.70
August 24, 2010	41,255	6.18	6.18		2.79
November 4, 2010	299,250	6.18	6.18		3.38
February 15, 2011	106,250	10.98	10.98		5.98
May 5, 2011	32,375	12.10	12.10		6.42
February 9, 2012	791,875	9.59	9.59		5.34

If we assumed a 100 basis point change, but not below zero, in the following assumptions or a one-year change in the expected life, the value of stock option grants in 2011 would increase (decrease) by the following percentages:

	+100 Basis Points	-100 Basis Points
Expected life	4.1%	(4.5)%
Expected volatility	1.2%	(1.2)%
Risk-free interest rate	2.8%	(2.7)%

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At each option grant date, our board of directors considers the most recent contemporaneous valuation from an independent third party valuation report. Our board considers the shelf life of that valuation as provided in the AICPA Practice Aid on Valuation of Privately-Held-Company Equity Securities Issued as Compensation. The significant factors considered in determining the valuation of common stock at the option grant dates were as follows:

May 7, 2009 and May 29, 2009 grant dates

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of December 31, 2008. The decline in fair value at December 2008 to \$6.14 per common share was primarily due to the significant decline in general economic and financial conditions, as reflected by the declines in gross domestic product, or GDP, in the fourth quarter of 2008 and was also attributable to our decision to postpone our initial public offering and therefore decrease its weighting in valuing our common stock. Our board considered the independent valuation at December 31, 2008 and reviewed and considered that valuation along with other relevant factors it deemed important in each valuation, including:

our interim activity and operating and financial performance for the period from January 1, 2009 to May 1, 2009;

general economic conditions and the specific outlook for our industry;

the likelihood of achieving different liquidity events or remaining a private company; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of December 31, 2008. Accordingly, our board determined the December 31, 2008 valuation (\$6.14) to be the fair value of our common stock for the May 2009 grants.

November 4, 2009 and December 15, 2009 grant dates

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of June 30, 2009. The increase in fair value at June 2009 to \$7.42 per common share was due to the recovery in the public market following the significant decline in the general economic and financial conditions in the fourth quarter of 2008. Our board considered the most recent available independent valuation at June 30, 2009 along with other relevant subjective factors, including:

our operating and financial performance and interim activity for the period from July 1, 2009 through November 1, 2009 and December 1, 2009, respectively;

general economic conditions and the specific outlook for our industry,

the likelihood of achieving different liquidity events or remaining a private company; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of June 30, 2009. Accordingly, our board determined the June 30, 2009 valuation (\$7.42) to be the fair value of our common stock for the November and December 2009 grants.

April 1, 2010 and May 6, 2010 grant dates

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Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of December 31, 2009. In December 2009, substantial improvement in the stock market increased the liquidity strategy values and we showed a year-over-year value increase in value of total weighted equity; however, we had a \$20 million convertible debt financing that was treated as dilutive for valuation purposes and

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reduced the per common share fair value to \$5.32. Economic conditions were flat for the period December 2009 through May 2010 and economic reports were mixed with strong recoveries predicted but considerable debate and disagreement over sustainability. Our board considered the most recent available independent valuation as of December 31, 2009 along with other relevant factors, including:

our operating and financial performance for the period from January 1, 2010 through April 1, 2010 and May 1, 2010, respectively;

general economic conditions, including the improvement in the public market and the specific outlook for our industry;

the likelihood of achieving different liquidity events; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of December 31, 2009. Accordingly, our board determined the December 31, 2009 valuation (\$5.32) to be the fair value of our common stock for the May 2010 grants.

August 24, 2010 and November 4, 2010 grant dates

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of June 30, 2010. The increase in value to \$6.18 from December 31, 2009 to June 30, 2010 was primarily the result of growth in operating profits and Adjusted EBITDA as well as increased weighting of a potential initial public offering. Our board again considered the most recent independent valuation available as of June 30, 2010 along with other relevant objective and subjective factors, including:

our operating and financial performance for the period from July 1, 2010 through August 1, 2010 and November 1, 2010, respectively;

general economic conditions, noting that for the one-month period ending August 1, 2010 and four-month period ending November 1, 2010 the public market was flat;

the specific outlook for our industry and the likelihood of achieving different liquidity events or remaining a private company; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of June 30, 2010. Accordingly, our board determined the June 30, 2010 valuation (\$6.18) to be the fair value of our common stock for the August 2010 and November 2010 grants.

February 15, 2011 grant date

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of December 31, 2010. The valuation showed an increase in value from the June 30, 2010 valuation to \$10.98 per share. The increase as of December 31, 2010, was due in part to the acquisition of FBM in December leading to our increased penetration into the public sector market and the increased weighting of a potential initial public offering in the valuation. The increase in the initial public offering scenario weighting was due to management and our board taking steps towards readying us for an initial public offering. Those steps included the holding of a pre-initial public offering organizational meeting in mid-December, and the initiation of the preparation of an offering document. Our board considered the most recent available independent valuation as December 31, 2010 along with other relevant factors, including:

general economic conditions and the specific outlook for our industry;

the proximity of the grant date of February 15, 2011;

the increased likelihood of achieving an initial public offering noted above; and

significant events or changes at our company.

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Our board determined there were no significant changes in relevant factors since the valuation date of December 31, 2010. Accordingly, our board determined the December 31, 2010 valuation (\$10.98) to be the fair value of our common stock for the February 2011 grants.

May 5, 2011 grant date

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of March 31, 2011. The increase in fair value at March 31, 2011 to \$12.10 per common share from the December 31, 2010 valuation of \$10.98 was primarily due to the increase in the IPO scenario weighting in the valuation. The increase in the initial public offering scenario weighting was due to our moving closer to an initial public offering. Our board considered the independent valuation at March 2011 and reviewed and considered that valuation along with other relevant factors it deemed important in each valuation, including:

our interim activity and operating and financial performance for the period from March 31, 2011 through May 1, 2011;

general economic conditions and the specific outlook for our industry;

the likelihood of achieving different liquidity events or remaining a private company; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of March 31, 2011. Accordingly, our board determined the March 31, 2011 valuation (\$12.10) to be the fair value of our common stock for the May 5, 2011 grants.

February 9, 2012 grant date

Our board obtained a contemporaneously prepared valuation from an independent third party valuation expert as of December 31, 2011. The decline in fair value at December 31, 2011 to \$9.59 per common share from the June 30, 2011 valuation of \$12.84 was primarily due to the decrease in the applicable multiples based upon our public company comparable analysis. Additionally, increases in stock market volatility resulted in an increase in the estimated discount for lack of marketability. Our board considered the independent valuation at December 31, 2011 and reviewed and considered that valuation along with other relevant factors it deemed important in each valuation, including:

our interim activity and operating and financial performance for the period from June 30, 2011 through February 9, 2012;

general economic conditions and the specific outlook for our industry;

the likelihood of achieving different liquidity events or remaining a private company; and

significant events or changes at our company.

Our board determined there were no significant changes in relevant factors since the valuation date of December 31, 2011. Accordingly, our board determined the December 31, 2011 valuation (\$9.59) to be the fair value of our common stock for the February 9, 2012 grants.

Fair Value of Warrants

We record warrants issued in connection with our debt financings based on their fair value on the grant date and adjust quarterly based on a mark-to-market valuation. The change in estimated fair value is classified as Gain (loss) on revaluation of warrants in our consolidated statement

of operations.

In connection with a May 23, 2005 debt financing, we granted a warrant, or the Lender Warrant, to purchase 423,529 shares of Series C preferred stock at a purchase price of \$4.25 per share. The Lender Warrant is classified as a liability on our consolidated balance sheet in accordance with ASC 480. The warrant is exercisable, in whole or

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in part, until the earliest of May 23, 2015 or 18 months after an initial public offering of our common stock. We value the Lender Warrant using an option pricing valuation model, and for 2009-2011 the assumptions were: expected term (1.75 – 3.5 years); risk-free interest rates (0.22% – 1.56%); dividend of 0%; fair value of underlying shares (\$5.14 – \$7.55) and volatility (43.4% – 56.4%). As a result of the completion of our initial public offering in May 2012, the Lender Warrant became exercisable for shares of common stock. As the warrant is no longer exercisable into shares of redeemable preferred stock, the warrant was reclassified from a liability to equity and we will no longer record any mark-to-market changes in the fair value of the warrant in the statements of operations. We performed the final remeasurement of the Lender Warrant at the closing date of our initial public offering on May 15, 2012.

If we assumed a 100 basis point change, but not below zero, in the following assumptions or a one-year change in the expected life, the value of the Lender Warrant would increase (decrease) by the following percentages:

	+100 Basis Points	-100 Basis Points
Expected life	10.5%	(13.7)%
Expected volatility	0.7%	(0.8)%
Risk-free interest rate	1.4%	(0.4)%

In connection with a December 28, 2009 debt financing, we granted warrants, or the Investor Warrants, to purchase \$20 million worth of Series E preferred stock. From December 28, 2009 through July 30, 2010, the Investor Warrants were classified as liabilities on our consolidated balance sheet in accordance with ASC 480 as these warrants are exercisable into redeemable shares. On July 30, 2010, the terms of the Investor Warrants were amended to allow for conversion to Series E-1 preferred stock, which is not redeemable. As a result, the Investor Warrants were reclassified from a liability to equity on July 30, 2010, and changes in the fair value of these warrants have not been recorded in our consolidated statement of operations after the third quarter of 2010. We valued the Investor Warrants from December 28, 2009 through July 30, 2010 using an option pricing valuation model with assumptions that ranged as follows: fair value of the underlying shares (\$3.42 – \$3.98); risk-free interest rates (0.84% – 2.68%); expected term (2.89 – 6.15 years); dividend of 0%; and volatility (48.4% – 66.1%).

Accretion of Redemption Premium

Our redeemable preferred stock was redeemable at the election of the majority of the preferred stock holders on or after December 31, 2012 if a qualified offering, defined as an initial public offering in which net proceeds from the sale of our common stock are \$40 million or greater and the offering price per share is at least \$20.78 (as adjusted for any stock dividends, combinations, or splits with respect to such shares), had not occurred. Prior to the completion of our initial public offering in May 2012, we recorded accretion related to this redemption premium, using the interest method, as an increase or decrease to the liquidation value of the redeemable preferred stock and a decrease or increase to additional paid-in capital based on the excess of the estimated fair value of each redeemable preferred stock over the stated minimum redemption price per share for each redeemable preferred stock over the period of time up to the redemption date. Upon the completion of our initial public offering in May 2012, the redeemable preferred shares converted to common shares that are not redeemable. We performed the final re-measurement of the redeemable preferred stock at the date when redemption was not probable and the preferred stock was then reclassified from the mezzanine to equity. We no longer record accretion of redeemable preferred shares.

Table of Contents**Results of Operations**

The following table sets forth our results of operations for the specified periods:

	Year Ended December 31,			Three Months Ended		Six Months Ended	
	2009	2010	2011	June 30,		June 30,	
	(in thousands)			(in thousands)		(in thousands)	
				(unaudited)		(unaudited)	
Consolidated Statements of Operations Data:							
Revenue:							
Healthcare	\$ 70,718	\$ 75,771	\$ 90,917	\$ 22,854	\$ 27,615	\$ 47,079	\$ 56,845
Commuter	27,603	29,304	33,325	8,382	13,220	16,589	25,212
Other	10,140	9,972	11,395	2,625	2,942	5,517	6,030
Total revenue	108,461	115,047	135,637	33,861	43,777	69,185	88,087
Operating expenses:							
Cost of revenues (excluding amortization of internal use software)	46,802	50,205	55,651	13,244	15,620	28,610	32,677
Technology and development	13,773	12,640	13,526	3,447	4,622	6,939	8,962
Sales and marketing	18,885	18,173	20,697	5,209	7,267	10,458	14,476
General and administration	20,134	18,231	20,876	5,104	7,325	10,466	14,803
Amortization and change in contingent consideration	8,398	7,764	11,327	2,682	4,094	5,175	8,532
Total operating expenses	107,992	107,013	122,077	29,686	38,928	61,648	79,450
Income from operations	469	8,034	13,560	4,175	4,849	7,537	8,637
Other income (expense):							
Interest income	851	220	36	9	9	20	19
Interest expense	(1,102)	(188)	(494)	(111)	(452)	(197)	(857)
Interest expense: amortization of convertible debt discount	(71)	(21,107)					
Loss on extinguishment of debt	(356)						
Gain (loss) on revaluation of warrants	70	(5,413)	351	51	407	(59)	381
Other income					12		27
Income (loss) before income taxes	(139)	(18,454)	13,453	4,124	4,825	7,301	8,207
Income tax (provision) benefit	(495)	1,204	19,868	(253)	(1,601)	(401)	(2,973)
Net income (loss)	(634)	(17,250)	33,321	3,871	3,224	6,900	5,234
Accretion of redemption premium (expense) benefit	1,037	(6,740)	(6,209)	(2,924)	(778)	(5,692)	(2,301)
Net income (loss) attributable to common stockholders	\$ 403	\$ (23,990)	\$ 27,112	\$ 947	\$ 2,446	\$ 1,208	\$ 2,933

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	Year Ended December 31,			Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2010	2011	2011 (unaudited)	2012 (unaudited)	2011 (unaudited)	2012 (unaudited)
Consolidated Statements of Operations Data as a Percentage of Revenue:							
Revenue:							
Healthcare	65%	66%	67%	67%	63%	68%	64%
Commuter	26	25	25	25	30	24	29
Other	9	9	8	8	7	8	7
Total revenue	100	100	100	100	100	100	100
Operating expenses:							
Cost of revenues (excluding amortization of internal use software)	43	44	41	39	36	41	37
Technology and development	13	11	10	10	10	10	10
Sales and marketing	17	16	15	16	17	15	16
General and administration	19	16	16	15	17	15	17
Amortization and change in contingent consideration	8	6	8	8	9	8	10
Total operating expenses	100	93	90	88	89	89	90
Income from operations		7	10	12	11	11	10
Other income (expense):							
Interest income	1			0	0	0	0
Interest expense	(1)			0	(1)	0	(1)
Interest expense: amortization of convertible debt discount		(18)					
Loss on extinguishment of debt							
Gain (loss) on revaluation of warrants		(5)		0	1	0	0
Other income					0		0
Loss before income taxes		(16)	10	12	11	11	9
Income tax (provision) benefit	(1)	1	15	(1)	(4)	(1)	(3)
Net income (loss)	(1)	(15)	25	11	7	10	6
Accretion of redemption premium (expense) benefit	1	(6)	(5)	(8)	(2)	(8)	(3)
Net income (loss) attributable to common stockholders	%	(21)%	20%	3%	5%	2%	3%

Comparison of the Three and Six Months Ended June 30, 2011 and 2012

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)		2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	
Revenue:						
Healthcare	\$ 22,854	\$ 27,615	21%	\$ 47,079	\$ 56,845	21%
Commuter	8,382	13,220	58%	16,589	25,212	52%
Other	2,625	2,942	12%	5,517	6,030	9%

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Total revenue	\$ 33,861	\$ 43,777	29%	\$ 69,185	\$ 88,087	27%
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Healthcare Revenue

The \$4.8 million increase in healthcare revenue from the second quarter of 2012 as compared to the second quarter of 2011 was primarily driven by the inclusion of \$3.1 million in post-purchase revenue for Choice Strategies, or CS, which was acquired in January 2012, and increases in interchange fees of \$0.4 million due to

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increased debit card usage as well as an increase in the number of debit cards issued. The growth in healthcare revenue was further driven by a \$1.3 million increase in FSA and HRA revenue due to an increase in employee participation in our programs in the second quarter of 2012 as compared to the second quarter of 2011.

The \$9.8 million increase in healthcare revenue for the first six months of 2012 as compared to the first six months of 2011 was primarily driven by the inclusion of \$6.1 million in post-purchase revenues for CS and increases in interchange fees of \$1.4 million due to increased debit card usage as well as an increase in the number of debit cards issued. The growth in healthcare revenue was further driven by a \$2.5 million increase in FSA and HRA revenue due to an increase in employee participation in our programs in the first six months of 2012 as compared to the first six months of 2011.

Commuter Revenue

The \$4.8 million increase in commuter revenue for the second quarter of 2012 as compared to the second quarter of 2011 reflected the inclusion of \$4.8 million in post-purchase revenue for TransitChek, or TC, which was acquired in February 2012.

The \$8.6 million increase in commuter revenue for the first six months of 2012 as compared to the first six months of 2011 was primarily driven by the inclusion of \$8.1 million in post-purchase revenue for TC. Excluding TC, commuter revenue increased by \$0.2 million, driven primarily by increased interchange revenue as a result of increased prepaid debit card usage.

Other Revenue

The \$0.3 million increase in other revenue for the second quarter of 2012 as compared to the second quarter of 2011 was primarily driven by a \$0.2 million increase of COBRA revenue.

The \$0.5 million increase in other revenue for the first six months of 2012 as compared to the first six months of 2011 reflected a \$0.5 million increase in COBRA revenue and direct billing services.

Cost of Revenue

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)		2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	
Cost of revenues (excluding amortization of internal use software)	\$ 13,244	\$ 15,620	18%	\$ 28,610	\$ 32,677	14%
Percent of revenue	39%	36%		41%	37%	

The \$2.4 million increase in cost of revenues for the second quarter of 2012 as compared to the second quarter of 2011 reflected the inclusion of approximately \$2.4 million in post-purchase expenses for CS and TC. In the second quarter of 2011, outsourced services expense was decreased by savings that were recognized from a negotiated reduction in rates with a third-party vendor. The savings that were recognized in the second quarter of 2011 also included savings related to the first quarter of 2011 as a result of the completion of the re-negotiation of the service agreement with that third party vendor effective January 1, 2011. When compared to the second quarter of 2012, this amounts to a \$0.4 million increase in outsourced services expense. The increase in outsourced services expense was further driven by MHM commencing to outsource claims in the latter part of the second quarter of 2011 and therefore only reflecting a partial quarter of expenses, while the second quarter of 2012 reflects a full quarter of outsourced services expense related to MHM claims processing. Increases in cost of revenues were offset in part by decreases in salaries and personnel-related costs of \$0.4 million primarily as a result of the integration of PBS and FBM. The cost of revenues decreased as a percentage of revenue from the

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second quarter of 2012 as compared to the second quarter of 2011 by 3%, primarily due to the TC acquisition that added to our commuter revenue, which has lower direct expenses relative to healthcare revenue because of the claims processing required by our services that generate healthcare revenue. Our company-wide cost saving efforts also contributed to the decrease in cost of revenue as a percentage of revenue decreasing.

The \$4.1 million increase in cost of revenues for the first six months of 2012 as compared to the first six months of 2011 was primarily driven by the inclusion of approximately \$4.4 million in post-purchase expenses for CS and TC, and an increase of \$0.4 million in net processing losses. These increases were offset in part by decreases in salaries and personnel-related costs of \$0.6 million primarily as a result of the integration of PBS and FBM. The cost of revenues decreased as a percentage of revenue from the first six months of 2012 as compared to the first six months of 2011 by 4%, and the decrease was primarily due to the TC acquisition as noted above for the second quarter of 2012 as compared to the second quarter of 2011. Our company-wide cost saving efforts also contributed to the decrease in cost of revenue as a percentage of revenue decreasing.

As we continue to scale our operations, we expect our cost of revenues to increase in absolute dollars to support increased employer client and employee participant levels. Cost of revenues will continue to be affected by our portfolio purchases, acquisitions and channel partner arrangements. Prior to migrating to our proprietary technology platforms, these new portfolios often operate with higher service delivery costs that result in increased cost of revenues until we are able to complete the migration process, which typically occurs over the 12- to 24-month period following closing of the portfolio purchase or acquisition.

Technology and Development

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)		2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	
Technology and development	\$ 3,447	\$ 4,622	34%	\$ 6,939	\$ 8,962	29%
Percent of revenue	10%	10%		10%	10%	

The \$1.2 million increase in technology and development expenses for the second quarter of 2012 as compared to the second quarter of 2011 was primarily driven by the inclusion of approximately \$1.0 million in post-purchase expenses for CS and TC. Excluding CS and TC, temporary help, consulting services, salaries and personnel-related costs increased by \$0.9 million due to continued investment in improving the functionality of our platform and mobile features, though these costs were offset by an increase in expenditures qualifying for capitalization of \$0.9 million.

The \$2.0 million increase in technology and development expenses for the first six months of 2012 as compared to the first six months of 2011 was primarily driven by the inclusion of approximately \$1.8 million in post-purchase expenses for CS and TC. Excluding CS and TC, temporary help, consulting services, salaries and personnel-related costs increased by \$2.1 million due to continued investment in improving the functionality of our platform and mobile features, though these costs were mostly offset by an increase in expenditures qualifying for capitalization of \$1.8 million.

We intend to continue to enhance the functionality of our software platform as part of our continuous effort to improve our employer client and employee participant experience and to maintain and enhance our control and compliance environment. As a result of our focus on technology development, our CS portfolio purchase and our TC acquisition, we expect our technology and development expenses to increase in absolute dollars in future periods. The timing of development and enhancement projects, including whether they are in phases where costs are capitalized or expensed, will significantly affect our technology and development expense both in absolute dollars and as a percentage of revenue.

Table of Contents**Sales and Marketing**

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012		2011	2012	
Sales and marketing	\$ 5,209	\$ 7,267	40%	\$ 10,458	\$ 14,476	38%
Percent of revenue	16%	17%		15%	16%	

The \$2.1 million increase in sales and marketing expense for the second quarter of 2012 as compared to the second quarter of 2011 was primarily driven by the inclusion of approximately \$1.8 million in post-purchase expenses for CS and TC.

The \$4.0 million increase in sales and marketing expense for the first six months of 2012 as compared to the first six months of 2011 was primarily due to the acquisition of CS and TC, which increased sales and marketing expense by \$3.2 million. Excluding CS and TC, sales and marketing expense also increased by \$0.5 million associated with a sales program to increase market awareness for our commuter program.

Sales and marketing expense as a percentage of revenue increased for both the second quarter and first six months of 2012 as compared to the second quarter and first six months of 2011 by 1%. These increases were primarily due to our TC acquisition and CS portfolio purchase having higher relative sales and marketing expenses as a percentage of revenue.

We intend to continue to invest in sales, client services and marketing by hiring additional direct sales personnel and continuing to build our broker and channel relationships. We also intend to promote our brand through a variety of marketing and public relations activities. As a result, we expect our sales and marketing expenses to increase in absolute dollars and as a percentage of revenue in future periods.

General and Administration

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012		2011	2012	
General and administration	\$ 5,104	\$ 7,325	44%	\$ 10,466	\$ 14,803	41%
Percent of revenue	15%	17%		15%	17%	

The \$2.2 million increase in general and administration expenses for the second quarter of 2012 as compared to the second quarter of 2011 was primarily due to the inclusion of approximately \$1.3 million in post-purchase expenses for CS and TC. General and administration expenses also increased by \$0.3 million due to additional stock-based compensation expense incurred during the second quarter of 2012 as a result of the vesting of performance-based option grants, and \$0.2 million due to increased professional services expenses, primarily related to continued efforts to enhance our control environment to meet the requirements of being a public company. The remaining increase in general and administration expenses is primarily driven by increased allocation of facilities costs to general and administration departments as a result of increased headcount, when compared to the same period a year ago.

The \$4.3 million increase in general and administration expenses for the first six months of 2012 as compared to the first six months of 2011 was primarily due to the inclusion of approximately \$2.6 million in post-purchase expenses for CS and TC. General and administration expenses increased by \$0.9 million due to increased professional and consulting expenses and salaries and personnel-related costs, related to continued efforts to enhance our control environment and to meet other requirements of being a public company. General and administration expenses also increased by \$0.3 million due to additional stock-based compensation expense incurred during the second quarter of 2012 as a result of the vesting of performance-based option grants at the

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closing of our initial public offering. The remaining increase in general and administration expenses is primarily driven by increased allocation of facilities costs to general and administration departments as a result of increased headcount, when compared to the same period a year ago.

General and administration expenses as a percentage of revenue increased for both the second quarter and first six months of 2012 as compared to the second quarter and first six months of 2011 by 2%. These increases were driven by our TC acquisition and CS portfolio purchase having higher relative general and administration expenses as a percentage of revenue.

We expect our general and administration expenses to continue to increase in absolute dollars and as a percentage of revenue in future periods due to expenses associated with being a public company.

Amortization and Change in Contingent Consideration

	Three Months Ended June 30,		Change from prior year	Six Months Ended June 30,		Change from prior year
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)		2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	
Amortization and change in contingent consideration	\$ 2,682	\$ 4,094	53%	\$ 5,175	\$ 8,532	65%

The \$1.4 million increase in amortization and change in contingent consideration for the second quarter of 2012 as compared to the second quarter of 2011 reflects \$1.0 million of additional amortization of acquired intangible assets primarily driven by the CS portfolio purchase and TC acquisition as well as \$0.8 million of additional contingent consideration expenses related to our CS portfolio purchase, due to greater than anticipated revenue growth, partly offset by a reduction in contingent consideration expenses related to FBM and PBS portfolio purchases of \$0.5 million.

The \$3.4 million increase in amortization and change in contingent consideration for the first six months of 2012 as compared to the first six months of 2011 reflects a \$1.6 million increase in amortization of acquired intangible assets primarily driven by the CS portfolio purchase and TC acquisition, as well as \$0.9 million and \$0.8 million of additional contingent consideration expenses related to our PBS and CS portfolio purchases, respectively, due to greater than anticipated revenue growth.

Other Income (Expense)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)
Interest income	\$ 9	\$ 9	\$ 20	\$ 19
Interest expense	(111)	(452)	(197)	(857)
Other income		12		27

The increase in interest expense for both the second quarter and first six months of 2012 as compared to the second quarter and first six months of 2011 was due to the increase in the amount borrowed under our credit facility with Union Bank, N.A. in 2012 to finance the TC acquisition.

Revaluation of Warrants

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)	2011 (in thousands, unaudited)	2012 (in thousands, unaudited)
Gain (loss) on revaluation of warrants	\$ 51	\$ 407	\$ (59)	\$ 381

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The mark-to-market adjustment related to our outstanding warrant for Series C redeemable preferred stock resulted in a \$0.4 million gain for the second quarter of 2012 and the first six months of 2012. Upon the closing of our initial public offering in May 2012 and the automatic conversion of the outstanding shares of our preferred stock into shares of common stock, the warrant for Series C redeemable preferred stock became exercisable for shares of common stock. We performed the final re-measurement of the warrant for Series C redeemable preferred stock at the closing date of our initial public offering and the warrant was then reclassified from a liability to equity. Subsequent to the closing date, we will no longer record any mark-to-market changes in the fair value of these warrants in the consolidated statement of operations.

Income Taxes

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2012	2011	2012
	(in thousands, unaudited)		(in thousands, unaudited)	
Income taxes provision	\$ (253)	\$ (1,601)	\$ (401)	\$ (2,973)

Our provision for income taxes increased from \$0.3 million for the second quarter of 2011 to \$1.6 million for the second quarter of 2012 and \$0.4 million for the first six months of 2011 to \$3.0 million for the first six months of 2012, due to a projected annual effective tax rate increase from 2.9% to 41.1% as a result of the release of our \$25.9 million valuation allowance in the fourth quarter of 2011. The tax provision for the three months and six months ended June 30, 2012 includes a discrete deferred tax benefit of \$0.5 million related to the increase of federal income tax rate from 34% to 35% due to an increase in estimated taxable future earnings.

Accretion of Redemption Premium

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2012	2011	2012
	(in thousands, unaudited)		(in thousands, unaudited)	
Accretion of redemption premium expense	\$ (2,924)	\$ (778)	\$ (5,692)	\$ (2,301)

We accounted for redemption premium by recording accretion charges reflecting the changes in the redemption value of certain of our series of redeemable preferred stock over the period from the date of issuance to the earliest redemption date. Upon the closing date of our initial public offering in May 2012, all outstanding redeemable preferred shares were converted into shares of common stock which are non-redeemable. We performed the final re-measurement of the redemption value of the redeemable preferred stock at the date when redemption was no longer probable and the redeemable preferred stock was then reclassified from the mezzanine level of the consolidated balance sheet into equity. We no longer record accretion of redeemable preferred shares.

Comparison of the Years Ended December 31, 2009, 2010 and 2011**Revenue**

	Year Ended December 31,			Change from Prior Year	
	2009	2010	2011	2010	2011
	(in thousands)				
Revenue:					
Healthcare	\$ 70,718	\$ 75,771	\$ 90,917	7%	20%
Commuter	27,603	29,304	33,325	6	14
Other	10,140	9,972	11,395	(2)	14
Total revenue	\$ 108,461	\$ 115,047	\$ 135,637	6%	18%

Table of Contents*Healthcare Revenue*

The growth in healthcare revenue from 2010 to 2011 was primarily driven by the inclusion of a full year of post-purchase revenue of \$4.4 million and \$8.9 million for PBS and FBM, which were acquired in August 2010 and November 2010, respectively. Healthcare revenue also increased due to \$1.2 million of increased revenue from SMB employer clients, which includes \$0.5 million of increased Premium Only Plan kits revenue arising from the sale of self-service plan kits that we provide to employer clients to initiate the deduction of healthcare premiums on a tax deferred basis.

The growth in healthcare revenues from 2009 to 2010 was primarily driven by the inclusion of \$1.8 million and \$0.8 million in post-purchase revenues for PBS, which was acquired in August 2010, and FBM, which was acquired in November 2010. Interchange fees grew by \$2.1 million due to an increased number of prepaid debit cards, both WageWorks-branded and those provided as part of our wholesale card program, and increased debit card usage as a percentage of overall employee participant spending.

Commuter Revenue

The growth in commuter revenue from 2010 to 2011 was primarily driven by an increased number of employee participants and the addition of a very large employer client in the first quarter of 2011. Commuter interchange revenue also increased by \$0.9 million as a result of increased prepaid debit card usage.

The growth in commuter revenues from 2009 to 2010 was principally due to an increase in the number of employee participants from our existing employer clients as our portfolio purchases during this period had only a nominal amount of commuter revenue.

Other Revenue

The growth in other revenue from 2010 to 2011 was primarily driven by the inclusion of a full year of post-purchase COBRA revenue of \$1.6 million and \$1.4 million for PBS and FBM, respectively. These increases were offset, in part, by decreases in COBRA revenue, in part due to the loss of employee participants and, in part, due to the ending of the American Recovery and Reinvestment Act (ARRA), which provided a subsidy for COBRA benefits.

Cost of Revenues

	Year Ended December 31,			Change from Prior Year	
	2009	2010	2011	2010	2011
	(in thousands)				
Cost of revenues (excluding amortization of internal use software)	\$ 46,802	\$ 50,205	\$ 55,651	7%	11%
Percent of revenue	43%	44%	41%		

The increase in cost of revenues (excluding amortization of internal use software) from 2010 to 2011 was primarily driven by the inclusion of a full year of post-purchase expenses for PBS and FBM of \$10.4 million. These increases were offset, in part, by a \$1.7 million decrease in costs as a result of substantially completing the integration of CB and a decrease in outsourced services expense of \$0.8 million primarily related to savings from a negotiated reduction in rates with a third party vendor. In addition, payroll and related expenses and temporary worker expense decreased \$1.1 million due to operations consolidation, the termination of ARRA and a decrease in depreciation expense of \$0.5 million. The decrease in cost of revenues as a percentage of revenue was due to the significant increase in revenue and the cost reduction items discussed above.

The increase in cost of revenues (excluding amortization of internal use software) from 2009 to 2010 was primarily due to \$1.4 million and \$0.7 million relating to the post-purchase costs of PBS and FBM, respectively. In 2009, we had \$1.1 million of net processing gains, due to the recovery of overpayments made in previous periods. In 2010, our net processing losses were \$0.3 million.

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In addition to these changes, headcount attributable to cost of revenues decreased by 7% in 2010, which contributed to a \$0.7 million decrease in cost of revenues. The decrease in headcount was the result of the continued consolidation of operations between locations and an increase in outsourcing. The consolidation also reduced facilities costs by \$0.4 million, while outsourcing costs increased by \$0.5 million. Cost of revenues in 2009 benefited from a \$0.3 million reduction in accrual for a third party claim. Cost of revenues as a percent of revenue increased due to the change from net processing gains in 2009 to net processing losses in 2010, despite higher revenue volume and other expense decreases.

Technology and Development

	Year Ended December 31,			Change from Prior Year	
	2009	2010 (in thousands)	2011	2010	2011
Technology and development	\$ 13,773	\$ 12,640	\$ 13,526	(8)%	7%
Percent of revenue	13%	11%	10%		

The increase in technology and development expenses from 2010 to 2011 was primarily driven by an increase in salaries and personnel-related costs of approximately \$1.5 million, an increase in outsourced services and temporary help and consulting services of \$1.0 million related to the reporting capability and functionality of our platform and \$0.9 million in Shared Services Agreement expenses paid to FBMC for support provided to certain acquired customer contracts. These increases were partially offset by a \$2.3 million increase in the expenditures qualifying for capitalization in 2011 related to implementation of additional mobile features for our platform, mobile applications for our SMB client base as well as the development of functionality and integration of our COBRA platform. The decrease in technology and development expenses as a percentage of revenue was primarily due to the significant increase in revenue.

The decrease in technology and development expenses from 2009 to 2010 was primarily a result of a 13% reduction in headcount due to increased outsourcing and consolidation of our IT operations, which led to a decrease in personnel expenses of \$0.6 million, excluding the effect of PBS and FBM which was a \$0.1 million increase in personnel expenses. In addition, we incurred decreased use of our personnel and less outsourced programming on expensed development activities due to the completion of several significant customization and internal control projects during 2009. Technology and development expense as a percentage of revenue decreased due to these changes and increased revenue volume.

Sales and Marketing

	Year Ended December 31,			Change from Prior Year	
	2009	2010 (in thousands)	2011	2010	2011
Sales and marketing	\$ 18,885	\$ 18,173	\$ 20,697	(4)%	14%
Percent of revenue	17%	16%	15%		

The increase in sales and marketing expense from 2010 to 2011 was primarily driven by \$2.5 million of additional expense arising from the acquisition of PBS and FBM. Excluding PBS and FBM, payroll and related expenses increased by approximately \$0.8 million due to increased headcount associated with the growth of our business. These increases were partially offset by decreases of \$0.4 million related to the completion of a public relations campaign and \$0.2 million of advertising expense. The decrease in sales and marketing expense as a percentage of revenue was due to the significant increase in revenue.

The decrease in sales and marketing expense from 2009 to 2010 was primarily due to a 10% reduction in sales and marketing headcount, which reduced personnel expense by \$2.1 million, excluding the effect of PBS and FBM which was a \$0.2 million increase in personnel expenses. In April 2009, we reorganized in a number of

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areas to enable key personnel to focus solely on servicing either our healthcare or commuter programs. In addition, we reduced and reorganized our client services team to focus on specific regions. This decrease in personnel expenses was offset in part by expenses for increased promotional activity and education efforts focused on increasing employee participation levels in our tax-deferred CDBs among our existing employer client base. Sales and marketing expense as a percentage of revenue decreased slightly, primarily due to increased revenue volume.

General and Administration

	Year Ended December 31,			Change from Prior Year	
	2009	2010 (in thousands)	2011	2010	2011
General and administration	\$ 20,134	\$ 18,231	\$ 20,876	(9)%	15%
Percent of revenue	19%	16%	16%		

The increase in general and administration expenses from 2010 to 2011 was primarily driven by an increase in payroll and related expenses, professional services expense and outsourced services expense aggregating approximately \$3.3 million primarily due to our preparation to become a public company. These increases were partially offset by a \$0.8 million decrease in temporary help and consulting services due to the completion of finance related infrastructure projects in 2010.

The decrease in general and administration expenses from 2009 to 2010 was primarily due to a decrease in consulting and accounting expenses of \$1.0 million relating to the improvement of our controls and processes that we incurred in 2009 and to a decrease of \$0.8 million in public service announcements and advocacy efforts that we incurred in 2009 relating to healthcare reform. General and administration expense as a percentage of revenues decreased due to these decreases together with increased revenue volume.

Amortization and Change in Contingent Consideration

	Year Ended December 31,			Change from Prior Year	
	2009	2010 (in thousands)	2011	2010	2011
Amortization and change in contingent consideration	\$ 8,398	\$ 7,764	\$ 11,327	(8)%	46%

Our amortization consists of three components: amortization of internal use software, amortization of acquired intangibles and change in contingent consideration. We capitalize our software development costs related to the development and enhancement of our business solution. When the technology is available for its intended use, the capitalized costs are amortized over the technology's estimated useful life, which is generally four years. Acquired intangibles are also amortized over their useful lives.

The increase in amortization and change in contingent consideration from 2010 to 2011 was primarily due to charges of \$1.4 million and \$1.3 million, respectively, for contingent consideration related to our PBS and FBM portfolio purchases. These increases were driven by increases in revenue levels achieved and forecasted to be achieved in 2012. Amortization of acquired intangible assets increased \$0.5 million due to the inclusion of a full year of post-purchase amortization of acquired intangible assets related to FBM and PBS.

The decrease in amortization from 2009 to 2010 was primarily a result of a decrease of \$1.2 million in amortization of acquired intangible assets due to a number of acquired intangible assets becoming fully amortized in 2010. This decrease was partially offset by an increase in a \$0.6 million amortization of internal use software as several major client specific platform enhancements and our daily settlement system were completed and amortization commenced, and increases in amortization related to the purchases of PBS and FBM of \$0.2 million

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and \$0.1 million, respectively. There was no change in contingent consideration in the years ended December 31, 2009 and 2010 as the acquisitions to which these contingent considerations relate occurred in the latter part of 2010.

We expect our amortization expenses to increase in 2012 and beyond due to the amortization of acquired intangibles associated with our CS and TC transactions in early 2012.

Other Income (Expense)

	Year Ended December 31,		
	2009	2010	2011
	(in thousands)		
Interest income	\$ 851	\$ 220	\$ 36
Interest expense	(1,102)	(188)	(494)
Interest expense: amortization of convertible debt discount	(71)	(21,107)	

The decrease in interest income from 2009 through 2011 was due to reduced short-term interest rates available to us on our invested funds.

The increase in interest expense from 2010 to 2011 was primarily due to the increase in the outstanding amount borrowed under our credit facility with Union Bank, N.A. in 2011 as compared to 2010.

The decrease in interest expense from 2009 to 2010 was primarily due to the repayment of a debt facility in December 2009.

The absence of amortization of convertible debt discount in 2011 is due to the full amortization of the convertible notes in 2010 and the conversion of the notes to equity in July 2010.

Our convertible notes issued on December 28, 2009 resulted in a debt discount of \$20.0 million. We amortized as interest \$11.4 million of the debt discount from January 1, 2010 to the date of the conversion of the notes and accrued interest of \$1.2 million on July 31, 2010. At the conversion date, the remaining unamortized debt discount balance of \$8.5 million was immediately expensed as interest.

Revaluation of Warrants

	Year Ended December 31,		
	2009	2010	2011
	(in thousands)		
Gain (loss) on revaluation of warrants	\$ 70	\$ (5,413)	\$ 351

The mark-to-market adjustment related to our outstanding warrants for Series C redeemable preferred stock was a \$0.4 million gain for the year ended December 31, 2011 primarily due to a decline in the underlying fair market value of our Series C redeemable preferred stock.

The significant increase in expense relating to revaluation of warrants in 2010 relative to 2009 is primarily due to the mark-to-market adjustment of Series E redeemable preferred stock warrants issued to the holders of our convertible debt on December 28, 2009. This mark-to-market adjustment was required as a result of the warrants being classified as a liability because the Series E preferred shares were redeemable. In July 2010, the warrants were amended to provide that, upon exercise, the holders would receive shares of our Series E-1 preferred stock which are not redeemable. For that reason, the warrants were reclassified from a liability to equity and mark-to-market adjustments were no longer required. The total mark-to-market adjustment for these warrants was approximately \$5.0 million for 2010.

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Upon the completion of our initial public offering, the warrants for Series C redeemable preferred stock became exercisable for common stock. As the warrants are no longer exercisable into shares of redeemable preferred stock, we will no longer record any mark-to-market changes in the fair value of these warrants in our consolidated statement of operations. The total mark-to-market adjustment for these warrants was approximately \$0.4 million for 2010.

Income Taxes

	Year Ended December 31,		
	2009	2010	2011
Income tax (provision) benefit	\$ (495)	\$ 1,204	\$ 19,868

(in thousands)

The change from 2010 to 2011 is primarily related to the release of the \$25.9 million valuation allowance at December 31, 2011. In the fourth quarter of 2011, we determined that the positive evidence of taxable income coupled with our forecasted profitability outweighed the negative evidence of prior losses. We deferred action on the release of the valuation allowance until the fourth quarter of 2011 when we had visibility into our 2012 enrollment levels, including enrollment and a full year of results from our 2010 portfolio purchases. We believe this information provides the basis for reliable forecasts of our 2012 pre-tax income due to the fixed monthly fees that form the majority of our revenue.

The change in income taxes from 2009 to 2010 is due to our purchase of PBS in August 2010 in which we recorded a deferred tax liability related to the book and tax bases differences in our purchase accounting. This increase in deferred tax liabilities resulted in a reduction of our valuation allowance for net deferred tax assets which is recorded as an income tax benefit in our statement of operations.

The expenses in 2009 primarily reflect the recording of deferred tax liabilities due to the book and tax bases differences related to the goodwill acquired in certain of our portfolio purchases.

Accretion of Redemption Premium

	Year Ended December 31,		
	2009	2010	2011
Accretion of redemption premium (expense) benefit	\$ 1,037	\$ (6,740)	\$ (6,209)

(in thousands)

At December 31, 2011, certain of our series of preferred stock were redeemable after December 31, 2012 at the election of the majority of the holders of those series if we had not completed an initial public offering by December 31, 2012. To the extent that the redemption was requested, the holders would have received the greater of the fair value of the preferred stock at the time of redemption and the original purchase price. We accounted for this redemption premium by recording accretion charges reflecting the changes in the redemption value over the period from the date of issuance to the earliest redemption date, which is December 31, 2012. Upon the completion of our initial public offering in May 2012, the redeemable preferred shares converted to common shares that are not redeemable. We performed the final re-measurement of the redeemable preferred stock at the date where redemption was deemed not probable and recorded \$0.7 million of accretion of redemption premium expense. The preferred stock was then reclassified from the mezzanine to equity. We no longer record accretion of redeemable preferred shares.

The significant increases in accretion of redemption premium expense in 2010 and 2011, relative to 2009, relate to the issuance of shares of Series E preferred stock in July 2010 that provide for the same type of redemption premium as well as an increase in the fair value of our preferred stock based on our performance and that of the general economy. The benefit in 2009 arises from a decrease in the value of shares of our preferred stock from 2008 to 2009 arising from general economic conditions.

Table of Contents**Quarterly Results of Operations**

The following table sets forth our unaudited quarterly condensed consolidated statements of operations data for each of the nine quarters ended June 30, 2012. The data has been prepared on the same basis as the audited consolidated financial statements and related notes included in this prospectus and you should read the following tables together with such financial statements. The quarterly results of operations include all normal recurring adjustments necessary for a fair presentation of this data. Results of interim periods are not necessarily indicative of results for the entire year and are not necessarily indicative of future results.

	Quarter Ended									
	March 31, 2010	June 30, 2010	September 30, 2010	December 31, 2010	March 31, 2011	June 30, 2011	September 30, 2011	December 31, 2011	March 31, 2012	June 30, 2012
	(in thousands, unaudited)									
Condensed Consolidated Statements of Operations Data:										
Revenue:										
Healthcare	\$ 20,017	\$ 18,249	\$ 17,733	\$ 19,772	\$ 24,225	\$ 22,854	\$ 21,511	\$ 22,327	\$ 29,230	\$ 27,615
Commuter	7,142	7,350	7,288	7,524	8,207	8,382	8,271	8,465	11,992	13,220
Other	2,553	2,208	2,312	2,899	2,892	2,625	2,665	3,213	3,088	2,942
Total revenue	29,712	27,807	27,333	30,195	35,324	33,861	32,447	34,005	44,310	43,777
Cost of revenues (excluding amortization of internal use software)										
Technology and development	13,297	11,747	11,336	13,825	15,366	13,244	12,537	14,504	17,057	15,620
Sales and marketing	3,557	3,051	2,966	3,066	3,492	3,447	3,403	3,184	4,340	4,622
General and administration	4,628	4,325	4,942	4,278	5,249	5,209	4,733	5,506	7,209	7,267
Amortization and change in contingent consideration	5,423	4,150	4,249	4,409	5,362	5,104	5,163	5,247	7,478	7,325
Total operating expenses	1,912	1,878	1,900	2,074	2,493	2,682	2,985	3,167	4,438	4,094
Total operating expenses	28,817	25,151	25,393	27,652	31,962	29,686	28,821	31,608	40,522	38,928
Income from operations	895	2,656	1,940	2,543	3,362	4,175	3,626	2,397	3,788	4,849
Other income (expense):										
Interest income	107	71	27	15	11	9	7	9	10	9
Interest expense	(42)	(3)	(19)	(124)	(86)	(111)	(125)	(172)	(405)	(452)
Interest expense: amortization of convertible debt discount	(5,358)	(5,418)	(10,331)							
Gain (loss) on revaluation of warrants	(5,935)	(9,606)	10,642	(514)	(110)	51	627	(217)	(26)	407
Other income									15	12
Income (loss) before income taxes	(10,333)	(12,300)	2,259	1,920	3,177	4,124	4,135	2,017	3,382	4,825
Income tax (provision) benefit	(195)	(283)	1,582	100	(148)	(253)	(234)	20,503	(1,372)	(1,601)
Net income (loss)	(10,528)	(12,583)	3,841	2,020	3,029	3,871	3,901	22,520	2,010	3,224
Accretion of redemption premium (expense) benefit	(70)	(70)	(3,094)	(3,506)	(2,768)	(2,924)	387	(904)	(1,523)	(778)

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Net income (loss) attributable to common stockholders	\$ (10,598)	\$ (12,653)	\$	747	\$	(1,486)	\$	261	\$	947	\$	4,288	\$	21,616	\$	487	\$	2,446
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	Quarter Ended									
	March 31, 2010	June 30, 2010	September 30, 2010	December 31, 2010	March 31, 2011	June 30, 2011	September 30, 2011	December 31, 2011	March 31, 2012	June 30, 2012
	(in thousands, unaudited)									
Condensed Consolidated Statements of Operations Data as a Percentage of Revenue:										
Revenue:										
Healthcare	67%	66%	65%	65%	69%	67%	66%	66%	66%	63%
Commuter	24	26	27	25	23	25	26	25	27	30
Other	9	8	8	10	8	8	8	9	7	7
Total revenue	100	100	100	100	100	100	100	100	100	100
Cost of revenues										
(excluding amortization of internal use software)	45	42	41	46	43	39	39	43	38	36
Technology and development	12	11	11	10	10	10	10	9	10	10
Sales and marketing	16	15	18	14	15	16	15	16	16	17
General and administration	18	15	16	15	15	15	16	16	17	17
Amortization and change in contingent consideration	6	7	7	7	7	8	9	9	10	9
Total operating expenses	97	90	93	92	90	88	89	93	91	89
Income from operations	3	10	7	8	10	12	11	7	9	11
Other income (expense):										
Interest income										
Interest expense									(1)	(1)
Interest expense: amortization of convertible debt discount	(18)	(19)	(38)							
Gain (loss) on revaluation of warrants	(20)	(35)	39	(2)			2	(1)		1
Other income										
Income (loss) before income taxes	(35)	(44)	8	6	10	12	13	6	8	11
Income tax (provision) benefit	(1)	(1)	6		(1)	(1)	(1)	60	(3)	(4)
Net income (loss)	(36)	(45)	14	6	9	11	12	66	5	7
Accretion of redemption premium (expense) benefit			(11)	(11)	(8)	(8)	1	(2)	(4)	(2)
Net income (loss) attributable to common stockholders	(36)%	(45)%	3%	(5)%	1%	3%	13%	64%	1%	5%

Changes in healthcare revenue reflect the seasonality of this portion of our business. The first quarter is expected to provide increased revenues because we continue to bill employer clients for employee participants who terminate their enrollment for the new plan year, but who still participate in the run-out or grace period of the old plan year that normally runs through the first quarter of the new plan year. Interchange revenue also typically increases during the first quarter due to employee participants who utilize their account balances for the new plan year and other employee participants who are spending any remaining account balances they may have under the old plan year during the grace period. The declining trend of healthcare revenue over the second and third quarters is partially attributable to a gradual decrease in interchange revenue as employee participants begin to slow their spending as the year progresses, subject to a small increase in activity in December as some

employee participants spend the remainder of their account balance prior to the end of the year. In

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addition, during the late third and fourth quarters, we have an increase in our revenue from sales of a self-service plan kit that we provide employer clients to initiate the deduction of healthcare premiums on a tax deferred basis, without the use of a spending account, which we refer to as our Premium Only Plan. Our quarterly revenue can also be impacted by the timing of our acquisitions and portfolio purchases.

Employees may elect to participate in our commuter programs at any time during the year. In the past, we have experienced some seasonality in this portion of our business because participation rates typically slow during the summer as employee participants take vacations and do not purchase transit passes or parking through us during that time period.

Other services revenues, which consist of COBRA and enrollment and eligibility fees, are generally consistent throughout the year but may increase in the fourth quarter due to additional enrollment and eligibility fees being earned after our clients' open enrollment seasons.

Quarterly revenue in 2010 was impacted by \$0.5 million from PBS in the third quarter of 2010 and an incremental \$1.1 million and \$1.0 million from PBS and FBM, respectively, in the fourth quarter of 2010, which accounted for part of the increase during this period. In addition, Premium Only Plan, or POP, revenue increased by \$0.7 million from the third quarter of 2010 to the fourth quarter of 2010. In the first quarter of 2011, as compared to the fourth quarter of 2010, quarterly revenue was impacted by \$1.9 million of additional revenue from FBM which reflects the full quarter compared to one month of revenue in the fourth quarter. First quarter 2011 revenue also reflects an increase in commuter participants and the seasonal increase in healthcare activity associated with the new plan year and run-out grace periods for the 2010 plan year when compared to the second quarter of 2011. POP revenue increased by \$1.0 million from the third quarter of 2011 to the fourth quarter of 2011, which reflects the seasonality of this revenue and is consistent with 2010. The first quarter of 2012 included \$3.3 million and \$3.0 million of post-purchase revenue from TC and CS, respectively, and an additional \$3.7 million of interchange revenue as compared to the fourth quarter of 2011 due to seasonality, increased debit card usage and an increase in the number of debit cards issued. First quarter 2012 revenue also reflects an increase in commuter participants and the seasonal increase in healthcare activity associated with the new plan year and run-out grace periods for the 2011 plan year when compared to the second quarter of 2012.

Cost of revenues (excluding amortization of internal use software) typically varies based on our revenue and is, therefore, impacted by the seasonality of the business. We incur higher expenses in the first quarter associated with increased headcount in the form of temporary workers, consultants and other outsourced services that are required to cover the increased call volume and activity associated with the new plan year. The need for these resources diminishes in the second and third quarters, but increases again in the fourth quarter when we provide services to our employer clients during their open enrollment periods. The fourth quarter also reflects expenses that relate to the sale of our Premium Only Plan kits and the production of debit cards. In addition, our quarterly revenue can also be impacted by the timing of our portfolio purchases. Portfolio purchases may have a short-term material adverse impact on our results of operations, including a potential material adverse impact on our cost of revenues as we seek to migrate acquired employer clients to our proprietary technology platforms, typically over the succeeding 12 to 24 months, in order to achieve additional operating efficiencies.

The fourth quarter of 2010 and first quarter of 2011 reflect additional cost of revenues of \$1.4 million and \$1.6 million, due to the purchases of PBS and FBM, respectively. Cost of revenues (excluding amortization of internal use software) for the first quarter of 2011 also increased in dollar amount due to the seasonal increases in our customer service center costs when compared to the second quarter of 2011 but decreased as a percentage of revenue as a result of our increased sales revenues. In the second quarter of 2011, there was a decrease of \$1.0 million in outsourced services expenses. Of the \$1.0 million decrease, \$0.5 million relates to savings for the first quarter of 2011 as a result of completion of the re-negotiation of a services agreement effective January 1, 2011. The decrease in cost of revenues from the second quarter of 2011 to the third quarter of 2011 was primarily caused by our continued efforts to consolidate operations and the seasonality of our business. Cost of revenues for the fourth quarter of 2011 increased in dollar amount due to increased outsourced services that are required to cover higher call volume during open enrollment and expenses that relate to the sale of our Premium Only Plan

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kits and the production of debit cards. The first quarter of 2012 included \$1.9 million of post-purchase cost of revenues from TC and CS. Cost of revenues for the first quarter of 2012 also increased in dollar amount due to the seasonal increases in our customer service center costs when compared to the second quarter of 2012.

Technology and development expense is most significantly affected by changes in the stage of development of our internal use software, which determines whether amounts spent are capitalized or expensed.

Sales and marketing expense generally varies from quarter to quarter based on when we undertake promotion activities and when sales commissions are earned. For example, sales and marketing expenses increased in the third quarter of 2010 because we invested in a promotional campaign to increase awareness of pre-tax CDB accounts. Sales commission expense increased in the first quarter of 2011 relative to the fourth quarter of 2010 as the 2010 sales plan year closed out and the new sales plan year commenced. Additionally, we hired new enterprise sales representatives. Sales and marketing expense increased in the fourth quarter of 2011 relative to the third quarter of 2011 due to the commencement of a six-month pilot sales program to increase market awareness for our commuter program.

General and administration expense varies from quarter-to-quarter based on the timing of expenses for accounting. For example, our accounting and consulting fees were higher in the first quarter of 2010 as a result of conducting our annual audit. Our expenses related to our preparation to become a publicly held company increased in the third and fourth quarters of 2010 because we commenced activities to file a registration statement for our initial public offering. In the first quarter of 2011, payroll and related expenses increased by \$0.7 million relative to the fourth quarter of 2010 as we increased our bonus expense accrual based on our 2011 forecast and filled several open positions. The first quarter of 2011 also reflects the expenses associated with our annual audit for 2010. Our general and administration expenses increased from the fourth quarter of 2011 to the first quarter of 2012 due to \$1.3 million of post-purchase expenses from TC and CS, expenses associated with our annual audit and a \$0.2 million restructuring charge related to closing our Troy, Michigan facility.

Amortization and change in contingent consideration increased by \$0.3 million from the second quarter of 2011 to the third quarter of 2011, by \$0.2 million from the third quarter of 2011 to the fourth quarter of 2011 and by \$0.7 million from the fourth quarter of 2011 to the first quarter of 2012 due to increased contingent consideration for our PBS and FBM portfolio purchases. The first quarter of 2012 also included \$0.7 million of amortization of acquired intangibles related to TC and CS.

Amortization of convertible debt discount terminated in the third quarter of 2010 when our convertible notes were converted into preferred stock. Gain (loss) on revaluation of warrants for our Series E preferred stock terminated in the third quarter when the warrants were reclassified from debt to equity and were no longer subject to mark-to-market changes.

Income tax (provision) benefit in the fourth quarter of 2011 reflects the release of the \$25.9 million valuation allowance. In the fourth quarter of 2011, we determined that the positive evidence of taxable income coupled with our forecasted profitability outweighed the negative evidence of prior losses. We deferred action on the release of the valuation allowance until the fourth quarter of 2011 when we had visibility into our 2012 enrollment levels, including enrollment and a full year of results from our 2010 portfolio purchases. We believe this information provides the basis for reliable forecasts of our 2012 pre-tax income due to the fixed monthly fees that form the majority of our revenue. Accordingly, in the fourth quarter of 2011, we released the valuation allowance on our deferred tax assets. Following this, our provision for income taxes for the first quarter of 2012 was \$1.4 million or an effective annual tax rate of approximately 40%.

Liquidity and Capital Resources

At June 30, 2012, our principal sources of liquidity were cash and cash equivalents totaling \$261.3 million comprised primarily of prefunds by clients of amounts to be paid on behalf of employee participants as well as, in recent years, other cash flows from operating activities. In connection with our initial public offering in May 2012, we received aggregate proceeds of \$62.6 million which included the exercise of the underwriters

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overallotment option, net of underwriters' discounts and commissions but before deducting offering costs of \$5.5 million. Prior to our initial public offering, our operations had been financed primarily through cash flows from operating activities, the sale of convertible preferred stock and short- and long-term borrowings.

We believe that our existing cash and cash equivalents, expected cash flow from operations, and net proceeds to us of this offering will be sufficient to meet our operating and capital requirements, as well as anticipated cash requirements for potential future portfolio purchases, over at least the next 12 months. We have historically been able to fulfill our obligations as incurred and expect to continue to fulfill our obligations in the future. Our expectation is based on our current and anticipated client retention rates and our continuing funding model in which the vast majority of our enterprise clients provide us with prefunds as more fully described below under *Prefunds*. To the extent these current and anticipated future sources of liquidity are insufficient to fund our future business activities and requirements, including any potential portfolio purchases, we may need to raise additional funds through public or private equity or debt financing. We cannot provide assurance that we will be able to raise additional funds on favorable terms, if at all.

Prefunds

Under our contracts with the vast majority of our enterprise employer clients, we receive prefunds that have been and are expected to continue to be a significant source of cash flows from operating activities. Each prefund is reflected in cash and cash equivalents on our balance sheet with an equivalent customer obligation recorded as a liability as the prefund is received. Changes in these prefunds and corresponding customer obligations are reflected in our cash flows from operating activities. The substantial majority of our SMB employer clients deposit funds into a separate custodial account, and those funds are neither a source of cash flows from operating activities nor reflected on our balance sheet. These SMB employer clients are responsible for maintaining an adequate balance in those custodial accounts to cover their employee participants' claims. We only pay SMB employee participant claims from amounts in the custodial accounts.

The operation of these prefunds for our enterprise employer clients throughout the year typically is as follows: at the beginning of a plan year, these employer clients provide us with prefunds for their FSA and HRA programs based on a percentage of projected spending by the employee participants for the plan year. In the case of our commuter program, at the beginning of each month we receive prefunds based on the employee participants' monthly elections. These prefunds are typically replenished on a weekly basis by our FSA and HRA employer clients and on a monthly basis by our commuter employer clients, in each case, after we have advanced the funds necessary to process employee participants' FSA and HRA claims as they are submitted to us and to pay vendors relating to our commuter programs. As a result, our cash balances can vary significantly depending upon the timing of invoicing of, and payment by, our employer clients of reimbursement for payments we have made on behalf of employee participants. This prefunding activity covers our estimate of approximately one week of spending on behalf of the employer client's employee participants. We do not require a prefund to administer any of our HSA programs because employee participants in these programs only have access to funds they have previously contributed.

By way of example, a new FSA enterprise employer client with a plan year starting January 1 will typically provide between 4-6% of the projected annual election for its employee participants as a prefund. In this example, we would typically receive this prefunding in late December. Once the new plan year starts, the employee participants can immediately access all elected funds of their FSA benefit even before any payroll deductions have commenced. This access to funds differs from our HSA programs where available funds are added to employee participants' accounts only as payroll deductions occur and HRA programs where funds are only available as contributions are made.

Following the run-out period and grace period, the FSA prefunds from the prior plan year are reconciled and funds are returned to the employer clients, resulting in a substantial decline in our cash position. The cycle then repeats itself in each plan year as participants enroll in programs and prefunds are received in the fourth quarter for the new plan year. In a majority of cases, new FSA prefunds for the succeeding plan year are received prior to

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a plan year's prefund being fully paid out in the form of benefits for employee participants or being returned to the employer client. Because participant activity in our commuter programs varies monthly, prefunds for these programs fluctuate monthly.

Our enterprise client contracts do not contain restrictions on our use of enterprise client prefunds and, as a result, these prefunds are reflected as cash and cash equivalents on our balance sheet and changes in prefunds are recorded as an element of our cash flow from operating activities. The timing of when employer clients make their prefunds as well as the timing of when we make payments on behalf of employee participants can significantly affect our cash flows.

Union Bank Credit Facility

In November 2011, we entered into an amendment to our Commercial Credit Agreement, dated as of August 31, 2010, with Union Bank, N.A., or UB, to increase the aggregate principal amount of our revolving credit line facility to \$50.0 million from \$15.0 million. Each loan under the credit facility bears interest at a variable rate of UB's prime rate plus 0.5% or, at our option, an interest rate equal to the LIBOR rate for a period of either one, two, three or six months, if offered by UB, plus 3.0%. At June 30, 2012, we had outstanding indebtedness of \$44.6 million under the credit facility at interest rates ranging from 3.47% to 3.79%. In addition, UB issued a letter of credit for \$5.4 million in the first quarter of 2012 related to a contingent payment that will be made in the third quarter of 2012 for our TC acquisition. The credit facility would have expired and all outstanding loans would have matured on October 31, 2012, except that in September 2012, we entered into an amendment to extend the maturity date to October 31, 2013.

Loans under the credit facility that bear interest at the prime rate may be prepaid by us, in whole or in part, without penalty or premium. Loans that bear interest at LIBOR rates may be prepaid, in whole or in part, upon five business days' notice to UB and subject to a prepayment fee equal to the present value of the difference between the return that UB could obtain if it used the amount of such prepayment of principal to purchase regularly quoted securities issued by the United States at bid price, and the return UB would have received had the prepayment not been made.

All of our obligations under the credit facility are secured by substantially all of our property. All of our existing and future subsidiaries are required to guaranty our obligations under the credit facility, other than certain non-material subsidiaries. Such guarantees by existing and future subsidiaries are and will be secured by substantially all of the property of such subsidiaries.

Our credit facility contains customary covenants which limit our and, in some cases, certain of our subsidiaries' ability to, among other things, incur additional indebtedness or guarantee indebtedness of others, create liens on our assets, enter into mergers or consolidations, dispose of assets, pay dividends and make other distributions on our capital stock, and redeem and repurchase our capital stock, make investments, including acquisitions, and make capital expenditures. Our credit facility additionally contains customary affirmative covenants, including requirements to, among other things, take certain actions in the event we form or acquire new subsidiaries and use commercially reasonable efforts to ensure that certain material contracts permit the assignment of the contract to UB; subject in each case to customary exceptions and qualifications.

To maintain availability of funds under the credit facility, we pay UB a commitment fee on the unused portion of the credit facility. The commitment fee is equal to 0.25% of the unused portion per annum and is recorded as interest expense.

We are also required to comply with certain financial covenants relating to a quick ratio, monthly minimum 3-month EBITDA coverage and a quarterly cash flow coverage ratio. We are currently in compliance with all covenants under our credit facility.

The credit facility contains customary events of default, subject to customary cure periods for certain defaults, that include, among others, non-payment defaults, covenant defaults, material judgment defaults, bankruptcy and

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insolvency defaults, cross-defaults of certain other material indebtedness and inaccuracy of representations and warranties. Upon an event of default, UB may declare all or a portion of the outstanding obligations payable by us to be immediately due and payable and exercise other rights and remedies provided for under the credit facility.

Cash Flows

The following table presents information regarding our cash flows, cash and cash equivalents in 2009, 2010 and 2011 and the six months ended June 30, 2011 and 2012:

	Year Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012
	(in thousands)			(unaudited)	
Net cash provided by operating activities	\$ 31,075	\$ 20,476	\$ 55,189	\$ 18,513	\$ 15,601
Net cash (used in) provided by investing activities	(9,253)	(12,299)	(12,594)	(6,109)	2,722
Net cash (used in) provided by financing activities	(663)	2,842	7,746	7,235	88,396
Net increase in cash and cash equivalents	21,159	11,019	50,341	19,639	106,719
Cash and cash equivalents, end of period	\$ 93,261	\$ 104,280	\$ 154,621	\$ 123,919	\$ 261,340

Cash Flows from Operating Activities

	Year Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012
	(in thousands)			(unaudited)	
Net cash provided by operating activities	\$ 31,075	\$ 20,476	\$ 55,189	\$ 18,513	\$ 15,601
Net cash provided by operating activities decreased \$2.9 million for the six months ended June 30, 2012 as compared to the six months ended June 30, 2011, primarily due to the timing difference of receiving prefun ds from our clients for their new plan year and refunding our clients prefun ds from the prior plan year which had an impact of \$10.1 million when compared to the same period in the previous year, a \$2.5 million decrease from cash outflows for a payment made related to contingent consideration and a \$1.7 million decrease in net income, which were partially offset by an aggregate increase in amortization and change in contingent consideration of \$3.4 million and the timing of collections and seasonal run-out of revenue impacting accounts receivable and increases in cash flows from changes in the other operating assets and liabilities which had an impact of \$2.8 million. Decreases in cash provided by operating activities were further offset by a \$2.3 million increase in deferred tax assets, a \$1.7 million decrease in accounts payable and accrued expenses and a \$0.8 million increase in other liabilities.					

Net cash provided by operating activities in 2011 resulted primarily from our net income of \$33.3 million being adjusted for the following non-cash items: depreciation, amortization and change in contingent consideration aggregating \$14.5 million and stock-based compensation of \$2.2 million offset by a \$20.2 million increase in deferred tax assets, primarily as a result of releasing the valuation allowance. Cash from operating activities was further increased by \$28.9 million of customer obligations primarily due to the increase in our commuter elections, an increase in prefun ds and the timing of our billings and employer client payments. These cash flows were offset in part by a \$4.0 million increase in prepaid expenses and other current assets, primarily due to prepaid expenses related to our public offering.

Net cash provided by operating activities in 2010 resulted primarily from our net loss of \$17.3 million being adjusted for the following non-cash items: amortization of convertible debt discount of \$21.1 million, depreciation and amortization of \$11.9 million, change in the fair value of our Series C and Series E-1 warrants of \$5.4 million and stock-based compensation of \$2.4 million. We also experienced a \$1.5 million increase in prefun ds due to the

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timing of our billings and employer client payments as discussed in Liquidity and Capital Resources Prefunds. These cash flows were offset in part by a \$1.3 million change in deferred taxes primarily related to our PBS acquisition and a \$2.1 million increase in accounts receivable attributable to our increased revenue volume.

Net cash provided by operating activities in 2009 resulted in part from our net loss of \$0.6 million being adjusted for the following non-cash items: depreciation and amortization of \$13.0 million and stock-based compensation of \$2.5 million. We also experienced a \$12.9 million increase in customer obligations which was principally the result of an increase in the size of employee participants' commuter elections and commuter prefunds, a portion of which was the direct result of pre-tax transit limits being almost doubled in 2009 as compared to 2008, and a \$2.4 million decrease in accounts receivable attributable to improved collections.

Cash Flows from Investing Activities

	Year Ended December 31,			Six Months Ended	
	2009	2010	2011	June 30,	2012
	(in thousands)			(unaudited)	
Net cash (used in) provided by investing activities	\$ (9,253)	\$ (12,299)	\$ (12,594)	\$ (6,109)	\$ 2,722

Net cash used in investing activities consists primarily of our investment in internal use software that is capitalized prior to it being available for its intended use, capital expenditures and purchases of portfolios.

Net cash provided by investing activities increased \$8.8 million for the six months ended June 30, 2012 as compared to the six months ended June 30, 2011, primarily due to the cash received in the acquisition of TransitChek which had an impact of \$10.4 million when compared to the same period the previous year and changes in restricted cash which had an impact of \$0.8 million, partially offset by an increase in purchases of property and equipment of \$2.4 million, driven by increased spending on capitalized internal use software.

Net cash used in investing activities in 2011 was primarily a result of \$9.4 million of capitalized internal use software and purchased equipment principally related to enhancing the functionality of our platform and a \$1.9 million cash payment, net of cash received, made in connection with our FBM portfolio purchase. We also used cash to increase our restricted cash by \$1.3 million, in preparation for our CS portfolio purchase on January 3, 2012.

Net cash used in investing activities in 2010 was primarily a result of \$7.3 million of capitalized internal use software and purchased equipment, which was largely related to further upgrades to our product platform and control environment. Some of our major projects for the year included the implementation of mobile features for our platform, such as our mobile application for use on Apple iPhone® and iPad® devices, the final stage of the daily settlement system implementation, increased automation for our COBRA services and significant platform changes to accommodate unique client requirements. We also used \$5.0 million of cash, net of cash received, for payments made in connection with the purchases of CB, PBS and FBM.

Net cash used in investing activities in 2009 was principally due to \$6.6 million of capitalized internal use software and purchased equipment, which was largely related to our continued upgrades to our product platform and control environment. We used \$2.1 million of cash for a contingent payment made in connection with the purchase of CB. We also used \$0.6 million of cash to increase our restricted cash due to an increase in a cash secured letter of credit for one of our commuter employer clients as a result of increased employee participation.

Cash Flows from Financing Activities

	Year Ended December 31,			Six Months Ended	
	2009	2010	2011	June 30,	2012
	(in thousands)			(unaudited)	
Net cash (used in) provided by financing activities	\$ (663)	\$ 2,842	\$ 7,746	\$ 7,235	\$ 88,396

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Net cash provided by financing activities increased \$81.2 million for the six months ended June 30, 2012 as compared to the six months ended June 30, 2011, primarily due to the cash received from our initial public offering of \$62.6 million and an increase in borrowing on our line of credit of \$20.4 million, partially offset by an increase of \$1.8 million in payments made related to contingent consideration.

Net cash provided by financing activities in 2011 was due to \$12.1 million in draw downs on our credit facility to fund payments related to our contingent consideration payments for FBM and PBS portfolio purchases that took place in 2010, partially offset by the FBM contingent consideration payment of \$2.3 million and the PBS contingent consideration payment of \$2.0 million.

Net cash provided in financing activities in 2010 was due to drawing down on our credit facility to fund our acquisition of PBS. Net cash used in financing activities in 2009 reflected payments on capital leases on service delivery equipment and our purchase of treasury stock from a stockholder.

Recent Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-11, *Disclosures about Offsetting Assets and Liabilities*, which created new disclosure requirements about the nature of an entity's rights of offset and related arrangements associated with its financial instruments and derivative instruments. The disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods therein, with retrospective application required. The adoption of ASU 2011-11 may have an impact on us as to financial disclosure but will not have a material impact on our financial position or results of operations.

In September 2011, the FASB issued Accounting Standards Update, or ASU 2011-08, *Intangibles - Goodwill and Other (Topic 350): Testing Goodwill for Impairment*. The guidance in ASU 2011-08 is intended to reduce complexity and costs by allowing an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it should calculate the fair value of a reporting unit. If impairment is deemed more likely than not, management would perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. The amendments also improve previous guidance by expanding upon the examples of events and circumstances that an entity should consider between annual impairment tests in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Also, the amendments improve the examples of events and circumstances that an entity having a reporting unit with a zero or negative carrying amount should consider in determining whether to measure an impairment loss, if any, under the second step of the goodwill impairment test. The amendments in this ASU are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued. The adoption of ASU 2011-08 is not expected to have a material impact on our financial position or results of operations.

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The following table describes our contractual obligations as of June 30, 2012:

	Total	Less than 1 Year	1-3 Years	4-5 Years	More than 5 Years
Short-term debt obligations(1)	\$ 44,600	\$ 44,600	\$	\$	\$
Interest on short-term debt obligations(2)	933	933			
Operating lease obligations(3)	25,198	5,173	7,748	3,516	8,761
Acquisition payments(4)	22,342	14,524	7,618	200	
Total	\$ 93,073	65,230	\$ 15,366	\$ 3,716	\$ 8,761

- (1) Credit facility: \$50.0 million credit facility with a variable interest rate of prime rate plus 50 basis points per annum or LIBOR plus 300 basis points per annum. See Note 8 of our consolidated financial statements. In September 2012, the due date was extended from October 31, 2012 to October 31, 2013. The \$44.6 million outstanding principal amount is recorded net of debt issuance costs on our balance sheet and the debt issuance costs are not included in the table above.
- (2) Estimated interest payments assume the current weighted average interest rate of 3.76% per annum on a \$44.6 million principal amount. The extension of the credit facility's maturity date to October 31, 2013 is not reflected in the calculation of the estimated interest payments due as of June 30, 2012.
- (3) We lease facilities under non-cancelable operating leases expiring at various dates through 2023.
- (4) Estimated undiscounted contingent consideration for companies acquired in 2010 and 2012. See Note 3 of our consolidated financial statements.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

Disclosures about Market Risk

Market risk represents the risk of loss that may affect our financial position due to adverse changes in financial market prices and rates. We are exposed to market risks related to changes in interest rates.

As of June 30, 2012, we had cash and cash equivalents of \$261.3 million. These amounts consist of cash on deposit with banks and money market funds. The cash and cash equivalents are held for working capital purposes. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of these investments, we do not believe that changes in interest rates would have a material impact on our financial position and results of operations. However, declines in interest rates and cash balances will reduce future investment income.

Our exposure to market risk also relates to the increase or decrease in the amount of interest expense we must pay on our outstanding debt instruments. As of June 30, 2012, we had outstanding principal of \$44.6 million under our credit facility. Loans under our credit facility bear interest at a variable rate of the prime rate plus 0.5%, or, at our option, a fixed interest rate equal to the LIBOR rate for a period of either one, two, three or six months, if offered by UB, plus 3.0%.

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BUSINESS

Overview

We are a leading on-demand provider of tax-advantaged programs for consumer-directed health, commuter and other employee spending account benefits, or CDBs, in the United States. We administer and operate a broad array of CDBs, including spending account management programs such as health and dependent care Flexible Spending Accounts, or FSAs, Health Savings Accounts, or HSAs, Health Reimbursement Arrangements, or HRAs, and commuter benefits, such as transit and parking programs.

We deliver our CDB programs through a highly scalable Benefits-as-a-Service, or BaaS, delivery model that employer clients and their employee participants may access through a standard web browser on any internet-enabled device, including computers, smart phones and other mobile devices, such as tablet computers. Our on-demand delivery model eliminates the need for our employer clients to install and maintain hardware and software in order to support CDB programs and enables us to rapidly implement product enhancements across our entire user base.

Our CDB programs enable employees and their families to save money by using pre-tax dollars to pay for certain of their healthcare and commuter expenses. Employers financially benefit from our programs through reduced payroll taxes, even after factoring in our fees. Under our FSA, HSA and commuter programs, employee participants contribute funds from their pre-tax income to pay for qualified out-of-pocket healthcare expenses not fully covered by insurance, such as co-pays, deductibles and over-the-counter medical products or for commuting costs.

These employee contributions result in savings to both employees and employers. As an example, based on our average employee participant's annual FSA contribution of approximately \$1,400 and an assumed personal combined federal and state income tax rate of 35%, an employee participant will reduce his or her taxes by approximately \$490 per year by participating in an FSA. Our employer clients also realize payroll tax (i.e., FICA and Medicare) savings on the pre-tax contributions made by their employees. In the above FSA example, an employer client would save approximately \$64 per participant per year, even after the payment of our fees.

Under our HRA programs, employer clients provide their employee participants with a specified amount of available reimbursement funds to help their employee participants defray out-of-pocket medical expenses such as deductibles, co-insurance and co-payments. All amounts paid by the employer into HRAs are deductible by the employer as an ordinary business expense and are tax-free to the employee.

We believe there is significant potential for growth in the market we serve. In order to increase employee participation, we educate and advocate the use of CDB programs through a comprehensive online and offline approach. The higher the election rates in these CDB programs, the more employees save on income taxes and the more employers save on payroll taxes.

Our clients include many of the Fortune 100 and Fortune 500 and approximately 3,200 small- and medium-sized businesses, or SMBs. Our larger employer clients, which we refer to as enterprise clients, generally enter into three-year written service agreements and commit to pay fixed monthly fees that are set at the beginning of the contract term based on the number of employee participants enrolled in our CDB programs at the beginning of each annual enrollment period. For SMB clients, our agreements are typically for one-year terms and the monthly fee remains constant for the plan year unless there is a 10% or greater increase in the number of employee participants, in which case it is subject to upward revision. In addition, we derive a portion of our revenues from interchange fees that we receive when employee participants use the prepaid debit cards we provide to them for healthcare and commuter expenses. We market and sell our CDB programs through multiple channels, including direct sales to large enterprises, direct sales and through brokers to SMBs, and direct sales to industry purchasing and affiliate groups.

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At January 31, 2012, we had approximately 2.0 million employee participants from approximately 5,000 employer clients. We believe that January 31 is the most appropriate point-in-time measurement date for annual plan metrics. Although plan changes and the entry and exit of employers and participants from our programs are usually decided late in the calendar year during open enrollment to be effective on January 1, it is not unusual for employers to still be submitting updated files of participants in early January. While updates can be delayed past January, any changes from such late updates are usually minimal. Consequently, we believe the January 31 point-in-time measurement date is the most appropriate date to use as a baseline. In 2011, employee participants used over two million WageWorks prepaid debit cards. Through a combination of the acquisition and integration of smaller third party administrators, or TPAs, which we refer to as portfolio purchases, and organic growth, we grew our revenue from \$108.5 million in 2009 to \$115.0 million in 2010 and to \$135.6 million in 2011. Our revenues are highly diversified. Our revenue increased from \$69.2 million for the six months ended June 30, 2011 to \$88.1 million for the six months ended June 30, 2012. Our largest employer client represented only 3.0% of our 2011 revenues and our top 10 employer clients represented only 14.4% of our 2011 revenues. We have a recurring revenue model that has been highly predictable. For each of 2009, 2010 and 2011, clients that accounted for more than 90% of our revenues (excluding interchange fees and vendor commissions) during the year have remained under contract with us in the succeeding year. Our net loss was \$0.6 million and \$17.3 million in the years 2009 and 2010, respectively, and our net income was \$33.3 million in 2011. Our net income decreased from \$6.9 million for the first six months of 2011 to \$5.2 million for the first six months of 2012 primarily due to an increase in tax expense as a result of providing for taxes in the first six months of 2012 without a corresponding and offsetting valuation allowance, since we released the remaining valuation allowance through earnings in December 2011. Our Adjusted EBITDA grew from \$15.9 million in 2009 to \$22.4 million in 2010 and to \$30.3 million in 2011, which represent increases of 40% and 36%, respectively. Adjusted EBITDA increased from \$15.7 million for the first six months of 2011 to \$20.3 million for the first six months of 2012. For a discussion of Adjusted EBITDA and a reconciliation of net income (loss) to Adjusted EBITDA, see footnote 1 to Selected Consolidated Financial Information.

We completed an additional portfolio purchase in early 2012 and also completed an acquisition in February 2012.

Industry Overview***Rising Cost of Healthcare to Employers and Employees***

Healthcare costs for both employers and employees continue to increase dramatically. According to a 2012 Kaiser Family Foundation survey, since 2002, family premiums for employer-sponsored health coverage have increased by 97%. A 2011 Hewitt Associates report predicts that employers can expect average annual premium increases of 7.0% from 2011 to 2012. To mitigate the continuing rise in healthcare costs, employers are more frequently passing these costs on to employees by increasing deductibles, out-of-pocket limits and non-network provider cost sharing and by migrating to co-insurance models systems where employees pay a percentage of the out-of-pocket costs for each healthcare service. As a result, according to the Hewitt Associates report, average employee out-of-pocket healthcare costs are expected to increase 13.4% from 2011 to 2012.

Rising Commuter Costs and Impacts on the Environment

We believe that rising commuter costs and a new era of corporate social responsibility have also led to the creation of a variety of programs that are aimed at helping employees understand and reduce their carbon footprint by encouraging alternatives to driving to work. These alternatives include carpooling, cycling and the use of public transportation. According to a 2011 American Public Transportation Association report, public transportation is twice as fuel efficient as private automobiles at reducing annual fuel consumption. The report further notes that public transportation ridership increased by 34% from 1995 to 2009, compared to a 23% growth in the use of the nation's highways over the same period. As gasoline prices continue to rise, we believe employees will be more inclined to utilize public transportation as a means of commuting to work.

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Establishment of Tax-Advantaged Spending Accounts

Beginning in the late 1970 s, federal laws have been enacted to establish ways for employers to offer structured benefit plans to their employees that lessen overall healthcare and transportation costs through the use of tax-advantaged spending accounts.

Tax-advantaged spending accounts for healthcare were first authorized in 1978. The legislation established a set of rules under which an employer could offer a special benefit plan that allows employees to set aside a portion of their earnings on a pre-tax basis, which are exempt from income and payroll taxes, to pay for certain expenses that are primarily related to healthcare, but also cover dependent care, vision and dental expenses. This benefit was called a flex or cafeteria plan, and a participating employee s funds were placed into an FSA. In 2011, there were approximately 35 million active FSA accounts.

Subsequent legislation enacted in 1980 established HRAs, which are employer-funded spending accounts with rules and tax treatment that generally mirror FSAs, but allow employers to have greater control over eligible expenditure designations and plan administration. In 2003, the Medicare Prescription Drug, Improvement, and Modernization Act established another closely related product, the HSA. HSAs also offer tax-advantaged treatment for contributed funds, but include savings account features and are only available to individuals who are enrolled in a qualified High Deductible Health Plan, or HDHP. According to a 2012 Employee Benefit Research Institute report, the combined number of HSAs and HRAs was 1.3 million in 2006, 5.4 million in 2010 and 8.4 million in 2011.

Commuter benefits were established in 1998 to provide tax incentives to employees to encourage the use of mass transportation. As with tax-advantaged healthcare accounts, commuter accounts allow employee participants to set aside earnings on a pre-tax basis to cover commuter rail, subway, bus, commuter-related parking and eligible vanpool expenses. In 2009, the American Recovery and Reinvestment Act increased the monthly pre-tax benefit cap for commuter accounts from \$120 to \$230, a level that was maintained through 2011, and brought parity between allowable monthly parking and transit benefits. In 2012, the temporary extension of the \$230 monthly pre-tax benefit cap for commuter accounts expired and the cap was reduced from \$230 to \$125. It is anticipated that Congress will, however, consider new tax and transportation related legislation in early 2012 that could result, once again, in an increase of the commuter account benefit cap. In the meantime, the monthly parking benefit cap for 2012 was increased from \$230 to \$240 due to an automatic cost of living increase. According to a 2010 TransitCenter survey, an estimated 35% of employers offer commuter benefits.

Challenges of Tax-Advantaged CDBs for Employers

Employers face numerous challenges in implementing and administering CDBs, including:

High regulatory risks and related compliance costs. The rules and regulations applicable to implementing and administering CDBs in-house are complex and continually changing. Failure to comply can lead to disqualification of the entire plan, as well as severe penalties. We believe, based on our industry experience and interactions with other CDB providers including interactions with potential and actual employer clients, that most employers do not have the internal resources required to assure such compliance and the cost of obtaining such internal resources is high.

Education to increase employee usage of plan benefits. Given the complexity of CDBs, employers are challenged with effectively communicating plan benefits to employees in order to increase employee participation.

Effectiveness of benefit programs. In order to help employers maximize the value of these programs, employers need quality data and analysis to help them understand employee participation, measure the effectiveness and efficiency of their CDB programs and improve cost management.

If not successfully met, these challenges can diminish the value employees and employers receive from CDBs and can lead to unnecessary friction between employees and their employers.

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Fragmented Landscape of CDB Providers

The current market for administrators of CDBs is highly fragmented. Larger service providers, including health insurance carriers, payroll providers, human resources consulting firms and commercial banks, generally offer CDB programs as non-core offerings bundled with their main products and services. The technology these larger service providers employ for many CDBs is often licensed or outsourced. Their relative lack of focus on CDB plans often restricts the breadth of their offerings in the CDB area. As a result, many of these providers only offer healthcare benefits and do not offer commuter or other CDBs.

There are also hundreds of TPAs that provide administration services for CDBs. We believe many regional TPAs lack sufficient resources to rapidly implement new technologies or to tailor their operations and service offerings in response to evolving rules and regulations.

We believe that the increasing regulation of the healthcare industry, and the increased demand for a variety of tax-advantaged CDBs will lead employers to seek providers that have a principal focus on CDBs and can provide best-in-class, full-featured and scalable programs.

Our CDB Programs

We focus on providing CDB programs to employer clients of any size.

Our CDB programs enable our employer clients and their employee participants to achieve significant tax savings through the use of tax-advantaged spending programs. Using our CDB programs, employee participants contribute a portion of either their pre-tax income or employer-provided funds to pay for qualified out-of-pocket healthcare expenses not fully covered by insurance, such as co-pays, deductibles and over-the-counter medical products, as well as to pay for commuting expenses. Our employer clients also benefit financially from our programs through reduced payroll taxes, even after payment of our fees.

Our programs are designed to increase employee participation in employer clients' CDB offerings. We believe our employer clients and their employee participants benefit from our superior customer service, efficient workflow processes and advanced monitoring applications. The quality of our customer support has resulted in high levels of client satisfaction and service level performance. We employ a wide range of sophisticated tools to communicate available benefit options to employees and measure the effectiveness of CDB program performance.

We deliver our CDB programs through a BaaS model under which we host and maintain the benefits programs that we provide to our employer clients. Our on-demand delivery model enables employer clients and their employee participants to implement, access and use our proprietary software remotely through a standard web browser on any internet-enabled device, including computers, smart phones and other mobile devices, such as tablet computers. We are able to implement improvements to our programs in a rapid and uniform manner because updates and upgrades to our programs are managed by us on behalf of our clients. Our CDB programs are delivered through integrated platforms that eliminate the need to support multiple versions of our products and multiple websites, and enable us to focus more of our development resources and efforts on the creation of innovative new functionality and features for our employer clients and employee participants. We, therefore, believe that our on-demand model requires less up-front investment by our employer clients than traditional third-party software and hardware options, as well as less personnel resources and implementation services.

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The following is a summary of the principal benefits that our CDB programs offer to our employer clients and their employee participants:

	Principal Benefits
Employer Clients	<p>Achieve FICA and Medicare tax savings on employee payroll deductions through increased employee participation in FSA, HSA and commuter programs</p> <p>Realize tax deductions on contributions to employee HRAs</p> <p>Outsource the risk and cost of compliance with regulation and industry standards related to CDBs</p> <p>Help increase employee awareness of CDB programs</p> <p>Improve ability to monitor the effectiveness of CDB programs through robust reporting capabilities</p> <p>Enable ability to offer best-in-class CDB benefits that are not tied to a single insurance provider</p> <p>Eliminate cost of on-premises information technology infrastructure management, systems security and disaster recovery</p>
Employee Participants	<p>Encourage activities and behaviors that may result in a healthier and more socially responsible workforce</p> <p>Reduce after-tax out-of-pocket healthcare and commuting costs through tax-advantaged spending</p> <p>Manage CDBs through an easy to use online interface</p> <p>Enhance convenience through multiple options for the payment, submission and reimbursement of claims, including the use of a prepaid debit card</p>
Key Attributes of Our Business	<p>Access to a broader selection of CDB programs to customize their health package to meet their specific needs</p>

Key attributes of our business include the following:

Recurring revenue model with high visibility. Our revenue is derived almost entirely from recurring monthly fees paid by our employer clients. We typically sign three-year agreements with our enterprise clients and one-year agreements with our SMB clients and, for each of 2009, 2010 and 2011, employer clients that accounted for more than 90% of our revenues (excluding interchange fees and vendor commissions) during each year remained under contract with us in the succeeding year.

Focus on quality of service. Our focus is to consistently deliver the highest quality service to our employer clients and their employee participants, which primarily means providing employee participants with timely and accurate responses to their inquiries, claims submissions and other account transactions. We normally enter into service level agreements with our employer clients where we incur financial penalties if we fail to meet the call and claims processing service standards outlined in those agreements. We have exceeded our contractual service levels to our enterprise employer clients each month since May 2007. We typically process 99% of claims within two business days of receipt. This consistent record of service performance includes five consecutive Januarys, the month in which our call volume is substantially greater than the average month.

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Leading-edge scalable technology platforms. Our CDB programs employ an easy-to-use website interface that provides our employer clients with robust data and reporting capabilities to help them manage their benefits offerings and healthcare spending, and provides employee participants with direct access to their accounts, claims history and balance information. Employee participants can also submit claims and upload receipts online. Our highly scalable on-demand technology infrastructure supports employers of any size, from SMBs to Fortune 100 companies.

Ability to identify, execute and integrate portfolio purchases. As demonstrated by the five portfolio purchases and one acquisition we have made since 2007, we have a proven ability to successfully identify and execute portfolio purchases and integrate the operations of these complementary businesses to expand our employer client base. While we have encountered some challenges in integrating accounting functions in connection with certain of these portfolio purchases, as often times these businesses may have lacked effective controls prior to our acquisition, we have leveraged the efficiencies afforded by our on-demand software platform to cross-sell additional CDB products and services to acquired employer clients.

Experienced, proven management team. Our senior management team has significant operating and service delivery experience with industry-leading businesses in healthcare, such as Kaiser Permanente, transaction processing, such as Alliance Data Systems and First Data Corporation, and financial services, such as American Express. Since 2007, our management team has focused on making improvements to our CDB programs and the implementation of improved controls and processes. As a result, we have achieved significant operational efficiencies, consistently high service levels and improved client and participant satisfaction levels.

Large and highly diversified employer client base. Our employer clients include many of the Fortune 100 and Fortune 500. Our top 50 employer clients include industry leaders such as Comcast, Duke University, Ford Motor Company, Harley-Davidson, HCA, Interpublic Group, L-3 Communications, Lowe's Companies, MetLife, Morgan Stanley, the State of New York, North Shore Long Island Jewish Health System and the State of Wisconsin. Our largest employer client represented only 3.0% of our 2011 revenues and our top 10 employer clients represented only 14.4% of our 2011 revenues.

Focus on CDB programs. Our core business is providing a comprehensive array of full-featured CDB programs to employers. Our technology and development resources are exclusively dedicated to creating, enhancing and optimizing our CDB programs and technology platforms to better support our employer clients and their employee participants. In contrast, many of our competitors, which include health insurance carriers, human resources consulting firms and payroll providers, generally offer CDBs as non-core service offerings.

Our Strategy

Our objective is to enhance our position as a leading provider of CDB account management programs. The key elements of our growth strategy are to:

Increase employee adoption and usage. We believe that significant opportunities exist to substantially increase employee participation levels within our existing client base. As of the end of 2011, employee participation levels in FSA benefit programs that we serviced for top tier clients averaged 26%. We aim to increase employee enrollment through the continued promotion of our CDB programs, including through the education and communication programs that we offer to our employer clients, and launched an initiative in 2010 specifically focused on this effort.

Cross-sell new products to existing employer clients. We believe that our broad portfolio of CDB products and strong employer client relationships create a significant opportunity for us to cross-sell additional CDB programs to our existing employer clients. For example, many of our employer clients currently utilize us for only healthcare or commuter CDB programs, but not both. In 2010, we reorganized our sales team to provide for dedicated personnel focusing on the specialized cross-selling of healthcare programs to our existing commuter employer clients and vice versa.

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Capitalize on portfolio purchases. We intend to continue to execute our focused strategy to broaden our employer client base through portfolio purchases. There are several hundred regional TPA portfolios that we continually monitor and evaluate in order to maintain a robust pipeline of potential candidates for purchase. We have demonstrated our ability to successfully integrate complementary businesses, as evidenced by the five TPA portfolio purchases and one acquisition we have made since 2007. Portfolio purchases have been the principal driver of our revenue growth from 2009 through 2011.

Leverage multiple sales channels. We believe that we can continue to gain market share with both Fortune 1000 companies and SMBs by leveraging our multiple sales channels. Our enterprise sales force generates new large client account relationships through employer prospecting, consultant relationships and strategic relationships. We will also continue to use an extensive network of brokers to reach SMBs. We believe that there is a significant growth opportunity in this sales channel, as there are millions of SMBs throughout the United States and the penetration of CDBs in this population is much lower than that for larger companies.

Continually enhance our products and develop new products and functionality. We believe that our focus on CDB programs and the breadth of our client base has provided us with a deep understanding of our employer clients' needs. We believe that this knowledge enables us to provide innovative CDB programs to our employer clients and their employee participants. Our easy to use process for online claim submissions is an example of our innovation.

Starting in 2010, our growth strategy has shifted from a singular focus on adding new employer clients to also seeking to take advantage of our substantial base of existing employer clients and their employees who are eligible to participate in our CDB programs. This shift has included initiatives to increase participation in pre-tax healthcare programs by targeting awareness and education at non-participating eligible employees, and the addition of dedicated sales personnel to focus on the specialized cross-selling of healthcare programs to our existing commuter employer clients and vice versa.

Our Services

Flexible Spending Accounts

Healthcare

We offer flexible spending accounts, or FSAs, which are employer-sponsored CDBs that enable employees to set aside pre-tax dollars to pay for eligible healthcare expenses that are not generally covered by insurance, such as co-pays, deductibles and over-the-counter medical products, as well as vision expenses, orthodontia, medical devices and autism treatments. Employers benefit from payroll tax savings on the pre-tax FSA contributions from the employee.

During each annual open enrollment period, an employee elects an amount to be placed into an FSA for the following plan year, subject to any limits set by his or her employer, and that amount is then deducted in equal increments out of each paycheck on a pre-tax basis over the plan year. The entire annual election amount is available to the participant for use starting on the first day of the plan year and cannot be changed except for the occurrence of certain life events such as a birth, death, marriage or divorce. During the course of the plan year, we are able to automatically process a substantial majority of our employee participants' claims for reimbursement. The remaining claims for reimbursement are independently adjudicated by us to ensure that FSA funds are used only for qualified healthcare expenses. Any unused funds that remain in the account at the end of the plan year are forfeited by the employee participant and revert to the employer, and are generally used by the employer to defray the administrative expenses of the FSA plans. Forfeitures also reduce excess claims costs that may have been incurred by employee participants who voluntarily or involuntarily leave their employ before the end of a plan year.

Under current law, there is no statutory contribution limit for FSA plans. Rather, employers set the maximum amount of dollars that their employees can deposit into FSAs, which is typically \$3,000 to \$5,000.

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Employers set limits for two principal reasons. First, the accounts must be structured in a way that prevents highly compensated employees from benefiting more than other employees. Setting limits helps ensure that highly compensated employees do not make higher elections that would threaten the plan's nondiscriminatory status. Second, regulations governing healthcare FSAs require that a participant's full annual election be available for use on the first day of the plan year, so employers utilize limits to minimize their risk in the event they are not able to recover the entire amount of their employee participants' elections through payroll deductions made over the course of the plan year.

The Affordable Care Act provides that, beginning January 1, 2013, there will be a \$2,500 limit, indexed to inflation, on pre-tax dollar employee contributions made to a healthcare FSA. Employers themselves will, however, be able to contribute additional amounts in excess of this statutory limit, and may choose to do so in an effort to mitigate the impact of rising healthcare costs on their employees.

Dependent Care

We also offer FSA programs for dependent care plans. These plans allow employees to set aside pre-tax dollars to pay for eligible dependent care expenses, which typically include child care or day care expenses but may also include expenses incurred from adult and elder care. Current laws and regulations limit the amount of pre-tax dollars employees can contribute to dependent care FSAs to \$5,000 per tax year. Like healthcare FSAs, employers can also contribute funds to employees' dependent care FSAs, subject to a statutory \$5,000 annual limit on total contributions. As with healthcare FSAs, employers realize payroll tax savings on the pre-tax dependent care FSA contributions made by their employees.

Health Reimbursement Arrangements

We offer employer-funded health reimbursement arrangements, or HRAs. Under HRAs, employers provide their employees with a specified amount of reimbursement funds that are available to help employees defray their out-of-pocket healthcare expenses, such as deductibles, co-insurance and co-payments. HRAs may only be funded by employers and, while there is no limitation on how much employers may contribute, employers are required to establish the programs in such a way as to prevent discrimination in favor of highly compensated employees. HRAs can be customized by employers so employers have the freedom to determine what expenses are eligible for reimbursement under these arrangements. At the end of the plan year, employers have the option to allow all, or a portion, of the unused funds to roll over and accumulate year-to-year if not spent. All amounts paid by employers into HRAs are deductible by the employer and tax-free to the employee.

Health Savings Accounts

We also administer health savings accounts, or HSAs, for employers that allow employee participants to invest funds to be used for qualified healthcare expenses at any time without federal tax liability or penalty. Such funds are also exempt from payroll taxes for employers. Both employees and employers can make contributions to an HSA. HSA funds are held by a custodian, accumulate year-to-year if not spent and are portable if a participant leaves his employer. Our HSA programs are designed to offer employers a choice of third party custodian to hold the funds as well as a variety of investment options within each custodial offering that enables employers the opportunity to explore a broader assortment of funds to offer their employees.

In order to be eligible for an HSA, an employee must be enrolled in a qualified HDHP that is HSA-compatible and not be covered by any other impermissible coverage. HSAs have annual contribution limits. For 2012, the annual HSA contribution limit is \$3,100 for an individual and \$6,250 for a family, with allowable catch-up annual contributions of \$1,000 for those aged 55 and older so that those individuals can accumulate adequate funds to meet their healthcare expense obligations. Withdrawals for non-medical expenses are treated similarly to those in an individual retirement account. Specifically, such withdrawals may provide tax advantages if taken after retirement age, and may incur penalties if taken earlier.

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Commuter Programs

We also offer qualified transportation fringe benefits. The federal tax code currently permits employers to provide the following commuter benefits to employees on a tax-free basis:

qualified parking;

transit passes;

transportation in a commuter highway vehicle, or vanpooling, if such transportation is in connection with travel between the employee's residence and place of employment; and

qualified bicycle commuting reimbursement.

For most commuter benefits, the maximum monthly amount that employees can exclude from income tax is subject to a statutory limit that is periodically adjusted for inflation. For 2012, the monthly maximum is \$125 for transit or vanpooling, \$240 for parking and \$20 for bicycle reimbursement.

We offer five variations of pre-tax commuter benefit programs: Commuter Express, Commuter Order, Commuter Account, Premium and Basic. Each of these programs is described below.

While these programs differ in terms of funding, implementation and available services, they include the following common features unless otherwise noted:

home delivery of transit passes and vouchers (other than Basic);

electronic loading of transit agency smartcards (where available) (other than Basic);

an express electronic payment feature for selected transit and vanpool operators (other than Premium and Basic);

access to transit vouchers (where available and accepted);

Commuter Card, a prepaid debit card used to pay for transit purchases or parking expenses;

Pay My Parking, a direct monthly payment to parking providers for eligible parking (other than Premium and Basic);

Park-n-Ride Support, which provides parking at or near transit stations or stops;

a cash reimbursement process for parking, vanpool, and certain other transit expenses (other than Basic); and

employer managed parking, which includes support for employer owned, managed, or leased parking, including customization capability by parking facility (other than Premium and Basic).

Under our Commuter Express program, which we target to SMBs, employers create transit and parking accounts on behalf of their employees using a web-based application on our proprietary platform. Employees then designate a monthly election amount, the employer submits the appropriate funds to us and we deposit those funds onto a prepaid debit card that we provide to the employee participants, which can be used to make transit or parking purchases at eligible locations. All such employee elections are exempt from income tax and the employer recognizes a financial benefit because it does not pay FICA or Medicare tax on amounts contributed by its employees. Employees may also supplement the amounts in their account with their own personal funds, although such supplemental funds are contributed on an after-tax basis.

Under our Commuter Order program, which we target to medium-sized and larger enterprise clients, employees place orders for transit, vanpool or parking benefits through our website or our toll-free customer service center. Employers pay us for transit and parking orders in advance and reimburse themselves through payroll deductions from the participants, which are exempt from payroll and income taxes.

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Under our Commuter Account program, which we target to medium-sized and larger enterprise clients, and particularly to those clients in the public sector, retail and service industries, employees make payroll deduction elections that employers use to fund accounts that we maintain. These deductions are exempt from payroll and income taxes. Participants use the funds in their accounts either automatically to fund a prepaid debit card that can be used to make transit or parking purchases at eligible locations or to purchase a transit or parking pass directly on our website. In addition to the payroll deductions, employees may also supplement the amounts in their account with their own personal funds, although such supplemental funds are contributed on an after-tax basis.

Under our Premium program, which we target primarily to SMBs, employer clients offer their employees the ability to enroll in a variety of pre-tax commuter benefit programs through a web-based application on our proprietary TransitChek Account Management System (TAMS®). Through TAMS®, employee participants may enroll and create an account for transit, parking and bicycle benefits. Employees designate a monthly election amount and the employer submits the appropriate funds to us, which are then used to fund the employees' selected benefit product. The transit and parking benefits may be offered by employers as a monthly pre-tax election deducted from an employee participant's salary, an employer paid fringe benefit on which employees pay no taxes, or a combination of both. The bicycle benefit may only be offered as an employer paid fringe benefit. In all cases, the elections are exempt from federal income tax and, in most cases, state income tax as well. The employer recognizes a financial benefit because it does not pay FICA or Medicare tax on amounts contributed by its employees. Once enrolled, employee participants may also manage their account online on TAMS®. All products are sent directly to the employee participants' home.

Under our Basic program, employee participants enroll through their employers for pre-tax commuter benefit programs. Employers may offer only transit and parking benefits under this program. These benefits may be offered as a monthly pre-tax election deducted from an employee's salary, an employer paid fringe benefit on which employees pay no taxes, or a combination of both. Employer clients order products on behalf of their employees and handle the administration and distribution of the benefit to their employee participants. In all cases, the elections are exempt from federal income tax and, in most cases, state income tax as well. The employer recognizes a financial benefit because it does not pay FICA or Medicare tax on amounts contributed by its employees.

Our commuter programs include a parking catalog with over 3,200 selectable locations and purchasable transit products from over 660 transit operators covering every major metropolitan area. At January 31, 2012, we offered over 133,000 different transportation products and we fulfill approximately 6.8 million commuter orders, including passes, smartcards, parking payments, vanpool vouchers and commuter cards, to commuters on an annual basis. We sell our commuter program to employers of all sizes and industries.

COBRA

We offer Consolidated Omnibus Budget Reconciliation Act, or COBRA, continuation services to employer clients to meet the employer's obligation to make available continuation of coverage for participants who are no longer eligible for the employer's COBRA covered benefits which includes medical, dental, vision, HRAs and certain healthcare FSAs. COBRA requires employers to make health coverage available for terminated employees for a period of up to 36 months post-termination. As part of our COBRA program, we offer a direct billing service where former employee participants pay for coverage they elect to continue. We handle the accounting and customer service for these separated employees, as well as interfacing with the carrier regarding the employees' eligibility. At January 31, 2012, we provided COBRA services to approximately 750 employer clients.

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Our Employer Clients

As of January 31, 2012, we had approximately 5,000 employer clients across a broad range of industries with approximately 2.0 million participating employees in all 50 states. Our employer clients include many of the Fortune 100 and Fortune 500 and approximately 3,200 SMBs.

Our top 50 employer clients include Comcast, Duke University, Ford Motor Company, Harley-Davidson, HCA, Interpublic Group, L-3 Communications, Lowe's Companies, MetLife, Morgan Stanley, the State of New York, North Shore Long Island Jewish Health System and the State of Wisconsin.

Our Technology Platforms

We run our services on two distinct on-demand technology platforms that have been designed to be highly scalable, and we closely monitor utilization of all aspects of our platforms for capacity planning purposes. Our existing infrastructure has been designed with sufficient capacity to meet our current and planned future needs.

The majority of our accounts run on our integrated and scalable proprietary platform, which we call our v5 platform. We generally use our v5 platform for medium-sized and enterprise clients. Our v5 platform supports all account administrative functions and provides integration with the systems used by employer clients, payment networks, health plans and key suppliers. Our v5 platform offers employer clients and employee participants a variety of payment features, in addition to traditional reimbursement, for our healthcare, commuter and other employee spending plans. Our v5 platform features a flexible, rules-based engine that includes multi-wallet functionality and is highly configurable to accommodate custom client plan designs and service requests. This multi-wallet functionality allows us to include more than one type of healthcare account (FSA, HRA and HSA) on one card, and helps ensure that funds that are otherwise subject to forfeiture at the end of a plan year are used first to pay for eligible expenses. Our v5 platform also allows for automated file interfacing with clients and external vendors, including card processors, custodian banks, health plan providers, claims and payment vendors. We have a daily settlement system and have implemented internal reporting and monitoring systems to ensure quality control on a daily basis.

In addition to our v5 platform, we also operate a technology platform known as WinFlexOne, which has been specifically designed and enhanced to address the needs of SMBs. While the overall features and capabilities of WinFlexOne are comparable to v5, WinFlexOne utilizes a simpler set of interfaces and product configurations that better accommodate the more limited administrative capabilities and needs of small employers.

In 2010, we released our mobile website to support our healthcare, commuter and COBRA products. Participants can view summary and detailed plan information, including card and account balances, important messages and alerts via our mobile site. We are currently enhancing our mobile site and expect to continue releasing new functionality in the future.

We recently deployed a mobile application that enables employee participants to access their accounts and submit healthcare and dependent care claims as well as healthcare debit card receipts. Employee participants can securely send digital photos of their receipts to verify expenses and debit card transactions directly from their iPhone®, iPad®, Android and Blackberry® devices.

Operations

Operation Support Services

We provide operational support services to our clients, including customer support center servicing and claims processing.

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Our customer support center servicing team is responsible for handling all incoming calls from our employee participants and is focused on continually improving the participants' customer service experience. Our team is trained to provide support on all our product offerings and is cross trained to support our claims servicing team. The customer support center servicing team is responsible for resolving any issues or problems an employee participant may have, including: education as to how our programs work; to what benefits an employee participant may be entitled; how to submit a claim for reimbursement; and why an employee participant may need to provide additional detail before a particular transaction is approved. We also have an executive escalations team that is trained to respond to any significant service issues that arise. Our customer support center team serviced over 2.3 million calls in 2011.

Our claims servicing team is responsible for processing all incoming claims for payment or reimbursement directly to providers or participants. This team reviews and adjudicates claims to ensure they meet all compliance and employer plan requirements and communicates with participants regarding the status of their claims using our in-house claims center technology tool. Like the customer support center servicing team, the claims servicing team is trained to support the customer support center servicing team when demand dictates. In 2011, the claims servicing team processed over 4.8 million claims and card use verification forms.

In an effort to increase our service efficiency and maintain our high-quality high-touch approach, we have outsourced and trained additional resources that we can use to support our customer support center and claims services teams during busy times such as open enrollment. All of these outsourced resources go through the same rigorous training as our own customer support center and claims servicing teams, and we believe that they provide the same level of quality service as our own employees.

Our operations support team is also responsible for processing and coordinating all activities required to support our high volume transaction business, including:

managing prepaid funds and reimbursement payments from client employers to settle participant transactions;

monitoring all card spending, authorizations and settlements with the transaction processors;

delivering electronic and paper statements directly to participants;

delivering explanation of benefits forms directly to participants;

delivering healthcare and commuter cards and passes directly to participants; and

managing process improvement projects across our organization.

Our operations support team utilizes both our v5 and WinFlexOne on-demand platforms to deliver products and services to clients and participants. In addition, we have supporting applications provided by third party vendors, the most significant of which is Fidelity National Information Services, which provides card network switching and settlement services, and Fiserv, Inc., which handles fulfillment of our printed healthcare statements, explanation of benefits and payment statements and open enrollment guides.

In 2011, our operations team delivered over 1.5 million healthcare and commuter prepaid debit cards, and fulfilled over 6.8 million commuter products to employees.

As part of our Go Green initiative to reduce our paper consumption and carbon footprint, we took steps to significantly reduce the use of paper statements as a means of communicating with our enterprise participant base beginning in late 2010. We started notifying employee participants via e-mail that they could access our online participant account portal that would provide them with 24/7 on demand access to balance information and all other account detail. We continue to mail paper statements and explanations of benefits to our enterprise participants without an email address on file with us, who receive reimbursements via a live check, or who request to receive paper statements, but this effort has reduced our use and delivery of paper statements to our enterprise participant base by 88% from 2010 to 2011.

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We also have a professional services team that is responsible for coordinating all activities related to the implementation, transition and on-board of new employer clients, assisting our existing clients with the addition of new services to their accounts and transitioning clients that we acquire from portfolio purchases to our platforms. This team also coordinates project planning to ensure that the startup of new programs coincide with the employer client's new plan year and acts as a client liaison to keep the client informed of the implementation status. In addition, our professional services team coordinates the completion of requests for proposals in response to new business prospects and works directly with all other functions in our organization to ensure each employer client receives consistent quality service.

Employer Client Services

We assign each employer client to a regionally aligned account team with a relationship manager who functions as the client's single point of contact. Our relationship managers are trained on all of our account offerings and receive prompt updates from internal subject matter experts on how regulatory or operational changes may impact a particular program or procedure. Our account service consultants, who are responsible for day-to-day management of client data, and our service account representatives, who are subject matter experts on new or specific aspects of our business, work closely with the relationship manager to ensure that our employer clients receive high-quality consultative service.

We provide assistance to our enterprise clients with their open enrollment processes. Our employer clients have an annual open enrollment period during which their employees have the opportunity to enroll, re-enroll or change their benefit elections for the upcoming plan year. We provide our employer clients with tools, such as educational information, calculators, video, webinars and onsite support to help facilitate their open enrollment and help drive employee participation in our programs.

We also provide both pre- and post-enrollment consultation services to employer clients to ensure that they utilize our services in a way that fits with their overall approach to employee benefit plans for the upcoming year. These consultations include providing employer clients with robust data regarding spend patterns, participation and service utilization, such as website usage, online claims submissions and participant feedback, to ensure maximum employee participation in their benefits programs. Our employer client services team also ensures that any platform or product changes are properly communicated to and adopted by our clients. Examples of these changes include service enhancements, such as online claims processing, the launch of our mobile application and website process changes.

We have relationships with a significant number of regional transit authorities, and have a large catalog of commuter pass offerings. Our employer client services team ensures that our commuter clients' employee participants are kept informed about rate changes, new pricing schemes and the adoption of new technologies, such as smart cards.

Sales and Business Development

We grow our employer client base through our various sales channels and through other business development efforts.

Sales

We sell our CDB programs to our employer clients through three different sales channels, each of which targets a distinct group of clients.

Enterprise Sales. Our enterprise sales force targets Fortune 1000 companies and generates new large account relationships through employer prospecting, consultant relationships and strategic partnerships. Our sales process includes responding to requests for proposals, making client presentations and providing demonstrations of our v5 platform, and is focused on both securing new accounts as well as cross-selling additional products to existing clients.

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SMB Distribution Channel. Our SMB distribution channel complements our enterprise sales channel and consists of third party advisors, including insurance agents and benefits consultants who typically have two to three enterprise clients and several hundred smaller employer clients, and institutional resellers, including regional and national insurance carriers, health plans, payroll providers, commercial banks and TPAs, who sell our CDB programs to smaller employers along with their own complementary products. We provide CDB programs to our resellers who either rebrand our programs under their own name or co-brand the programs with us.

Group Purchasing Organizations. We also sell our programs through group purchasing organizations in which we negotiate a standard service contract with group purchasing organizations that are formed by industry specific employers to cover their members. Once the standard contract and pricing have been negotiated, we are able to add additional employers that are members of the group at a low incremental cost.

Business Development

In addition to our sales channels, we utilize portfolio purchases as a business development strategy to broaden our employer client base and to acquire new employer clients. Since 2007, we have purchased CDB portfolios of five TPAs: CB, MHM, PBS, FBM and CS. In addition, we completed one acquisition, TC. We migrate acquired clients to our proprietary technology platforms over time following the completion of a portfolio purchase. The acquired portfolios often contain a mix of large employer clients and SMB clients. In general, larger clients will be transitioned to our v5 platform and smaller clients will be transitioned to the WinFlexOne platform. This process is usually completed over a 12-to-24-month period. In connection with these portfolio purchases, we have leveraged the ease of integration and efficiencies afforded by our on-demand software platforms and cross-sold additional CDB products and services to many acquired employer clients.

Marketing

We market ourselves as a provider of CDB programs and services through three primary channels.

Public Communications

Our public communications marketing efforts include:

Our website, which includes information about WageWorks, our CDB programs and developments in the CDB industry, generally;

Our nationwide media campaign to educate consumers about FSAs, which includes a consumer website, utilization of spokespersons and broadcast and print media stories;

Targeted email and multimedia campaigns to select audiences through leading trade industry publications;

Involvement with various industry organizations; and

Participation in trade shows, conferences and organizations, such as the Employers Council on Flexible Compensation, the Special Interest Group for IIAS Standards and the Society of Human Resource Management.

Client Communications

Our client communications marketing initiatives include:

Publication of a monthly client newsletter;

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Providing clients with educational programs, such as webinars and white papers;

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Creating education and awareness tools for employees to support clients' annual open enrollment processes; and

Providing clients with regulatory updates and guidance.

Participant Communications

Our participant communications marketing efforts include:

Providing open enrollment materials that are easy for participants to understand and complete;

Preparing welcome materials and introductory guides for new participants; and

Providing ongoing educational resources for participants regarding program features, benefits and regulatory changes.

We also regularly engage in advocacy efforts to educate legislators and regulators about the importance of retaining and expanding the availability of CDBs for employees. For example, during the healthcare reform efforts in 2009, we led an industry-wide initiative that focused on creating awareness amongst legislators about the consumer benefits associated with flexible spending programs and other healthcare-related benefits accounts. We continue to work with the industry and legislators to improve mechanical aspects of CDBs, including trying to eliminate the forfeiture rule associated with FSAs and reestablishing parity of the monthly pre-tax benefit caps for the parking and transit statutory limits.

Government Regulation

Our business is subject to extensive, complex and rapidly changing federal and state laws and regulations.

IRS Regulations

We are subject to applicable Internal Revenue Service regulations, which lay the foundation for tax savings and eligible expenses under the CDB programs we administer. Each year, the IRS issues guidance regarding employee plans.

ERISA

Certain of our CDB programs are covered by the Employee Retirement Income Security Act of 1974, as amended, or ERISA, which governs the structure of employee benefits plans. ERISA does not apply to dependent care FSAs, HSAs or any of our commuter programs, and does not typically apply to agreements with churches or governments. ERISA generally imposes extensive reporting requirements on employers, as well as an obligation to provide detailed disclosure to covered individuals, which includes both employees and beneficiaries. The Department of Labor can bring enforcement actions or assess penalties against employers for failing to comply with ERISA's requirements.

HIPAA, Privacy and Data Security Regulations

In connection with processing data on behalf of our clients and participants, we frequently undertake or are subject to specific compliance obligations under privacy and data security-related laws, including the Health Insurance Portability and Accountability Act of 1996, or HIPAA, and related state laws. We are also subject to federal and state security breach notification laws, as well as state laws regulating the processing of personal information, including laws governing the collection, use and disclosure of social security numbers and related identifiers. As part of the payment-related aspects of our business, we may also undertake security-related obligations arising out of the Gramm-Leach-Bliley Act and the Payment Card Industry guidelines applicable to card systems.

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Department of Labor

The Department of Labor, or the DOL, is responsible for issuing guidance under any component plans that are subject to ERISA, including healthcare FSAs and HRAs.

The DOL issues technical releases that apply to employee benefit plans generally. In addition, in response to a request by an individual or an organization, the DOL's Employee Benefits Security Administration may issue an advisory opinion that interprets and applies ERISA to a specific situation, including issues related to consumer-directed healthcare accounts.

Centers for Medicare and Medicaid Services Regulations

The Centers for Medicare and Medicaid Services, or CMS, is heavily involved in the oversight of the plans we administer as a division of the Department of Health and Human Services. Other than ERISA provisions relating to HIPAA, which are enforced by the Department of Labor, and the provisions of the Internal Revenue Code of 1986, as amended, or the Code, related to HIPAA, which are enforced by the Department of Treasury, CMS has primary responsibility for enforcement and implementation of HIPAA and many of the requirements of health reform.

Healthcare Reform

In March 2010, the federal government enacted significant reforms to healthcare legislation through the Patient Protection and Affordable Care Act, or PPACA, and the Healthcare and Education Reconciliation Act of 2010, or HCERA. These laws amended various provisions in many federal laws, including the Code and ERISA. These amendments include numerous coverage changes affecting group health plans, which now apply to insurers and governmental plans, as well as employer-sponsored health plans, including self-insured plans.

Dodd-Frank Act and Durbin Amendment

In July 2010, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, which includes the Durbin Amendment to the Electronic Fund Transfer Act. On June 29, 2011, final rules were issued that implement interchange transaction fee restrictions and prohibitions against payment card network exclusivity arrangements and transaction routing restrictions related to the processing of electronic debit transactions. Although the rules do not include an explicit exemption for health benefit debit cards, they do contain a general purpose reloadable prepaid card exception that exempts almost all of our CDB programs. In addition, the rules call for a delay in the implementation date of the network exclusivity rules until April 1, 2013. We do not currently expect that these rules will have, or are reasonably likely to have, a material adverse impact on our financial condition or operating results.

Competition

The market for CDBs is highly competitive, rapidly evolving and fragmented. Key categories of competitors include:

National CDB specialists, such as TASC or SHPS, Inc.;

Health insurance carriers, such as Aetna or UHC;

Human resources consulting firms, such as Aon Hewitt;

Payroll providers, such as ADP or Ceridian;

Small regional TPAs focused on CDBs; and

Commercial banks, such as Bank of America.

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CDB sales opportunities are presented through a number of different channels and often involve direct competition and requests for proposal processes. Many of our competitors, such as health insurance carriers, payroll providers, human resources consulting firms and commercial banks, offer CDB programs as non-core offerings bundled with their main products and services. We also compete against many regional TPAs who often lack sufficient resources to rapidly implement new technologies or to tailor their operations and service offerings in response to evolving rules and regulations. We further compete against the limited number of other CDB specialists.

Our ability to compete successfully depends on a number of factors, including:

our products performance and cost relative to that of our competitors;

the quality of service that we provide to our employer clients and their employee participants;

our ability to easily identify, acquire and integrate client portfolio purchases; and

our industry leadership and expertise.

Some of our competitors have longer operating histories and significantly greater financial, technical, marketing and other resources than we do. As a result, some of these competitors may choose to devote greater resources to the development, promotion, sale and support of their products and services. We believe our focus on CDB programs, our high quality service and our highly scalable BaaS delivery model are the principal basis on which we can compete in the CDB market. We cannot assure you that our products will continue to compete favorably or that we will be successful in the face of increasing competition from new products and enhancements introduced by our existing competitors or new companies entering our market.

Intellectual Property

Our success depends in part on our ability to protect our core technology and intellectual property. To accomplish this, we rely on a combination of patent laws, trade secrets, including know-how, employee and third party nondisclosure agreements, copyright laws, trademarks, intellectual property licenses and other contractual rights to establish and protect our proprietary rights in our technology. We have one issued patent which expires in 2027.

Despite our efforts to preserve and protect our proprietary and intellectual property rights, unauthorized third parties may attempt to copy, reverse engineer, or otherwise obtain portions of our products. Competitors may attempt to develop similar products that could compete in the same market as our products. Unauthorized disclosure of our confidential information by our employees or third parties could occur.

Third-party infringement claims are also possible in our industry, especially as software functionality and features expand, evolve, and overlap with other industry segments. Current and future competitors, as well as non-practicing patent holders, could claim at any time that some or all of our products infringe on patents they now hold or might obtain, or be issued in the future.

Employees

At June 30, 2012, we had 910 employees, including 871 full-time employees, 22 part-time employees and 17 temporary or seasonal employees. There are 120 employees located in our Northern California headquarters and the remainder are located in our various other offices throughout the United States or work remotely from various locations. None of our employees is currently represented by labor unions or is covered by a collective bargaining agreement with respect to his or her employment. To date we have not experienced any work stoppages, and we consider our relationship with our employees to be good.

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Legal Proceedings

From time-to-time, we are subject to various legal proceedings that arise in the normal course of our business activities. In addition, from time-to-time, third parties may assert intellectual property infringement claims against us in the form of letters and other forms of communication. As of the date of this prospectus, we are not a party to any litigation whereby the outcome of which, if determined adversely to us, would individually or in the aggregate be reasonably expected to have a material adverse effect on our results of operations, prospects, cash flows, financial position or brand.

Facilities

We do not currently own any of our facilities. Our corporate headquarters are located in San Mateo, California where we occupy approximately 38,249 square feet of space under a lease that expires in December 2014. We have additional facilities in Arizona, California, Colorado, Florida, Kansas and Wisconsin under various leases that expire between November 30, 2012 and November 30, 2015. We believe that our facilities are adequate for our current needs and that suitable additional or substitute space will be available as needed to accommodate planned expansion of our operations. In the first quarter of 2012, we assumed additional leases for the two transactions that we completed earlier in 2012.

Table of Contents**MANAGEMENT****Executive Officers and Directors**

Our executive officers and directors, and their ages and positions as of June 30, 2012, are as set forth below:

Name	Age	Position
Joseph L. Jackson	51	Chief Executive Officer and Director
Richard T. Green	53	Chief Financial Officer
Edgar O. Montes	51	Senior Vice President, Service Delivery Operations
Kimberly L. Jackson	44	Senior Vice President, General Counsel and Secretary
Richard M. Berkeley(3)	60	Director
Thomas A. Bevilacqua(2)(3)	55	Director
Bruce G. Bodaken(1)	60	Director
Mariann Byerwalter(1)	51	Director
Jerome D. Gramaglia(2)	56	Director
John W. Larson(3)	77	Director
Edward C. Nafus(1)(2)	71	Director

- (1) Member of our audit committee
(2) Member of our compensation committee
(3) Member of our nominating and corporate governance committee

Executive Officers

Joseph L. Jackson has served as our Chief Executive Officer, and as a member of our board of directors, since February 2007. Prior to joining us, Mr. Jackson served in various roles at First Data Corporation, a provider of payment processing services, from January 1983 until March 2006, most recently as President of Commercial Services for its Western Union subsidiary. Mr. Jackson holds a B.S. in Business Administration from the University of Nebraska. We believe that Mr. Jackson possesses specific attributes that qualify him to serve as a member of our board of directors, including his past business experience and his perspective as our Chief Executive Officer, which brings operational expertise to our board of directors.

Richard T. Green has served as our Chief Financial Officer since December 2008. Prior to joining us, Mr. Green served as Chief Financial Officer for Vertex Business Services N.A., a leading global outsourcing company, from July 2008 to December 2008, and as Chief Financial Officer of the Utility Services Division of Alliance Data Systems, a provider of loyalty marketing solutions derived from transaction-rich data, from March 2000 to July 2008. Mr. Green holds a Masters in Computer Systems Management from Creighton University and an M.B.A. and a B.S.B.A. from the University of Nebraska.

Edgar O. Montes has served as our Senior Vice President, Service Delivery Operations since March 2007, and as our Vice President, Operations from November 2006 until March 2007. Prior to joining us, Mr. Montes served in various positions with American Express, most recently as Vice President Customer Service, where he was responsible for overseeing customer service, from December 1982 until November 2006. Mr. Montes holds an M.B.A., a B.S. in Accounting and a B.S. in Real Estate from Arizona State University.

Kimberly L. Jackson has served as our Senior Vice President, General Counsel and Secretary since March 2008. Prior to joining us, Ms. Jackson served as Senior Corporate Counsel for Aricent Inc., a leading communications software company, from May 2007 to March 2008, where she advised Aricent on legal matters, and prior to that as Associate General Counsel for KLA-Tencor Corporation, a provider of yield management and process control solutions for semiconductor manufacturing and related industries, from April 2000 to May 2007, where she advised KLA-Tencor on legal matters. Ms. Jackson holds a J.D. from the University of the Pacific, McGeorge School of Law and a B.A. in Political Science from the University of California, Santa Barbara.

Table of Contents**Board of Directors**

Richard M. Berkeley has served as a member of our board of directors since March 2005, and as a member of our nominating and corporate governance committee since July 2005. Mr. Berkeley has served as a managing member of Camden Partners Holdings, LLC, a growth private equity firm, since October 2002, where he focuses on investments in the business and financial services, healthcare and education markets. Prior to joining Camden Partners, Mr. Berkeley spent 19 years with Alex. Brown & Sons, Incorporated and its successor organizations, Bankers Trust Corporation and Deutsche Bank Securities, Inc., where he was responsible for the origination, structuring and consummation of private equity financings for public and private companies. From December 2005 to June 2012, he served on the board of directors of RealPage, Inc., a leading provider of on demand software solutions for the rental housing industry, and has served or is serving on the boards of directors of a number of private companies, educational institutions and charitable organizations. Mr. Berkeley served as an officer in the United States Air Force between 1974 and 1976. He received an M.B.A., a J.D. and a B.A. in History from the University of Virginia. We believe that Mr. Berkeley possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as a member of our nominating and corporate governance committee, including his extensive experience in business and investing and knowledge of equity financings.

Thomas A. Bevilacqua has served as a member of our board of directors since November 2009, as a member of our compensation committee since February 2010 and as a member of our nominating and corporate governance committee since February 2011. Mr. Bevilacqua has served as a Managing Director and Group Co-leader, Information Technology with VantagePoint Capital Partners, a venture capital firm, since November 2007, where he focuses on investments in the Internet and information technology market. Prior to joining VantagePoint, Mr. Bevilacqua served as Executive Vice President of E*TRADE Financial from 1997 to 2002, where he served in a variety of operational roles and established E*TRADE's acquisition and investment strategies. While at E*TRADE, Mr. Bevilacqua founded ArrowPath Venture Partners, an early stage venture capital fund that was later spun out from E*TRADE, and served as the Managing Partner of that firm from 1999 to November 2007. Mr. Bevilacqua was previously a partner at two leading Silicon Valley law firms, Brobeck, Phleger & Harrison LLP and Orrick, Herrington & Sutcliffe LLP. Since April 2011, Mr. Bevilacqua has served on the board of directors of Gain Capital Holdings, Inc., a provider of online foreign exchange trading services. Mr. Bevilacqua received a J.D. from the University of California, Hastings College of the Law and a B.S. in business administration from the University of California at Berkeley. We believe that Mr. Bevilacqua possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as a member of our compensation committee and nominating and corporate governance committee, including his knowledge of technology investments and Internet services, his financial literacy and his general business and legal experience.

Bruce G. Bodaken has served as a member of our board of directors since September 2005, as chairman of our audit committee since May 2009 and as a member of our audit committee since February 2006. Mr. Bodaken has served as the Chairman, President and Chief Executive Officer of Blue Shield of California, California's second largest nonprofit health insurer, since 2000. Mr. Bodaken joined Blue Shield in 1994 as President and Chief Operating Officer. Prior to joining Blue Shield, Mr. Bodaken served as Senior Vice President and Associate Chief Operating Officer of FHP International Corporation. Mr. Bodaken also serves on numerous professional and civic boards. He is a member of the Institute of Medicine's Roundtable on Value & Science-Driven Healthcare and serves on the board of directors of the California Business Roundtable, and the University of California, Berkeley's Health Services Management Program. Mr. Bodaken received an M.S. in Philosophy from the University of Colorado and a B.A. in Philosophy from Colorado State University. We believe that Mr. Bodaken possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as chairman of our audit committee, including his extensive business experience as an executive in the health insurance industry.

Mariann Byerwalter has served as a member of our board of directors since May 2010 and as a member of our audit committee since May 2010. Ms. Byerwalter has been the chairman of JDN Corporate Advisory LLC, a privately-held advisory services firm, since October 2001. Ms. Byerwalter served as Chief Financial Officer and

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Vice President for Business Affairs of Stanford University from February 1996 through February 2001. Prior to joining Stanford University, she was a partner and co-founder of America First Financial Corporation from 1987 through January 1996. Ms. Byerwalter was also the Chief Operating Officer, Chief Financial Officer and a director of America First Eureka Holdings, the holding company for EurekaBank, a publicly-traded institution. She was the Chief Financial Officer of Eureka Bank from 1993 to 1996 and was a member of its board of directors from 1988 until the company was sold in 1998. Ms. Byerwalter served as a member of the board of directors of PMI Group, Inc., a provider of residential mortgage insurance, from May 2001 until March 2009. Ms. Byerwalter currently serves on the boards of certain investment companies affiliated with Charles Schwab Corporation, Redwood Trust, Inc., Pacific Life Corporation and Burlington Capital. She serves as a director and as chairman of the board of the Stanford Hospital & Clinics and a director of the Lucile Packard Children's Hospital. Ms. Byerwalter received an M.B.A. from Harvard University and a B.A. in Economics and Political Science/Public Policy from Stanford University. We believe Ms. Byerwalter possesses specific attributes that qualify her to serve a member of our board of directors and to serve as a member of our audit committee, including her experience as a company executive and her financial and accounting expertise with public companies.

Jerome D. Gramaglia has served as a member of our board of directors since November 2002, as a member of our compensation committee since October 2003 and as the chairman of our compensation committee since February 2006. Mr. Gramaglia is a private investor/advisor to consumer-oriented technology start-ups. From March 2011 to July 2011, Mr. Gramaglia served as interim Chief Executive Officer and President of Acxiom Corporation, a leading provider of marketing data, services and technology. From May 2002 to March 2008, Mr. Gramaglia served as Entrepreneur-in-Residence and then as Partner for ArrowPath Venture Partners. Previously, Mr. Gramaglia served as Chief Marketing Officer and then as President and Chief Operating Officer for E*TRADE Group, Inc., a leading provider of electronic financial services. Mr. Gramaglia began his career at Procter & Gamble and later held marketing and general management positions for Nestle, PepsiCo, Imasco and Sprint. Mr. Gramaglia has also served on the boards of directors of Coldwater Creek, a national retailer of women's apparel, since June 2004 and Acxiom since August 2009, where he currently serves as non-executive chairman of the board. Mr. Gramaglia received a B.A. in Economics from Denison University. We believe Mr. Gramaglia possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as the chairman of our compensation committee, including his experience in various executive roles of a public company, his service on the board of other public companies and his marketing, financial, technology and management expertise.

John W. Larson has served as a member of our board of directors since June 2000, as chairman of our board of directors since July 2006 and as chairman of our nominating and corporate governance committee since February 2006. Mr. Larson retired as a partner at the law firm of Morgan, Lewis & Bockius LLP in December 2009, which he joined in February 2003. Mr. Larson served as partner at the law firm of Brobeck, Phleger & Harrison LLP from 1969 until retiring in January 2003, except for the period from July 1971 to September 1973 when he was in government service as Assistant Secretary of the United States Department of the Interior and Counselor to George P. Shultz, Chairman of the Cost of Living Council. From 1988 until March 1996, Mr. Larson served as the Chief Executive Officer for Brobeck. Mr. Larson has served on the board of directors of Sangamo Biosciences, Inc., a biotechnology company focusing on zinc finger DNA-binding proteins, since January 1996. Mr. Larson also serves on the board of Needham Funds and MBA Polymers. Mr. Larson received an L.L.B. from Stanford Law School and a B.A., with distinction, in Economics from Stanford University. We believe Mr. Larson possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as the chairman of our nominating and corporate governance committee, including his extensive legal career and business background and his experience on the boards of numerous public and private companies.

Edward C. Nafus has served as a member of our board of directors since August 2010, as a member of our compensation committee since August 2010 and as a member of our audit committee since February 2012. From April 2005 until his retirement in December 2007, Mr. Nafus served as President and Chief Executive Officer of

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CSG Systems International, Inc., a leading provider of customer interaction management solutions to the North American market. Mr. Nafus joined CSG Systems in August 1998 as Executive Vice President and became President, Convergent Services and Solutions Division in January 2002. From 1992 to 1998, he served as Executive Vice President of First Data Resources, Chief Executive Officer of First Data Resources Limited and President of First Data International. From 1984 to 1992, he served as President of First Data Resources and Executive Vice President of First Data Corporation. From 1971 to 1978, Mr. Nafus worked in sales management, training and sales for Xerox Corporation. From 1966 to 1971, Mr. Nafus was a pilot and division officer in the United States Navy. Mr. Nafus serves on the board of directors of CSG Systems International, Inc. Mr. Nafus received a B.S. degree from Jamestown College. We believe Mr. Nafus possesses specific attributes that qualify him to serve as a member of our board of directors and to serve as a member of our compensation and audit committees, including his experience as an executive and board member of a public company and general business experience.

Code of Business Conduct and Ethics

Our board of directors has adopted a code of business conduct and ethics that applies to all of our employees, officers, and directors, including our chief executive officer, chief financial and accounting officer and other principal executive and senior financial officers.

Board of Directors and Risk Oversight

Our board of directors is currently composed of eight members, seven of whom have been determined to be independent within the meaning of the independent director guidelines of the NYSE. Our amended and restated certificate of incorporation and bylaws provide that the number of our directors shall be fixed from time-to-time by a resolution of the majority of our board of directors. Each officer serves at the discretion of the board of directors and holds office until his successor is duly elected and qualified or until his or her earlier resignation or removal. There are no family relationships among any of our directors or executive officers.

Our amended and restated certificate of incorporation and amended and restated bylaws provide for a classified board of directors consisting of three classes of directors, each serving staggered three-year terms, as follows:

the Class I directors are Richard M. Berkeley and Jerome D. Gramaglia, and their terms will expire at the annual meeting of stockholders to be held in 2013;

the Class II directors are Mariann Byerwalter, John W. Larson and Edward C. Nafus and their terms will expire at the annual meeting of stockholders to be held in 2014; and

the Class III directors are Thomas A. Bevilacqua, Bruce G. Bodaken and Joseph L. Jackson, and their terms will expire at the annual meeting of stockholders to be held in 2015.

Our board of directors is responsible for, among other things, overseeing the conduct of our business, reviewing and, where appropriate, approving our long-term strategic, financial and organizational goals and plans, and reviewing the performance of our chief executive officer and other members of senior management. Our board of directors intends to conduct an annual self-evaluation at the end of each fiscal year, which will include a review of any areas in which the board of directors or management believes the board of directors can make a better contribution to our corporate governance, as well as a review of the committee structure and an assessment of the board of directors' compliance with corporate governance principles. In fulfilling the board of directors' responsibilities, directors will have full access to our management and independent advisors.

Our board of directors, as a whole and through its committees, has responsibility for the oversight of risk management. Our senior management is responsible for assessing and managing our risks on a day-to-day basis. Our audit committee will discuss with management our policies with respect to risk assessment and risk management and our significant financial risk exposures and the actions management has taken to limit, monitor

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or control such exposures. Our compensation committee will oversee risk related to compensation policies. Both our audit and compensation committees will report to the full board of directors with respect to these matters, among others.

As part of its oversight of our compensation programs, our compensation committee has considered our executive officer and non-executive employee compensation programs as they relate to our risk management and based upon this assessment, we believe that any risks arising from such policies and practices are not reasonably likely to have a material adverse effect on us. Our employees' base salaries are fixed in amount and do not depend on performance. Our cash incentive program takes into account multiple metrics, thus diversifying the risk associated with any single performance metric, and we believe it does not incentivize our employees to focus exclusively on short-term outcomes. Our equity awards are limited by the terms of our equity plans to a fixed maximum specified in the plan, and are subject to vesting to align the long-term interests of our employees with those of our stockholders. We do not believe that these equity-based incentives encourage unnecessary or excessive risk taking because their ultimate value is tied to our stock price.

Director Independence

Our common stock is listed on the NYSE. Under NYSE rules, independent directors must comprise a majority of a listed company's board of directors within a specified period of time following the completion of a listed company's initial public offering. In addition, NYSE rules require that, subject to specified exceptions, each member of a listed company's audit, compensation and nominating and corporate governance committees be independent. Audit committee members must also satisfy the independence criteria set forth in Rule 10A-3 under the Securities Exchange Act of 1934, as amended. Under NYSE rules, a director will only qualify as an independent director if, in the opinion of that company's board of directors, that person does not have a relationship that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.

In order to be considered independent for purposes of Rule 10A-3, a member of an audit committee of a listed company may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee: (1) accept, directly or indirectly, any consulting, advisory, or other compensatory fee from the listed company or any of its subsidiaries; or (2) be an affiliated person of the listed company or any of its subsidiaries.

Our board of directors has undertaken a review of its composition, the composition of its committees and the independence of each director. Based upon information requested from and provided by each director concerning his or her background, employment and affiliations, including family relationships, our board of directors has determined that none of Ms. Byerwalter and Messrs. Berkeley, Bevilacqua, Bodaken, Gramaglia, Larson, and Nafus, representing seven of our eight directors, has a relationship that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director and that each of these directors is independent as that term is defined under NYSE rules. Our board of directors also determined that Ms. Byerwalter and Messrs. Bodaken and Nafus, who comprise our audit committee, Messrs. Bevilacqua, Gramaglia and Nafus, who comprise our compensation committee, and Messrs. Berkeley, Bevilacqua and Larson, who comprise our nominating and corporate governance committee, satisfy the independence standards for those committees established by applicable SEC rules and NYSE rules. In making this determination, our board of directors considered the relationships that each non-employee director has with our company and all other facts and circumstances our board of directors deemed relevant in determining their independence, including the beneficial ownership of our capital stock by each non-employee director.

Committees of the Board of Directors

Our board of directors has established an audit committee, a compensation committee and a nominating and corporate governance committee, each of which has the composition and responsibilities described below. The audit committee, compensation committee and nominating and corporate governance committee all operate under charters approved by our board of directors, which charters are available on our website.

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Audit Committee. Our audit committee is comprised of Ms. Byerwalter and Messrs. Bodaken and Nafus, each of whom is a non-employee member of our board of directors. Mr. Bodaken is the chairman of our audit committee and our audit committee financial expert, as that term is defined under the SEC rules implementing Section 407 of the Sarbanes-Oxley Act of 2002, and possesses financial sophistication as defined in the rules of the NYSE. Our audit committee is responsible for, among other things:

reviewing and approving the selection of our independent registered public accounting firm, and approving the audit and non-audit services to be performed by our independent registered public accounting firm;

monitoring the integrity of our financial statements and our compliance with legal and regulatory requirements as they relate to financial statements or accounting matters;

reviewing the adequacy and effectiveness of our internal control policies and procedures;

discussing the scope and results of the audit with the independent auditors and reviewing with management and the independent auditors our interim and year-end operating results; and

preparing the audit committee report that the SEC requires in our annual proxy statement.

Compensation Committee. Our compensation committee is comprised of Messrs. Bevilacqua, Gramaglia and Nafus. Mr. Gramaglia is the chairman of our compensation committee. The compensation committee is responsible for, among other things:

overseeing our compensation policies, plans and benefit programs;

reviewing and approving for our executive officers: the annual base salary, the annual incentive bonus, including the specific goals and amount, equity compensation, employment agreements, severance arrangements and change in control arrangements, and any other benefits, compensations or arrangements;

preparing the compensation committee report that the SEC requires to be included in our annual proxy statement; and

administering our equity compensation plans.

Nominating and Corporate Governance Committee. Our nominating and corporate governance committee is comprised of Messrs. Berkeley, Bevilacqua and Larson. Mr. Larson is the chairman of our nominating and corporate governance committee. The nominating and corporate governance committee is responsible for, among other things:

assisting our board of directors in identifying prospective director nominees and recommending nominees for each annual meeting of stockholders to the board of directors;

evaluating director compensation, consulting with outside consultants and/or with our human resources department when appropriate, and making recommendations to our board of directors regarding director compensation;

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reviewing developments in corporate governance practices and developing and recommending governance principles applicable to our board of directors;

reviewing the succession planning for our executive officers;

overseeing the evaluation of our board of directors and management; and

recommending members for each board committee to our board of directors.

Compensation Committee Interlocks and Insider Participation

No interlocking relationship exists between our board of directors or compensation committee and the board of directors or compensation committee of any other entity, nor has any interlocking relationship existed in the past.

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Table of Contents**Director Compensation**

The following table sets forth information concerning compensation paid or accrued for services rendered to us by members of our board of directors for the fiscal year ended December 31, 2011. The table excludes Mr. Jackson, who is a named executive officer, and did not receive any compensation from us in his role as a director in the fiscal year ended December 31, 2011.

	Fees Earned or Paid in Cash(1)	Total
	\$	\$
Richard M. Berkeley		
Thomas A. Bevilacqua		
Bruce G. Bodaken	42,000	42,000
Mariann Byerwalter	28,500	28,500
Jerome D. Gramaglia	35,000	35,000
John W. Larson	47,000	47,000
Leigh E. Michl(2)		
Edward C. Nafus	26,000	26,000

(1) See *Standard Compensation Arrangements for Non-Employee Directors* below for a description of how cash fees are paid to non-employee directors. Prior to the completion of our initial public offering, we did not pay any cash fees to directors affiliated with our major venture capital stockholders.

(2) Mr. Michl resigned from our board, effective January 31, 2012.

The aggregate number of shares subject to stock options outstanding at December 31, 2011 for each non-employee director is as follows:

Name	Aggregate Number of Stock Options Outstanding as of December 31, 2011(1)
Richard M. Berkeley	24,500
Thomas A. Bevilacqua	6,500
Bruce G. Bodaken	30,500
Mariann Byerwalter	25,000
Jerome D. Gramaglia	30,500
John W. Larson	50,250
Leigh E. Michl(2)	24,500
Edward C. Nafus	25,000

(1) Does not include options for 97,500 shares granted in February 2012.

(2) Mr. Michl resigned from our board, effective January 31, 2012.

Standard Compensation Arrangements for Non-Employee Directors

Pursuant to our non-employee director compensation program, our non-executive chairman of the board receives an annual retainer of \$40,000 and each of our remaining non-employee directors receives an annual retainer of \$20,000, payable quarterly. If a non-employee director serves for only a portion of a year, such non-employee director's retainer is pro-rated for that portion of the year. The chair of our audit committee receives an additional annual retainer of \$10,000, the chair of our compensation committee receives an additional annual retainer of \$6,500 and the chair of our nominating and corporate governance committee receives an additional annual retainer of \$4,000. Our chairman of the board will not be paid an additional committee chair retainer if he or she also serves as a committee chair. Our non-employee director compensation program allows a non-employee director to elect to be paid their annual retainers in options to purchase that number of shares of our common stock equal to 2.5 times the retainer amount divided by the then-current fair market value of a share of our common stock.

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Our non-employee directors are also paid \$1,000 for every meeting of the board of directors or committee attended in person, and \$500 for every meeting of the board of directors or committee attended telephonically. Prior to our initial public offering, directors affiliated with our major venture capital stockholders, Messrs. Berkeley, Bevilacqua and Michl, did not receive retainer payments or payments for attending board or committee meetings.

Under the non-employee director compensation program, each non-employee director is automatically granted a stock option to purchase 25,000 shares of our common stock on the date such person first becomes a non-employee director, under the equity incentive plan in place at that time. Additionally, annually, each non-employee director is automatically granted a stock option to purchase 10,000 shares of our common stock under the equity incentive plan in place at that time. The grant of these annual retainer stock awards will be made as of the annual meetings of stockholders. Prior to our initial public offering, our non-executive chairman of the board was granted a stock option to purchase 10,000 shares of our common stock and prior to Ms. Byerwalter's appointment to the board of directors in May 2010, each non-employee director was granted a stock option to purchase 13,000 shares of our common stock on the date such person first became a non-employee director, under the equity incentive plan in place at that time. Commencing with Ms. Byerwalter's appointment to the board of directors in May 2010, we increased the number of shares subject to the stock option granted to each non-employee director upon joining the board of directors to 25,000 shares in anticipation of a potential initial public offering and the increased demands related to directors' responsibilities in connection therewith. Prior to our initial public offering, annually, our non-executive chairman of the board was automatically granted a stock option to purchase 9,750 shares of our common stock and each of our other non-employee directors was granted a stock option to purchase 6,500 shares of our common stock.

In November 2010, we granted each of Messrs. Bodaken and Gramaglia a one-time additional stock option to purchase 11,000 shares of our common stock. These grants were made partially in recognition of the dilution caused by the conversion of convertible promissory notes we issued and sold in December 2009.

On February 9, 2012, each of our non-employee directors was granted options to purchase our common stock at an exercise price of \$9.59 per share. These grants represent the annual awards to be made to our non-employee directors for both 2011 and 2012 under our director compensation program in effect prior to our initial public offering. These options are subject to the vesting terms described below. Mr. Larson, our non-executive chairman, received options to purchase 19,500 shares and Messrs. Berkeley, Bevilacqua, Bodaken, Gramaglia and Nafus and Ms. Byerwalter each received options to purchase 13,000 shares.

The exercise price of all stock options granted pursuant to the non-employee director program is equal to the fair market value of our common stock on the date of grant. The term of all stock options will be 10 years. Subject to the adjustment provisions of our equity incentive plans, the initial stock option awards vest monthly over two years, provided the non-employee director continues to serve as a director through each vesting date. Subject to the adjustment provisions of our equity incentive plans, the annual awards vest monthly over one year, provided the non-employee director continues to serve as a director through each vesting date.

Each vested stock option granted under the non-employee director compensation program is exercisable by the grantee for three years following separation from the board of directors.

In the event of a change in control, as defined in the appropriate equity incentive plan, with respect to awards granted under the non-employee director compensation program, the participant non-employee director will fully vest in and have the right to exercise awards as to all shares underlying such awards.

Table of Contents**EXECUTIVE COMPENSATION****Compensation Discussion and Analysis**

This Compensation Discussion and Analysis provides information about the material components of our compensation program for our named executive officers, or NEOs. Our NEOs for 2011 were Joseph L. Jackson, Chief Executive Officer, who we refer as our CEO; Richard T. Green, Chief Financial Officer, who we refer to as our CFO; Edgar O. Montes, Senior Vice President, Service Delivery Operations and Kimberly L. Jackson, Senior Vice President, General Counsel and Secretary, who we refer to as our GC. More information on the compensation for our NEOs appears in the Summary Compensation Table that follows this section.

2011 Highlights

We believe that the leadership of our executives is critical to the success of our business and that establishing appropriate compensation and incentives helps us to attract, retain and motivate highly skilled executives. In order to provide an executive compensation program that emphasizes pay for performance, we subject a substantial portion of our executives' compensation to the achievement of performance-based goals.

In 2011, through a combination of client portfolio purchases and organic growth, we grew our revenue from \$115.0 million in 2010 to \$135.6 million in 2011, despite global adverse economic conditions. We increased healthcare revenues by 20% and commuter revenues by 14% from 2010 to 2011. Further, our employee participants, employer clients and debit card transaction volume all increased from 2010 to 2011. Our Adjusted EBITDA grew from \$22.4 million in 2010 to \$30.3 million in 2011, an increase of 36%. In line with our executive compensation program's emphasis on pay-for-performance, compensation to our executives reflected our financial results.

As a result of our strong performance in 2011, we paid out NEO bonuses under our annual bonus plan at 130% of the targeted amounts.

Overview, Philosophy and Objectives

Our compensation philosophy is to provide programs that attract, retain and motivate key employees who are critical to our long-term success. We strive to provide our NEOs with compensation packages that are competitive, but that also pay for performance, by rewarding achievement of our business goals and aligning our NEOs' interests with those of our stockholders.

The following table identifies the main elements of our 2011 NEO compensation program and the reason we chose to provide each:

Element of Compensation	Basis for Providing Element
Base Salary	To reward NEOs for day-to-day efforts based on demonstrated experience, competencies and performance
Short-term Incentives (also referred to as cash bonuses)	To motivate and reward achievement of our annual strategic goals and to better align the NEOs' interest with those of our stockholders by promoting strong, annual financial and business results
Long-term Incentives	To align the NEOs' interests with the long-term interests of our stockholders and to promote the retention of our NEOs through multi-year vesting schedules
Employee Benefits	To provide for the safety and wellness of our NEOs through benefits that are competitive
Change in Control and Severance Benefits	To promote the retention of our NEOs

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Compensation-Setting Process

Role of the Board and Compensation Committee

Our board of directors, or the Board, established the compensation committee, or the Committee, of the Board to carry out the Board's responsibilities to administer our compensation programs (as described further in the section titled *Compensation Committee* under *Management Committees of the Board of Directors* above). The Committee has the final decision-making authority for the compensation of our NEOs, except for our CEO whose compensation is recommended by the Committee and approved by the Board. The Committee operates under a written charter adopted by the Committee and approved by the Board. The charter is available on our website. Each committee member qualifies as (i) an independent director under NYSE requirements, (ii) a non-employee director under Rule 16b-3 of the Exchange Act of 1934, as amended, and (iii) an outside director under Section 162(m) of the Internal Revenue Code of 1986, as amended, or the Code.

Our Committee has independent authority to engage outside consultants and obtain input from external advisers as well as our management team or other employees.

Role of Compensation Consultant

In late 2010, our Senior Vice President of Human Resources, at the direction of the Committee, engaged Compensia, a third party executive compensation consultant, to assist us with respect to 2011 compensation of our executives, including our NEOs. Compensia updated its competitive market assessment for both pre-initial public offering and public companies in February 2011 and this data was considered by the Committee in setting executive compensation in 2011. This process involved Compensia analyzing, reviewing and making recommendations to the Committee regarding (i) our peer group companies and (ii) various elements of our executive pay program as compared to privately held and publicly traded peer group companies, including base salary, cash bonuses, and long term incentives, as well as total equity ownership, and change in control and severance arrangements. From time-to-time, our management also discussed their questions with Compensia regarding the projects and presentations that Compensia provided to the Committee. In 2011, Compensia did not provide any services to us, or receive any payments from us, other than in their capacity as a consultant to the Committee.

Role of Management

Our CEO typically attends Committee meetings, except for executive sessions (unless specifically requested by the Committee to be present). No NEO attends an executive session at which his or her compensation is considered. Our CEO, with the assistance of the CFO and GC, as appropriate, may provide recommendations with respect to compensation for the NEOs other than himself. The Committee considers these recommendations, but may approve, reject or adjust them as the Committee deems appropriate.

Peer Companies

Peer Private Companies

For 2011, with the assistance of Compensia, the Committee considered various data in order to conduct a comparative analysis of our NEOs compensation against our peer companies. In particular, the Committee looked to the Advanced HR Option Impact Pre-IPO Compensation Database that covers privately held high technology companies, each with revenues and privately raised capital over \$100 million, which we refer to as the Peer Private Companies. Compensia recommended, and the Committee agreed, that the Peer Private Companies data offered a more relevant comparative framework than a set of public companies, due to our stage of development and status as a private company at the time. Due to the fact that privately held companies participate on a confidential basis in the surveys that yield the database results, we have no visibility into the companies that participated in the survey and, instead, only visibility as to the aggregated data provided by employee position.

Table of Contents*Peer Public Companies*

The Committee also considered data from certain publicly traded companies in order to conduct a comprehensive review of our executive compensation practices and to enable any appropriate planning needed for a potential initial public offering in the upcoming year. This additional data consisted of both publicly traded high technology companies in the Radford Executive Survey with revenues in the \$50 million to \$200 million range, which we refer to as the Radford Companies, and a separate set of 17 publicly traded companies based on publicly available data compiled by Compensia, which we refer to as the Peer Group Companies, and together with the Radford Companies, the Peer Public Companies, that the Committee approved based on various factors including company revenue (approximately \$50 million to \$360 million) and the industry in which the companies operate (companies chosen are in the human resources and outsourced services and human resources software industries) as follows:

Peer Group Companies

Athenahealth, Inc.	HMS Holdings Corp.	SuccessFactors, Inc.
Callidus Software, Inc.	Innodata Isogen, Inc.	Taleo Corporation
Concur Technologies, Inc.	Kenexa Corporation	Tier Technologies, Inc.
Constant Contact, Inc.	Online Resources Corporation	The Ultimate Software Group, Inc.
Dice Holdings, Inc.	S1 Corporation	Wright Express Corporation
ExlService Holdings, Inc.	Saba Software, Inc.	

We did not review the companies that comprised the set of Radford Companies, but instead obtained only aggregated data according to the relevant employee position. The Committee believed that this set of data was appropriate because the companies were similar in size and operated within the same or similar industries as us. With respect to our CEO, CFO and GC, the Peer Public Companies data for base salary and short-term incentive was a blend of the Radford Companies and Peer Group Companies, and Peer Public Companies data for equity compensation was limited to the Peer Group Companies. For Mr. Montes position as our Senior Vice President, Service Delivery Operations, the peer market data with respect to base salary and short-term incentives was based on the Radford Companies due to the limited data available in the Peer Group Companies. However, all of the equity compensation market analysis for our NEOs was based on the Peer Group Companies.

Use of Peer Data

Within these peer companies, we generally target the 50th percentile for each element of compensation. We believe that this benchmark level provides a competitive compensation package that has sufficient retention and incentive value for our executives. In setting the various elements of compensation for the NEOs, rather than reviewing each element of compensation in isolation, we also take into account total cash compensation (i.e., base salary plus short-term incentives) and total direct compensation (i.e., total cash compensation plus equity incentives), both of which are also targeted at the 50th percentile. We believe that considering these measures is important because it allows us to provide compensation that, as a complete package, is appropriate for each individual.

The data described above was used principally for purposes of validation and as guidelines, with the expectation that adjustments to compensation that vary from the target will be made incrementally over time (rather than implementing any dramatic changes immediately). Moreover, other factors, such as performance, contributions, motivation, retention, and importance of the role, ultimately may drive the decision and result in compensation that differs from the targeted percentile. However, over time, we intend NEO compensation with respect to the targeted elements to be at approximately the 50th percentile of our peer group.

Table of Contents*Elements of Compensation**Total Cash Compensation*

As described above, in early 2011, we reviewed our NEOs' targeted total cash compensation, which compared to our Peer Private Companies as follows:

Name	Base Salary at 2010 Year End (\$)	2010 Target Bonus Amount (\$)	2010 Targeted Total Cash Compensation (\$)	2010 Targeted Total Cash Compensation Compared to Peer Private Companies
Joseph L. Jackson	400,000	200,000	600,000	At Approximately the 50 th Percentile
Richard T. Green	281,875	112,750	394,625	At Approximately the 75 th Percentile
Edgar O. Montes	218,400	87,360	305,760	Above the 75 th Percentile
Kimberly L. Jackson	198,550	79,420	277,970	At Approximately the 50 th Percentile

The Committee believed that our NEOs' total cash compensation percentile rankings reflected the fact that many of our employees came from larger companies at which they otherwise would have earned higher base salaries and bonuses than a company more similar in size to us. In the past, this necessitated offering a sufficiently high level of cash compensation in order to attract the executive to join us. However, as compared to the Peer Public Companies, the total cash compensation of Mr. Jackson was below the 25th percentile, Mr. Green was at approximately the 25th percentile, Mr. Montes was at approximately the 75th percentile and Ms. Jackson was below the 25th percentile. Because the available peer market data for Mr. Montes' position as Senior Vice President, Service Delivery Operations was not comprehensive, the Committee believed that the peer group analysis with respect to his compensation did not take into account some of his larger responsibilities with respect to our operations. As a result, the Committee generally also took into consideration these larger responsibilities in reviewing and setting Mr. Montes' compensation for 2011.

Base Salary

We typically review and consider adjustments to base salaries on an annual basis, following the Committee's review (or the Board's review, with respect to our CEO) of the executive's performance for the most recently ended fiscal year. Base salaries generally are set at levels intended to recognize the NEOs' experience, competencies and responsibilities and, over time, are intended to reflect the NEOs' overall sustained performance and contributions to our company. We expected to become a public company in 2011, so no base increases were implemented for any NEOs during 2011, as we believed that base salary adjustments, if any, should take place after we become a public company.

Short-Term Incentives (Cash Bonuses)

We adopted a 2011 Bonus Plan, or the Bonus Plan, in order to reward the performance of our NEOs, in achieving our financial and strategic objectives for the year. Bonuses are discretionary and the Committee and Board may determine bonuses based on achievement of performance goals and other factors they deem relevant. The Committee and Board may determine to award a bonus at a level higher than the bonus amount that otherwise would become payable based on actual achievement of performance goals; the Committee and Board also have discretion to reduce bonus amounts or to determine not to award any bonus.

Table of Contents*Target Bonuses*

Each year we typically establish a target bonus for our NEOs expressed as a percentage of base salary. Prior to setting bonuses for 2011, the Committee reviewed the market analysis with respect to bonuses for our NEOs. The following table shows the 2011 target bonus that was approved for each NEO:

Name	2011 Target Bonus as a Percentage of Base Salary (%)	2011 Target Bonus Compared to Peer Private Companies	2011 Target Bonus Compared to Peer Public Companies
Joseph L. Jackson	50	At Approximately the 25 th Percentile	Below the 25 th Percentile
Richard T. Green	40	At Approximately the 50 th Percentile	Below the 25 th Percentile
Edgar O. Montes	40	Above the 75 th Percentile	At Approximately the 50 th Percentile
Kimberly L. Jackson	40	Above the 75 th Percentile	Between the 25 th and 50 th Percentile

Performance Goals

For 2011, the performance goals under the Bonus Plan were based on the achievement of our annual adjusted earnings before interest, tax, depreciation and amortization, or Adjusted 2011 EBITDA, an overall company objective and individual goals. These goals were weighted as follows:

Performance Goal	Weighting
Adjusted 2011 EBITDA	45%
Overall Company Objective	40
Individual Goals	15

We believe that this mix of corporate and individual goals for 2011 was appropriate because the former incentivized our executives to work as a team to achieve important financial, business and strategic goals, while the latter focused each NEO's attention on the critical objectives specific to his or her role and responsibilities within our company.

Adjusted 2011 EBITDA. For purposes of the Bonus Plan, Adjusted 2011 EBITDA means our 2011 EBITDA as adjusted by: (1) adding back compensation costs for 2011 for share-based payments that otherwise would be amortized for financial reporting purposes; (2) excluding the financial results of any businesses acquired by us during 2011 (unless such business also was included in the budgeted Adjusted 2011 EBITDA target as approved by the Board); and (3) including the effect of bonuses paid to our employees (including our NEOs) for 2011. The following table describes the levels of Adjusted 2011 EBITDA performance required for 2011 for our NEOs, as well as the multiplier that would be applied to the portion of the eligible bonus (45% of the bonus) upon achievement of this performance goal:

Achievement of	Multiplier Allocated to Adjusted 2011 EBITDA Performance Goal
Adjusted 2011 EBITDA(1) Greater than \$29,500,000	A multiplier of 150% is allocated to achievement of the performance goal
At least \$26,500,000 but not greater than \$29,500,000	A multiplier between 90% and 150% is allocated to achievement of the performance goal, prorated based on the level of achievement within such Adjusted 2011 EBITDA range
Less than \$26,500,000	No amount becomes payable with respect to the Adjusted 2011 EBITDA performance goal

(1)

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The target goal (which at 100% achievement yields a multiplier of 100%) is based on achievement of Adjusted 2011 EBITDA at \$27.0 million.

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Overall Company Objective. The 2011 overall company objective selected by the Committee for the 2011 Bonus Plan was to achieve actual adjusted organic revenue growth of at least 4.5%. Actual adjusted organic revenue is defined as total revenue less run-out and grace period fees less any revenue from any portfolio purchases during 2011 and adding back any client credits or other extensions.

The following table describes the levels of actual adjusted organic revenue growth performance required for 2011 for our NEOs, as well as the multiplier that would be applied to the portion of the eligible bonus (40% of the bonus) upon achievement of this performance goal:

Achievement of 2011 Actual	
Adjusted Organic	
Revenue Growth Company	
Objective(1)(2)	Multiplier Allocated to Company Objective Performance Goal
Greater than 6.25%	A multiplier of 125% is allocated to achievement of the performance goal
Between 4.5% and 6.25%	A multiplier between 90% and 125% is allocated to achievement of the performance goal prorated based on the level of achievement within such organic revenue growth range
Below 4.5%	No amount becomes payable with respect to the 2011 company objective

- (1) The target goal (which at 100% achievement yields a multiplier of 100%) is based on achievement of actual adjusted organic revenue growth of 5%.
- (2) If Adjusted EBITDA is less than \$26.5 million, no amount becomes payable with respect to the 2011 company objective.

Individual Goals. In addition to the corporate goals, the bonuses for our NEOs depended on achievement of individual goals that were specific to his or her roles and responsibilities. The following table summarizes the individual goals for each NEO for 2011:

Name	Individual Performance Goals
Joseph L. Jackson	Rated on his overall performance using the following factors: (1) complete a successful Initial Public Offering, (2) complete at least one portfolio purchase by 11/1/2011 and (3) use key learnings to improve the 2012 open enrollment process to include focus on reenrollments and new participants.
Richard T. Green	Rated on his overall performance using the following factors: (1) complete a successful Initial Public Offering, (2) develop and integrate the internal audit function into the Company, (3) complete the SOX implementation, (4) support acquisitions and (5) establish working relationships with each of the five research analysts of the bankers selected to be a part of the initial public offering syndicate.
Edgar O. Montes	Rated on his overall performance using the following factors: (1) meet service levels for all key operational areas for 12 months or 4 quarters, (2) improve transactional participant satisfaction, (3) improve new implementation satisfaction and (4) achieve full year budget target.
Kimberly L. Jackson	Rated on her overall performance using the following factors: (1) prepare for Initial Public Offering, (2) assist with portfolio purchases, (3) lead training for other functional groups and (4) improve contract process.

Each individual performance goal for the NEOs other than our CEO is assigned a score on a scale of one through five, with a score of one equating to unsatisfactory and a score of five equating to exceptional performance. The scores for each NEO then are averaged to arrive at a single score for each NEO (other than for our CEO). If the final average score of all of the NEO's individual performance goals resulted in a score of three or higher, the individual performance goals for him or her would be deemed achieved in full. However, even if these goals were 100% achieved, no bonuses with respect to the individual performance goals would be payable unless a minimum Adjusted 2011 EBITDA of \$26.5 million was achieved for 2011. Our CEO's performance was

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reviewed by the Committee and Board and achievement levels were subject to the Board's approval. All other NEOs' performances were reviewed and recommended by our CEO, subject to the Committee's review and approval.

2011 Results

Following the 2011 performance period, the Committee assessed our performance against the criteria under the Bonus Plan and determined that for 2011, we achieved an Adjusted 2011 EBITDA of \$30.3 million (resulting in a multiplier of 150% for the Adjusted 2011 EBITDA performance goal) and the actual adjusted organic revenue growth was greater than 6.25% (resulting in a multiplier of 125% for the company objective performance).

Also following the 2011 performance period, Mr. Jackson assessed the performance of our other NEOs versus their respective individual performance goals, and the Committee assessed Mr. Jackson's performance against his individual performance goals. Mr. Jackson determined that Mr. Green had achieved a weighted average score of 4.2, based on Mr. Green having achieved each of his goals (that is, a score of not less than 3). This included the goal related to an initial public offering as each of the sub-elements of that goal (including, among others, support for, and participation in, analyst and investor presentations, and preparation and filing of the registration statement for the initial public offering) had been completed (although the Company had decided not to proceed with the offering in 2011). With respect to Mr. Montes, Mr. Jackson determined that Mr. Montes had achieved an overall score of 4.7 and had achieved each of his goals, with exceptional performance against several goals (including, but not limited to, meeting and exceeding service levels and budget targets). With respect to Ms. Jackson, Mr. Jackson determined that Ms. Jackson had achieved an overall score of 4.6 based on having achieved each of her goals (especially, among others, preparation and filing of the registration statement for the initial public offering, directing and completing the legal aspects of portfolio purchases and leading training for other functional groups within the Company). Taking these scores into account, Mr. Jackson recommended to the Committee that an overall bonus payable at 130% of target be approved for each of our NEOs (other than Mr. Jackson). The Committee elected to follow this recommendation. Mr. Jackson's performance against his individual performance goals was assessed by the Board. The Board assessed Mr. Jackson's performance versus the goals on an aggregate basis and did not assign an individual numerical score to each goal element. The Board determined that on an overall basis, Mr. Jackson's individual performance goals had been achieved in full. In reaching this conclusion, the Board considered that the Company had completed the necessary steps to launch an initial public offering but had decided not to proceed with the offering in 2011 and the Board further considered that Mr. Jackson had led the Company to a year of strong financial performance in 2011. Based on the Board's overall assessment of Mr. Jackson's performance, the Board awarded him a bonus payable at 130% of target.

The following table sets forth the 2011 bonuses paid to our NEOs:

Name	Target Bonus as a Percentage of Base Salary	Actual Bonuses	Actual Bonuses as a Percentage of Base Salary
Joseph L. Jackson	50%	\$ 260,000	65%
Richard T. Green	40	146,575	52
Edgar O. Montes	40	113,568	52
Kimberly L. Jackson	40	103,246	52
<i>Long-Term Incentives (Equity Awards)</i>			

We believe that strong, long-term corporate performance is achieved with a corporate culture that encourages a long-term focus by our NEOs through the use of equity awards, the value of which depends on our stock performance. We have established equity incentive plans to provide certain of our employees, including

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our NEOs, with incentives to help align those employees' interests with the interests of our stockholders and to enable them to participate in the long-term appreciation of our stockholder value. Additionally, to the extent equity awards are granted, these provide an important retention tool for key employees, as the awards generally are subject to vesting over an extended period of time subject to continued service with us. We expected to become a public company in 2011, so no equity awards were granted for any NEOs during 2011.

On February 9, 2012, our compensation committee granted each of our NEOs options to purchase our common stock at an exercise price of \$9.59 per share. These options are subject to the vesting terms described in footnote 2 of Outstanding Equity Awards at Fiscal Year-End below. Mr. Jackson received options to purchase 150,000 shares and Mr. Green, Ms. Jackson and Mr. Montes each received options to purchase 40,000 shares.

In early 2011, with the assistance of Compensia, the Committee reviewed total direct compensation and the percent equity ownership of our NEOs based on their outstanding equity awards and shares held (excluding shares acquired as an investment) and determined that as compared to the Peer Private Companies and the Peer Public Companies, their equity holdings were as follows:

Name	Percentile Equity Ownership Compared to Peer Private Companies	Percentile Equity Ownership Compared to Peer Public Companies
Joseph L. Jackson	Between the 50 th and 75 th Percentiles	Between the 50 th and 75 th Percentiles
Richard T. Green	Between the 50 th and 75 th Percentiles	Between the 50 th and 75 th Percentiles
Edgar O. Montes	At Approximately the 75 th Percentiles	N/A
Kimberly L. Jackson	N/A	Below the 25 th Percentile

Consistent with our compensation philosophy, these awards are intended to increase the alignment of our NEOs' interests with the long-term interests of our stockholders. We believe that any performance-based grants that ultimately vest demonstrate our commitment to our compensation philosophy of paying for performance.

Equity Award Grant Practices

Equity awards are granted to our NEOs and other employees under our 2010 Equity Incentive Plan. The grant date of all equity awards is the date on which the Committee approves the award (or the Board with respect to our CEO). The Committee has not delegated authority to grant equity awards under the 2010 Equity Incentive Plan. The Committee does not intend to establish any program, plan or practice of timing the grant of equity awards in coordination with the release of material non-public information that is likely to result in any increase or decrease in the value of our common stock.

Stock Ownership Guidelines

At this time, we have not adopted stock ownership guidelines with respect to the NEOs or other employees, although we may consider doing so in the future. We have established an insider trading policy that prohibits, among other things, short sales, hedging of stock ownership positions, and transactions involving derivative securities relating to our common stock.

Employee Benefits

Our NEOs are eligible to participate in the same group insurance and employee benefit plans as our other full-time, U.S. employees. We provide employee benefits to all eligible employees, including our NEOs, which we believe are reasonable and consistent with our overall compensation objective to better enable us to attract and retain employees. These include benefits such as medical, dental, and vision care, disability benefits and life insurance. We also sponsor a 401(k) tax-qualified retirement savings plan pursuant to which employees, including our NEOs, are entitled to participate. Employees can make contributions to the plan on a pre-tax basis up to 85% of their eligible compensation, subject to the maximum amount prescribed by the Internal Revenue

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Service. Under the 401(k) plan, we provide discretionary matching contributions at 25% of the first 4% of the employee contribution, up to a maximum of 1% of the employee's eligible compensation. Other than this plan, we do not maintain any other deferred savings plans in which the NEOs participate. We do not maintain or provide any defined benefit plans for our employees.

Change in Control and Severance Benefits

In hiring our executive officers, we recognized that it would be necessary to recruit qualified candidates that have the requisite experience, talent and skills to fill critical positions. In recruiting these executives, we offered compensation packages that we believe were competitive and sufficiently compelling in order for them to forego other opportunities and/or leave their prior employment. We have entered into agreements with each of our NEOs and certain other executives, either in connection with their hire or for internal equity considerations, which provide for certain severance benefits in the event of a qualifying termination. We believe that these agreements will help our NEOs and other executives to maintain their focus and dedication to their responsibilities to help maximize stockholder value by minimizing distractions due to the possibility of an involuntary termination or termination in connection with a potential change in control of us. We also believe that these arrangements further our interest in encouraging retention among our key employees.

The benefits include continued payment of base salary and health coverage for six months (or 12 months for Mr. Jackson) and a tax gross-up, if any, with respect to health coverage, upon an Involuntary Termination (as defined in the applicable agreement). Mr. Jackson additionally would be eligible to receive all or a portion of his bonus in effect for the year that the termination occurs subject to the Board's sole discretion, and he will be entitled to receive accelerated vesting of certain options as if he remained employed through the date 24 months following his termination, upon an Involuntary Termination within 24 months following a Change in Control (as defined in the applicable agreement) or during the time between signing a definitive agreement for a Change in Control and either (x) the closing of such Change in Control or (y) the termination of such agreement without completion of the proposed Change in Control. The other NEOs additionally would be entitled to receive his or her prorated bonus and acceleration of options as if he or she had remained employed through the date 18 months following such termination, upon an Involuntary Termination within 12 months following a Change in Control or during the time between signing a definitive agreement for a Change in Control and either (x) the closing of such Change in Control or (y) the termination of such agreement without completion of the proposed Change in Control. The severance benefits are subject to the NEO executing a release of claims in favor of us and complying with certain covenants (described further below).

An Involuntary Termination generally refers to a termination without cause or the NEO's resignation within 90 days following a material reduction in base salary or job duties, a material relocation of principal place of employment, or our material breach of our obligations under the applicable agreement. Change in Control generally refers to a change in ownership of us, change in the effective control of us, or change in ownership of a substantial portion of our assets, in each case which also qualifies as a change in control event under Section 409A of the Code.

Our 2011 Bonus Plan provided for bonuses to become payable to the NEO (or his or her estate, as applicable) in the event of death or disability, in an amount equal to the bonus that otherwise would have been paid if he or she remained employed with us through the date that the bonus is paid.

These various agreements are described in more detail in *Employment Agreement and Executive Severance Benefit Agreements* and *Potential Payments Upon Termination or Change in Control* below.

Tax and Accounting Considerations

Deductibility of Executive Compensation

Generally, Section 162(m) of the Code disallows a tax deduction to any publicly held corporation for any remuneration in excess of \$1.0 million paid in any taxable year to its chief executive officer and to certain other

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highly compensated officers. Remuneration in excess of \$1.0 million may be deducted if, among other things, it qualifies as performance-based compensation within the meaning of the Code. In this regard, the compensation income realized upon the exercise of stock options granted under a stockholder-approved stock option plan generally will be deductible so long as the options are granted by a committee whose members are non-employee directors and certain other conditions are satisfied.

As we had been a privately-held corporation, the deductibility limit imposed by Section 162(m) previously did not apply to us. Moreover, under a certain Section 162(m) exception, any compensation paid pursuant to a compensation plan in existence before the effective date of this public offering will not be subject to the \$1.0 million limitation until the earliest of: (i) the expiration of the compensation plan, (ii) a material modification of the compensation plan (as determined under Section 162(m)), (iii) the issuance of all the employer stock and other compensation allocated under the compensation plan, or (iv) the first meeting of stockholders at which directors are elected after the close of the third calendar year following the year in which the public offering occurs. We expect that, where reasonably practicable, we will seek to qualify the variable compensation paid to our executive officers for the performance-based compensation exemption from the deductibility limit. As such, in approving the amount and form of compensation for our executive officers in the future, we will consider all elements of the cost to us of providing such compensation, including the potential impact of Section 162(m). The Committee may, in its judgment, authorize compensation payments that do not comply with an exemption from the deductibility limit when it believes that such payments are appropriate to attract and retain executive talent.

Taxation of Parachute Payments and Deferred Compensation

We did not provide any executive officer, including any NEO, with a gross-up or other reimbursement payment for any tax liability that he or she might owe as a result of the application of Sections 280G, 4999, or 409A of the Code during 2011 and we have not agreed and are not otherwise obligated to provide any NEOs with such a gross-up. Sections 280G and 4999 of the Code provide that executive officers and directors who hold significant equity interests and certain other service providers may be subject to an excise tax if they receive payments or benefits in connection with a change in control that exceeds certain prescribed limits, and that we, or a successor, may forfeit a deduction on the amounts subject to this additional tax. Section 409A of the Code also imposes additional significant taxes on the individual in the event that an executive officer, director or other service provider receives deferred compensation that does not meet the requirements of Section 409A of the Code.

Accounting Treatment

We follow Financial Accounting Standards Board Accounting Standards Codification Topic 718, Stock Compensation, or ASC Topic 718, for our stock-based awards. ASC Topic 718 requires companies to measure the compensation expense for all share-based payment awards made to employees and directors, including stock options and restricted stock awards, based on the grant date fair value of these awards. This calculation is performed for accounting purposes even though our executive officers may never realize any value from their awards. ASC Topic 718 also requires companies to recognize the compensation cost of their stock-based compensation awards in their income statements over the period that an executive officer is required to render service in exchange for the option or other award.

Table of Contents**Summary Compensation Table**

The following table presents information concerning the total compensation of our named executive officers, for services rendered to us in all capacities during the fiscal years ended December 31, 2010 and 2011:

Summary Compensation Table

Name and Principal Position	Year	Salary	Bonus	Option Awards(1)	Non-equity	Other	Total
					Incentive Plan Compensation(2)		
Joseph L. Jackson Chief Executive Officer	2011	\$ 400,000	\$	\$	\$ 260,000	\$ 2,450(3)	\$ 662,450
	2010	400,000		1,486,674	200,000	376,095(4)	2,462,769
Richard T. Green Chief Financial Officer	2011	281,875			146,575	1,715(3)	430,165
	2010	279,583	20,000	305,211	112,750	39,133(5)	756,677
Edgar O. Montes Senior Vice President, Service Delivery Operations	2011	218,400			113,568	2,378(3)	334,346
	2010	214,933	20,000	136,457	87,360	2,450(3)	461,200
Kimberly L. Jackson Senior Vice President, General Counsel and Secretary	2011	198,550			103,246	1,986(3)	303,782
	2010	196,206	25,000	82,344	79,420	2,450(3)	385,420

- (1) Amounts represent the aggregate fair market value of options granted in the fiscal years ended December 31, 2010 and 2011 to the named executive officer calculated in accordance with ASC Topic 718 without regard to estimated forfeitures. See Note 12 to our consolidated financial statements for a discussion of assumptions made in determining the grant date fair value and compensation expense of our stock options.
- (2) Amounts represent the total performance-based bonuses earned for services rendered in 2010 and 2011 under our Bonus Plan. For more information, please see the description of the Bonus Plan in the Compensation Discussion and Analysis section.
- (3) Amount represents 401(k) matching contribution by us.
- (4) Amounts represent (i) \$201,906 in reimbursements for relocation related expenses, (ii) \$171,739 in tax gross-ups associated with taxable relocation related expenses and (iii) \$2,450 in 401(K) matching contribution by us.
- (5) Amounts represent (i) \$20,550 in reimbursements for relocation related expenses, (ii) \$16,133 in tax gross-ups associated with taxable relocation related expenses and (iii) \$2,450 in 401K matching contribution by us.

Grants of Plan-Based Awards

The following table presents grants of plan-based awards to our named executive officers during 2011:

Name	Grant Date	Threshold	Estimated Future Payouts Under Non-Equity Incentive Plan Awards		Estimated Future Payouts under Equity Incentive Plan Awards	All Other Option Awards: Number of Securities Underlying Options (3)	Exercise Price of Options (\$/sh)(3)	Grant Date Fair Value of Options (3)
			Target (1)	Maximum (2)				
Joseph L. Jackson		\$	\$ 200,000	\$ 265,000			\$	\$
Richard T. Green			112,750	149,394				
Edgar O. Montes			87,360	115,752				

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Kimberly L. Jackson

79,420

105,232

- (1) Amounts reported in this column represent the target performance-based bonus of each named executive officer granted under our Bonus Plan, as described in Compensation Discussion and Analysis.

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- (2) The maximum bonus payout amount represents the amount payable if we achieve an Adjusted EBITDA of greater than \$29,500,000, actual adjusted organic revenue growth greater than 6.25% and full achievement of the individual performance goals, as described in the Compensation Discussion and Analysis section.
- (3) No equity awards were granted in 2011.

Outstanding Equity Awards at Fiscal Year-End

The following table presents certain plan information of equity awards held by our named executive officers as of December 31, 2011:

Name	Grant Date	Number of Securities Underlying Unexercised Exercisable Options	Exercise Price of Option	Expiration Date of Options
Joseph L. Jackson	5/25/2007(1)	675,000(3)	\$ 9.42	5/25/2017
	2/7/2008(1)	50,000(4)	8.28	2/7/2018
	5/7/2009(1)	100,000(5)	6.14	5/7/2019
	5/6/2010(1)	187,500(6)	5.32	5/6/2020
	5/6/2010(2)	187,500(7)	5.32	5/6/2020
Richard T. Green	11/4/2010(2)	150,000(7)	6.18	11/4/2020
	5/29/2009(1)	150,000(8)	6.14	5/29/2019
	5/6/2010(1)	87,500(9)	5.32	5/6/2020
Edgar O. Montes	11/4/2010(2)	30,000(7)	6.18	11/4/2020
	2/8/2007(1)	27,500(3)	8.48	2/8/2017
	4/18/2007(1)	22,500(3)	9.42	4/18/2017
	5/1/2007(1)	25,000(3)	9.42	5/1/2017
	2/7/2008(1)	25,000(10)	8.28	2/7/2018
	5/29/2009(1)	25,000(11)	6.14	5/29/2019
	5/6/2010(1)	30,000(12)	5.32	5/6/2020
Kimberly L. Jackson	11/4/2010(2)	20,000(7)	6.18	11/4/2020
	5/7/2008(1)	50,000(13)	8.24	5/7/2018
	5/29/2009(1)	25,000(11)	6.14	5/29/2019
	5/6/2010(1)	17,500(14)	5.32	5/6/2020
	11/4/2010(2)	12,500(7)	6.18	11/4/2020

- (1) 25% of the shares on the first anniversary of the vesting commencement date, and an additional 1/48th of the shares on each of the 36 succeeding monthly anniversaries of the vesting commencement date, subject to the respective named executive officer's continued service to us on each such vesting date. The options contain an early exercise feature subject to our right of repurchase.
- (2) The shares subject to the option vest in full on the seven-year anniversary of the grant date; provided, however, (a) 25% of each grant will vest immediately if certain financial performance goals are met, (b) 25% of each grant will vest immediately upon a successful listing of our common stock on NASDAQ or the New York Stock Exchange and (c) the remaining 50% of each grant will vest immediately if both (a) and (b) occur, subject to the respective named executive officer's continued service to us on each such vesting date. The vesting of the option is described in the Compensation Discussion and Analysis section. The options contain an early exercise feature subject to our right of repurchase.
- (3) This option is fully vested.
- (4) As of December 31, 2011, 47,917 of the shares underlying this option were vested.
- (5) As of December 31, 2011, 64,583 of the shares underlying this option were vested.
- (6) As of December 31, 2011, 74,219 of the shares underlying this option were vested.
- (7) As of December 31, 2011, none of the shares underlying this option were vested.
- (8) As of December 31, 2011, 112,500 of the shares underlying this option were vested.
- (9) As of December 31, 2011, 34,635 of the shares underlying this option were vested.
- (10) As of December 31, 2011, 23,958 of the shares underlying this option were vested.
- (11) As of December 31, 2011, 16,146 of the shares underlying this option were vested.

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(12) As of December 31, 2011, 11,875 of the shares underlying this option were vested.

(13) As of December 31, 2011, 46,875 of the shares underlying this option were vested.

(14) As of December 31, 2011, 6,927 of the shares underlying this option were vested.

Option Exercises and Stock Vested

None of our named executive officers exercised stock options or had any restricted stock vest in the fiscal year ended December 31, 2011.

Employment Agreement and Executive Severance Benefit Agreements

Joseph L. Jackson

We entered into a second amended and restated employment agreement, or the employment agreement, with Joseph L. Jackson, our Chief Executive Officer, on November 23, 2010. The employment agreement has no specific term and constitutes at will employment. Mr. Jackson's current annual base salary is \$400,000 and he is eligible to receive an annual bonus with a target amount equal to no less than 50% of his then-current salary. The actual annual bonus amount depends on Mr. Jackson's performance and achievement of corporate performance goals set for that year, as determined by our compensation committee.

The employment agreement provides that in the event of an involuntary termination, if Mr. Jackson executes a general release of claims in favor of us, he will receive at least two months of salary and medical care coverage. If he also enters into and abides by an agreement not to compete with us, Mr. Jackson will receive payment of his salary over a total period of 12 months and reimbursement (plus a tax gross up for such reimbursement, if applicable) for the cost of medical care coverage through our benefit plans for Mr. Jackson, his spouse and his eligible dependents for a total period of 12 months.

In the event of an involuntary termination of his employment with us (i) within 24 months following a change in control of us or (ii) during the time between signing a definitive agreement for a change in control transaction and either (x) the closing of such change in control transaction or (y) the termination of such agreement without completion of the proposed change in control transaction, the employment agreement provides that he will receive the severance described above (subject to the execution of a release of claims and non-compete covenant as described above), plus: (a) accelerated vesting of certain stock options listed in his employment agreement with respect to the number of shares subject thereto that would have vested had he remained an employee for an additional 24 months; and (b) potential payment of all or a portion of his annual bonus, at the discretion of our board of directors.

The terms "involuntary termination" and "change in control" have the meanings set forth in the employment agreement.

Richard T. Green, Edgar O. Montes and Kimberly L. Jackson

On January 27, 2011, we entered into amended and restated executive severance benefit agreements, or the severance benefit agreements, with each of our named executive officers, other than Mr. Jackson. Each severance benefit agreement provides that in the event of an involuntary termination, if the named executive officer executes a general release of claims in favor of us, he or she will receive at least one month of base salary and medical care coverage. If the named executive officer also enters into and abides by an agreement not to compete with us, such named executive officers will receive payment of his or her salary over a total period of six months and reimbursement (plus a tax gross up for such reimbursement, if applicable) for the cost of medical care coverage through our benefit plans for such named executive officer and his or her spouse and eligible dependents for a total period of six months.

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In the event of an involuntary termination of employment with us (i) within 12 months following a change in control of us or (ii) during the time between signing a definitive agreement for a change in control transaction and either (x) the closing of such change in control transaction or (y) the termination of such agreement without completion of the proposed change in control transaction, the severance benefit agreements provide that he or she will receive the severance described above (subject to the execution of a release of claims and non-compete covenant as described above), plus: (a) accelerated vesting of certain stock options listed in his employment agreement with respect to the number of shares subject thereto that would have vested had he or she remained an employee for an additional 18 months; and (b) a prorated payment of such named executive officer's annual target bonus based on the number of months that he or she was an employee during such fiscal year.

The terms "involuntary termination" and "change in control" have the meanings set forth in the severance benefit agreements.

Potential Payments Upon Termination or Change in Control

The following table shows the amounts each of our named executive officers would have received in the event of their involuntary termination, assuming the involuntary termination took place on December 31, 2011, the last day of our most recent completed fiscal year. The terms "involuntary termination" and "change in control" have the meanings set forth in the relevant agreement.

Name	Benefits	Involuntary Termination	
		Not in connection with change in control	In connection with change in control
Joseph L. Jackson	Severance Payment (Salary)	\$ 400,000(1)	\$ 400,000(1)
	Severance Payment (Bonus)		** (2)
	Healthcare Benefits	31,394(3)	31,394(3)
	Acceleration of Stock Options		1,837,355(4)
Richard T. Green	Severance Payment (Salary)	140,937(5)	140,937(5)
	Severance Payment (Bonus)		112,750(6)
	Healthcare Benefits	15,697(7)	15,697(7)
	Acceleration of Stock Options		269,484(8)
Edgar O. Montes	Severance Payment (Salary)	109,200(5)	109,200(5)
	Severance Payment (Bonus)		87,360(6)
	Healthcare Benefits	15,697(7)	15,697(7)
	Acceleration of Stock Options		79,949(8)
Kimberly L. Jackson	Severance Payment (Salary)	99,275(5)	99,275(5)
	Severance Payment (Bonus)		79,420(6)
	Healthcare Benefits	4,919(7)	4,919(7)
	Acceleration of Stock Options		62,787(8)

- (1) Upon an involuntary termination, Mr. Jackson would receive payment of his salary over a period of 12 months, provided Mr. Jackson executes a general release of claims and an agreement not to compete with us during the period of time that he receives severance benefits from us.
- (2) Upon an involuntary termination (i) within 24 months of a change in control or (ii) during the time between the signing and closing a definitive agreement for a change in control transaction, Mr. Jackson will be considered for a termination bonus, with the amount of such termination bonus to be determined by our board of directors subject to achieving corporate and individual performance goals.
- (3) Upon an involuntary termination, Mr. Jackson would receive reimbursement, and tax gross-up payments for such reimbursement, for the cost of medical care coverage through our benefit plans for Mr. Jackson, his spouse and his eligible dependents for a period of 12 months, provided Mr. Jackson agrees to a general release of claims and covenant not to compete with us during the period of time that he receives severance benefits from us.

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- (4) Upon an involuntary termination (i) within 24 months of a change in control or (ii) during the time between signing and closing a definitive agreement for a change in control transaction, 24 months of unvested shares subject to stock options that vest over time would accelerate and 100% of unvested shares subject to stock options that have performance vesting would accelerate. Value represents the gain the named executive officer would receive, calculated as the difference between the stock price on December 31, 2011 and the exercise price of such accelerated shares. The stock price as of December 31, 2011 as determined by our board of directors was \$9.59 per share.
- (5) Upon an involuntary termination, the named executive officer would receive payment of his or her salary over a period of 6 months, provided the named executive officer executes a general release of claims and an agreement not to compete with us during the period of time that he or she receives severance benefits from us.
- (6) Upon an involuntary termination (i) within 12 months of a change in control or (ii) during the time between signing and closing a definitive agreement for a change in control transaction, the named executive officer will be eligible to receive a payment equal to the pro-rata portion of their annual target bonus.
- (7) Upon an involuntary termination, the named executive officer would receive reimbursement, and tax gross-up payments for such reimbursement, for the cost of medical care coverage through our benefit plans for the named executive officer, his or her spouse and dependents for a period of 6 months, provided the named executive officer executes a general release of claims and an agreement not to compete with us during the period of time that he or she receives severance benefits from us.
- (8) Upon an involuntary termination (i) within 12 months of a change in control or (ii) during the time between signing and closing a definitive agreement for a change in control transaction, 18 months of unvested shares subject to stock options that vest over time would accelerate. Value represents the gain the named executive officer would receive, calculated as the difference between the stock price on December 31, 2011 and the exercise price of such accelerated shares. The stock price as of December 31, 2011 as determined by our board of directors was \$9.59 per share.

Employee Benefit Plans

2010 Equity Incentive Plan

Our 2010 Equity Incentive Plan, or our 2010 Plan, was adopted by our board of directors in May 2010 and approved by our stockholders in June 2010. Our board of directors and our stockholders adopted and approved amendments to the 2010 Plan in connection with our initial public offering. Our 2010 Plan provides for the grant of incentive stock options, or ISOs, within the meaning of Code Section 422, to our employees, and for the grant of nonstatutory stock options, or NSOs, stock appreciation rights, restricted stock, and restricted stock units to our employees, directors and consultants.

Authorized Shares. The maximum aggregate number of shares that may be issued under our 2010 Plan is 750,000 shares of our common stock. In addition, the number of shares available for issuance under our 2010 Plan will be annually increased on the first day of each of our fiscal years beginning in 2011, by an amount equal to the least of:

1,500,000 shares;

3% of the outstanding shares of our common stock as of the last day of our immediately preceding fiscal year; or

such other amount as our board of directors may determine.

Shares may be authorized, but unissued, or reacquired common stock. Shares issued pursuant to awards under our 2010 Plan that we repurchase or that are forfeited, as well as shares used to pay the exercise price of an award or to satisfy the tax withholding obligations related to an award, will become available for future grant under our 2010 Plan. In addition, to the extent that an award is paid out in cash rather than shares, such cash payment will not reduce the number of shares available for issuance under our 2010 Plan.

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Plan Administration. Our 2010 Plan is administered by the board of directors or a committee appointed by the board of directors. Subject to the provisions of our 2010 Plan, the administrator has the power to determine the terms of awards, including the recipients (also referred to herein as participants), the exercise price, if any, the number of shares subject to each award, the fair value of a share of our common stock, the vesting schedule applicable to the awards, together with any vesting acceleration, and the form of consideration, if any, payable upon exercise of the award and the terms of the award agreement for use under our 2010 Plan. The administrator may institute a program under which (i) outstanding awards are cancelled in exchange for awards of the same or different type and/or cash, (ii) participants may transfer outstanding awards to a financial institution or other person or entity, and (iii) the exercise price of awards are increased or decreased.

Stock Options. Under the 2010 Plan, the exercise price of options must equal at least the fair market value of our common stock on the date of grant and the term of the options may not exceed 10 years, provided, however, that an ISO held by a participant who owns more than 10% of the total combined voting power of all classes of our stock may not have a term in excess of five years and must have an exercise price of at least 110% of the fair market value of our common stock on the grant date. Subject to the provisions of the 2010 Plan, the administrator determines the remaining terms of the options (for example, vesting). After the termination of employment or other service, the participant may exercise his or her option, to the extent vested as of such date of termination, for the period of time stated in his or her option agreement subject to the terms of the 2010 Plan. However, in no event may an option be exercised later than the expiration of its term.

Stock Appreciation Rights. Stock appreciation rights are awards that allow the recipient to receive the appreciation in the fair market value of the common stock between the exercise date and the date of grant. Subject to the provisions of the 2010 Plan, the administrator determines the terms of stock appreciation rights, including when such rights vest and become exercisable and whether to settle such awards in cash or with shares of our common stock, or a combination of both, except that the per share exercise price for the shares to be issued pursuant to the exercise of a stock appreciation right will be no less than the fair market value per share on the date of grant. The specific terms will be set forth in an award agreement.

Restricted Stock. Restricted stock awards are grants of shares of our common stock that are subject to various restrictions, including restrictions on transferability and forfeiture provisions. Shares of restricted stock will vest and the restrictions on such shares will lapse, based on terms and conditions established by the administrator. Recipients of restricted stock awards generally will have voting and dividend rights with respect to such shares upon grant without regard to vesting, unless the administrator provides otherwise. Shares of restricted stock that do not vest for any reason will be forfeited by the recipient and will revert to us. The specific terms will be set forth in an award agreement.

Restricted Stock Units. Each restricted stock unit granted under the 2010 Plan is a bookkeeping entry representing an amount equal to the fair market value of one share of our common stock. The administrator determines the terms and conditions of restricted stock units including the vesting criteria and the form and timing of payment. The administrator determines in its sole discretion whether an award will be settled in stock, cash or a combination of both. The specific terms will be set forth in an award agreement.

Transferability. The 2010 Plan generally does not allow for the transfer of awards other than by will or the laws of descent and distribution, unless the administrator otherwise determines, and only the recipient of an award may exercise an award during his or her lifetime.

Certain Adjustments. In the event of any dividend or other distribution, recapitalization, stock split or other similar change in our corporate structure, the administrator will adjust the number and class of shares that may be issued and/or the number, class and price of shares covered by awards and the numerical shares limits under the 2010 Plan, in order to prevent the decrease or enlargement of benefits or potential benefits intended to be made under the 2010 Plan.

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Merger or Change in Control. Our 2010 Plan provides that in the event of a merger or change in control, as defined under our 2010 Plan, each outstanding award will be treated as the administrator determines, except that if a successor corporation or its parent or subsidiary does not assume or substitute an equivalent award for any outstanding award, then such award will fully vest, all restrictions on such award will lapse, all performance goals or other vesting criteria applicable to such award will be deemed achieved at 100% of target levels and such award will become fully exercisable, if applicable, for a specified period prior to the transaction. The award will then terminate upon the expiration of the specified period of time.

Plan Amendment, Termination. Our board of directors has the authority to amend, suspend or terminate our 2010 Plan provided such action does not impair the existing rights of any participant. Our 2010 Plan will automatically terminate in 2020, unless we terminate it sooner.

2012 Employee Stock Purchase Plan

Concurrently with our initial public offering, our board of directors and our stockholders adopted and approved our 2012 Employee Stock Purchase Plan, or the ESPP. Our executive officers and all of our other employees are allowed to participate in our ESPP. A total of 500,000 shares of our common stock has been made available for sale under our ESPP. In addition, our ESPP provides for annual increases in the number of shares available for issuance under the ESPP on the first day of each fiscal year beginning with the 2012 fiscal year, equal to the least of:

500,000 shares;

1% of the outstanding shares of our common stock as of the last day of our immediately preceding fiscal year; or

such other amount as may be determined by the administrator.

Our board of directors or its committee has full and exclusive authority to interpret the terms of the ESPP and determine eligibility.

Our employees are eligible to participate if they have completed at least 90 days of service with us and work at least 20 hours per week for more than five months during a calendar year. However, an employee may not be granted rights to purchase stock under our ESPP if such employee:

immediately after the grant would own stock possessing 5% or more of the total combined voting power or value of all classes of our capital stock; or

holds rights to purchase stock under all of our employee stock purchase plans that would accrue at a rate that exceeds \$25,000 worth of our stock for each calendar year.

Our ESPP is intended to qualify under Code Section 423, and provides for consecutive three-month offering periods. The offering periods generally start on the first trading day on or after February 15, May 15, August 15 and November 15 of each year, except that the first offering period under the ESPP commenced upon the first trading day after the closing of our initial public offering and will end on the first trading day on or before August 15, 2012, and the second offering period will begin on the first trading day on or after August 15, 2012. Each offering period (other than the first offering period) will begin after one exercise date and will end with the next exercise date approximately three months later. The administrator may, in its discretion, modify the terms of future offering periods.

Our ESPP permits participants to purchase common stock through payroll deductions of up to 25% of their eligible compensation, which includes a participant's base straight time gross earnings, commissions, payments for overtime and shift premium, incentive compensation, bonuses and other similar compensation provided under our normal payroll practices. A participant may purchase a maximum of 5,000 shares of common stock during each offering period.

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On the first trading day of each offering period, each participant automatically is granted an option to purchase shares of our common stock. The option expires at the end of the offering period or upon termination of employment, whichever is earlier, but is exercised at the end of each offering period to the extent of the payroll deductions accumulated during such offering period. The purchase price of the shares will be 85% of the lower of the fair market value of our common stock on the first trading day of the offering period or on the last day of the offering period. Participants may end their participation at any time during an offering period, and will be paid their accrued payroll deductions that have not yet been used to purchase shares of common stock. Participation ends automatically upon termination of employment with us.

A participant may not transfer rights granted under the ESPP other than by will, the laws of descent and distribution or as otherwise provided under the ESPP.

In the event of our merger or change in control, as defined under the ESPP, a successor corporation may assume or substitute each outstanding purchase right. If the successor corporation refuses to assume or substitute for the outstanding purchase rights, the offering period then in progress will be shortened, and a new exercise date will be set which will occur prior to the proposed merger or change in control. The administrator will notify each participant in writing that the exercise date has been changed and that the participant's option will be exercised automatically on the new exercise date unless the participant has already withdrawn from the offering period.

Our ESPP will automatically terminate in 2032, unless we terminate it sooner. In addition, our board of directors has the authority to amend, suspend or terminate our ESPP, except that, subject to certain exceptions described in the ESPP, no such action may adversely affect any outstanding rights to purchase stock under our ESPP.

2000 Stock Option/Stock Issuance Plan

Our 2000 Stock Option/Stock Issuance Plan, or our 2000 Plan, was adopted in June 2000 and was subsequently amended a number of times to increase the share limit of the 2000 Plan. Our 2000 Plan provided for the grant of ISOs to our employees, and for the grant of NSOs and stock issuances in the form of stock purchase rights or stock bonuses to our employees, directors, and consultants. The 2000 Plan terminated in 2010 and as a result, no additional awards will be granted under the 2000 Plan. However, the 2000 Plan will continue to govern the terms and conditions of the outstanding awards previously granted thereunder.

Authorized Shares. We had reserved a total of 5,080,111 shares of our common stock pursuant to the 2000 Plan. As of June 30, 2012, options to purchase 3,918,491 shares of our common stock were outstanding under the 2000 Plan.

Plan Administration. Our Board, or a committee appointed by the Board, administered the 2000 Plan. Subject to the provisions of our 2000 Plan, the administrator had the power to determine the terms of awards, including the recipients, the exercise price, if any, the number of shares subject to each award, the vesting schedule applicable to the awards, together with any vesting acceleration, and the terms of the award agreement for use under our 2000 Plan. With the consent of affected option holders, the administrator may institute a program under which outstanding options are cancelled in exchange for new options covering the same or a different number of shares of our common stock but with an exercise price per share based on the fair market value per share of our common stock on the new option grant date.

Stock Options. The 2000 Plan permitted the grant of ISOs and NSOs. The exercise price of ISOs must equal at least 100% of the fair market value of our common stock on the date of grant and the exercise price of NSOs may not be less than 85% of the fair market value of our common stock on the date of grant. The term of an option may not exceed 10 years. Provided, however, that an option held by a participant who owns more than

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10% of the total combined voting power of all classes of our stock, or a 10% Stockholder, must have an exercise price of at least 110% of the fair market value of our common stock on the date of grant, and if such option held by a 10% Stockholder is an ISO, the ISO may not have a term in excess of five years.

Subject to the provisions of our 2000 Plan, the administrator determined the remaining terms of the options (e.g., vesting). However, the vesting schedule of options granted other than to officers, members of the Board and independent consultants must allow for vesting with respect to at least 20% of the shares per year, with the first vesting event occurring not later than one year after grant. After the termination of employment or other service, the participant may exercise his or her option, to the extent vested as of such date of termination, for the period of time stated in his or her option agreement subject to the terms of the 2000 Plan. However, in no event may an option be exercised later than the expiration of its term. Additionally, if a recipient's service is terminated for misconduct, the recipient's outstanding options immediately terminate.

Stock Issuances. Stock issuance awards are grants of rights to purchase our common stock for cash or to receive our common stock as a bonus for past services rendered to us. Stock issuance awards may be subject to various restrictions, including restrictions on transferability and forfeiture provisions. After the administrator determines that it will offer a stock issuance award, it advises the recipient of the terms, conditions, and restrictions related to the grant, including the number of shares that the recipient is entitled to purchase or receive, the price to be paid, if any, which may not be less than 85% of the fair market value of our common stock on the date of grant (or 110% of the fair market value of our common stock on the date of grant if the recipient is a 10% Stockholder), the form of consideration the recipient may use to pay the purchase price, and the vesting schedule applicable to the award, if any. However, the vesting schedule of an award granted other than to officers, members of the Board and independent consultants must allow for vesting with respect to at least 20% of the shares per year, with the first vesting event occurring not later than one year after grant. A recipient accepts the offer by execution of a stock issuance agreement in the form determined by the administrator, which will set forth all the terms of the award.

Transferability of Awards. The 2000 Plan generally does not allow for the transfer of awards other than by will or the laws of descent and distribution and only the recipient of an award may exercise the award during his or her lifetime. Certain assignments are permitted with respect to NSOs to family members.

Certain Adjustments. If any change is made in our common stock subject to the 2000 Plan, such as through a stock split, stock dividend, recapitalization, combination of shares, exchange of shares, or other change affecting the outstanding common stock as a class without the receipt of consideration by us, appropriate adjustments will be made to the number and/or class of securities and the exercise price per share in effect under each outstanding option.

Corporate Transaction. In the event of corporate transaction, as defined under our 2000 Plan, each outstanding award will be either assumed or replaced with a cash incentive program preserving the spread existing in the unvested options, by the successor corporation or its parent. Unless otherwise provided for in a recipient's award agreement, if the successor corporation or its parent refuses to assume awards or establish a cash incentive program for options, then such awards will fully vest (unless specified otherwise in an applicable award agreement), and the awards will terminate if not exercised, if applicable, at or prior to the corporate transaction.

Plan Amendment, Termination. Our Board has the authority to amend the 2000 Plan provided such action does not impair the rights of any award recipient. The 2000 Plan terminated in 2010, but continues to govern the terms and conditions of awards granted under the 2000 Plan.

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401(k) Plan

We maintain a tax qualified 401(k) retirement plan for all employees who satisfy certain eligibility requirements, including requirements relating to length of service. Under our 401(k) plan, employees may elect to defer a portion of their eligible compensation, subject to applicable annual Code limits. Employees can make contributions to the plan on a before tax basis up to 85% of their eligible compensation, subject to the maximum amount prescribed by the Internal Revenue Service. Under the 401(k) plan, we provide discretionary matching contributions at 25% of the first 4% of the employee contribution, up to a maximum of 1% of the employee's eligible compensation. We intend for the 401(k) plan to qualify under Section 401(a) and 501(a) of the Code so that contributions by employees to the 401(k) plan, and income earned on those contributions, are not taxable to employees until withdrawn from the 401(k) plan.

Limitation on Liability and Indemnification Matters

Our amended and restated certificate of incorporation contains provisions that limit the liability of our directors for monetary damages to the fullest extent permitted by Delaware law. Consequently, our directors will not be personally liable to us or our stockholders for monetary damages for any breach of fiduciary duties as directors, except liability for:

any breach of the director's duty of loyalty to us or our stockholders;

any act or omission not in good faith or that involves intentional misconduct or a knowing violation of law;

unlawful payments of dividends or unlawful stock repurchases or redemptions as provided in Section 174 of the Delaware General Corporation Law; or

any transaction from which the director derived an improper personal benefit.

Our amended and restated certificate of incorporation and amended and restated bylaws provide that we are required to indemnify our directors and officers, in each case to the fullest extent permitted by Delaware law. Our amended and restated bylaws also provide that we are obligated to advance expenses incurred by a director or officer in advance of the final disposition of any action or proceeding, and permit us to secure insurance on behalf of any officer, director, employee or other agent for any liability arising out of his or her actions in that capacity regardless of whether we would otherwise be permitted to indemnify him or her under the provisions of Delaware law. We have entered and expect to continue to enter into agreements to indemnify our directors, executive officers and other employees as determined by our board of directors. With specified exceptions, these agreements provide for indemnification for related expenses including, among other things, attorneys' fees, judgments, fines and settlement amounts incurred by any of these individuals in any action or proceeding. We believe that these bylaw provisions and indemnification agreements are necessary to attract and retain qualified persons as directors and officers. We also maintain directors' and officers' liability insurance.

The limitation of liability and indemnification provisions in our amended and restated certificate of incorporation and amended and restated bylaws may discourage stockholders from bringing a lawsuit against our directors and officers for breach of their fiduciary duty. They may also reduce the likelihood of derivative litigation against our directors and officers, even though an action, if successful, might benefit us and other stockholders. Further, a stockholder's investment may be adversely affected to the extent that we pay the costs of settlement and damage awards against directors and officers as required by these indemnification provisions. Insofar as indemnification for liabilities arising under the Securities Act of 1933, as amended, may be permitted to our directors, officers and controlling persons pursuant to the foregoing provisions, or otherwise, we have been advised that, in the opinion of the SEC, such indemnification is against public policy as expressed in the Securities Act, and is, therefore, unenforceable. At present, there is no pending litigation or proceeding involving any of our directors, officers or employees for which indemnification is sought, and we are not aware of any threatened litigation that may result in claims for indemnification.

Table of Contents**CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS**

In addition to the cash and equity compensation arrangements of our directors and executive officers discussed above under *Management Director Compensation and Executive Compensation*, the following is a description of transactions since January 1, 2009, to which we have been a participant in which the amount involved exceeded or will exceed \$120,000 and in which any of our directors, executive officers, beneficial holders of more than 5% of our capital stock, or entities affiliated with them, or immediate family members of a director or executive officer, had or will have a direct or indirect material interest. None of our directors or executive officers or immediate family members of a director or executive officer, purchased shares of our convertible preferred stock during this time period.

Bridge Debt Financing

In December 2009, we entered into a Note and Warrant Purchase Agreement with certain of our stockholders pursuant to which we issued convertible promissory notes in an aggregate principal amount of \$20,000,000 and warrants to purchase shares of preferred stock. In July 2010, we entered into an amendment to the Note and Warrant Purchase Agreement. The convertible promissory notes accrued interest at the rate of 10% per annum. In July 2010, the convertible promissory notes were converted into an aggregate of 5,294,514 shares of our Series E preferred stock at a conversion price of \$4.00 per share and the warrants to purchase shares of preferred stock became exercisable to purchase an aggregate of 8,733,617 shares of our Series E-1 preferred stock at exercise prices of \$2.29 per share.

The following table summarizes the investment amounts under the bridge debt financing:

Name of Stockholder	Aggregate Principal Amount of Notes	Shares of Series E Preferred Stock issued upon Conversion of Notes	Shares of Series E-1 Preferred Stock issued upon Exercise of Preferred Warrants
Funds managed by VantagePoint Capital Partners(1)	\$ 16,094,731	4,260,693	7,028,265
Funds managed by Advent International Corporation(2)	2,165,153	573,168	945,477
Camden Partners(3)	1,694,049	448,458	739,759

- (1) Funds managed by VantagePoint holding our securities whose shares are aggregated for purposes of reporting share ownership information are VantagePoint Venture Partners IV (Q), L.P., VantagePoint Venture Partners IV, L.P. and VantagePoint Venture Partners IV Principals Fund, L.P. Thomas A. Bevilacqua is a member of the general partner of these funds and a member of our board of directors.
- (2) Funds managed by Advent International Corporation holding our securities whose shares are aggregated for purposes of reporting share ownership information are Advent Partners II Limited Partnership, Advent Partners II-A Limited Partnership, Advent Partners DMC III Limited Partnership, Digital Media & Communications III Limited Partnership, Digital Media & Communications III-A Limited Partnership, Digital Media & Communications III-B Limited Partnership, Digital Media & Communications III-C Limited Partnership, Digital Media & Communications III-D C.V. and Digital Media & Communications III-E C.V. Leigh E. Michl is a limited partner of certain of these Advent Funds and was a member of our board of directors until January 31, 2012.
- (3) Affiliates of Camden Partners holding our securities whose shares are aggregated for purposes of reporting share ownership information are Camden Partners Strategic Fund III, L.P. and Camden Partners Strategic Fund III-A, L.P. Richard M. Berkeley is a managing member of Camden Partners and a member of our board of directors.

Table of Contents**Purchases of Stock by Affiliates**

In July 2009, we purchased shares of our capital stock from certain former stockholders, including a former director and executive officer, and assigned the right to purchase additional shares of our capital stock from such former stockholders to certain of our existing investors, as set forth below. We received no consideration in connection with such assignment or purchases.

Name of Stockholder	Shares of Common Stock Purchased/ (Sold)(1)	Shares of Series A-1 Preferred Stock Purchased/ (Sold)(2)	Shares of Series A-2 Preferred Stock Purchased/ (Sold)(2)	Shares of Series D Preferred Stock Purchased/ (Sold)(2)
Registrant	185,634	0	0	0
Funds managed by VantagePoint Capital Partners(3)	149,739	6,857	3,917	27,106
Funds managed by Advent International Corporation(4)	20,084	919	526	3,635
Camden Partners(5)	15,383	704	403	2,784
Jon Kessler	(60,634)	0	0	(30,817)
Laura Gottsman	(310,634)	0	0	0

- (1) The price per share paid for each share of common stock was \$2.00.
- (2) The price per share paid for each share of preferred stock was \$2.16.
- (3) Funds managed by VantagePoint holding our securities whose shares are aggregated for purposes of reporting share ownership information are VantagePoint Venture Partners IV (Q), L.P., VantagePoint Venture Partners IV, L.P. and VantagePoint Venture Partners IV Principals Fund, L.P.
- (4) Funds managed by Advent International Corporation holding our securities whose shares are aggregated for purposes of reporting share ownership information are Advent Partners II Limited Partnership, Advent Partners II-A Limited Partnership, Advent Partners DMC III Limited Partnership, Digital Media & Communications III Limited Partnership, Digital Media & Communications III-A Limited Partnership, Digital Media & Communications III-B Limited Partnership, Digital Media & Communications III-C Limited Partnership, Digital Media & Communications III-D C.V. and Digital Media & Communications III-E C.V.
- (5) Affiliates of Camden Partners holding our securities whose shares are aggregated for purposes of reporting share ownership information include Camden Partners Strategic Fund III, L.P. and Camden Partners Strategic Fund III-A, L.P.

Engagement of Morgan, Lewis & Bockius LLP

Prior to September 2009, the law firm of Morgan, Lewis & Bockius LLP, or Morgan Lewis, served as our outside legal counsel. John W. Larson, a member of our board of directors since June 2000 and chairman of our board of directors since July 2006, was a partner at Morgan Lewis from January 2003 until his retirement in December 2009. Amounts paid to Morgan Lewis for services and fees were \$211,815, \$10,890 and less than \$1,000 in the years ending December 31, 2009, 2010 and 2011, respectively. Mr. Larson had no financial interest in the transactions between us and Morgan Lewis during this period. We believe that the services performed by Morgan Lewis were provided on terms no more or less favorable than those with unrelated parties.

Related Party Transaction Policy

We have adopted a formal written policy that our executive officers, directors, holders of more than 5% of any class of our voting securities, and any member of the immediate family of and any entity affiliated with any of the foregoing persons, are not permitted to enter into a related party transaction with us without the prior consent of our audit committee, or other independent members of our board in the case it is inappropriate for our audit committee to review such transaction due to a conflict of interest. Any request for us to enter into a

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transaction with an executive officer, director, principal stockholder, or any of their immediate family members or affiliates, in which the amount involved exceeds \$120,000 must first be presented to our audit committee for review, consideration and approval. In approving or rejecting any such proposal, our audit committee is to consider the relevant facts and circumstances available and deemed relevant to the audit committee, including, but not limited to, whether the transaction is on terms no less favorable than terms generally available to an unaffiliated third party under the same or similar circumstances and the extent of the related party's interest in the transaction. All of the transactions described above were entered into prior to the adoption of this policy.

Stockholder Agreement

Our certificate of incorporation, bylaws and stockholder agreement between us and VantagePoint provide for a number of board of director, stockholder and related governance matters.

The following actions by us will require the approval of VantagePoint for so long as VantagePoint owns at least 25% or more of our outstanding shares of common stock: (i) any amendment of our bylaws; (ii) the issuance of any securities with economic rights senior to our common stock or with voting rights different than our common stock, subject to certain exceptions; (iii) the incurrence or guarantee of any debt in excess of \$20.0 million; (iv) the issuance of equity or debt, or any securities convertible into equity or debt, for consideration in excess of 12.5% of our market capitalization (as determined by the average trading price of our common stock over the 30 trading days prior to approval by our board of directors of such issuance); (v) the acquisition or disposition of stock or assets, including through a license or lease, for consideration in excess of 12.5% of our market capitalization (as determined by the average trading price of our common stock over the 30 trading days prior to approval by our board of directors of such transaction); (vi) the adoption of a stockholder rights plan; (vii) the approval of any golden parachute or other compensatory plan contingent upon a change in control of us for any of our executive officers valued in excess of \$1 million for an individual officer or \$5 million for a group of officers, at the time such compensatory arrangement is adopted; and (viii) any change in the number of authorized directors.

Amendments or modifications of our certificate of incorporation and bylaws relating to VantagePoint's rights can occur only with the approval of VantagePoint. VantagePoint and its representatives have access to our books and records, subject to customary confidentiality and non-disclosure provisions. So long as VantagePoint owns at least 40% of our outstanding voting stock, our stockholders may act by written consent to change the number of authorized directors, remove a director without cause or fill a vacancy on our board of directors (following this offering, VantagePoint will own approximately 34.5% of our outstanding common stock).

VantagePoint has the right to designate (and remove or replace) three members of our board of directors if VantagePoint owns at least 50% or more of our outstanding shares (following this offering, VantagePoint will own approximately 34.5% of our outstanding common stock). VantagePoint will continue to have a right to designate (and remove or replace) two members of our board of directors if VantagePoint owns between 20% and 50% of our outstanding shares and will have a right to designate (and remove or replace) one member of our board of directors if VantagePoint owns between 10% and 20% of our outstanding shares. VantagePoint also has the right to select one of its board designees to serve on our compensation committee, our nominating and corporate governance committee and any other special committee of our board of directors so long as it continues to hold at least 10% of our outstanding shares.

Table of Contents**Registration Rights**

Certain holders of common stock, including the following related persons, are entitled to certain registration rights with respect to the common stock they hold. See *Description of Capital Stock Registration Rights* for additional information.

Name of Stockholder	Shares of Registrable Securities
Funds managed by VantagePoint Capital Partners(1)	16,840,246
Funds managed by Advent International Corporation(2)	2,260,968
Camden Partners(3)	1,744,314
John W. Larson	93,493

- (1) Funds managed by VantagePoint Capital Partners holding our securities whose shares are aggregated for purposes of reporting share ownership information are VantagePoint Venture Partners IV (Q), L.P., VantagePoint Venture Partners IV, L.P. and VantagePoint Venture Partners IV Principals Fund, L.P.
- (2) Funds managed by Advent International Corporation holding our securities whose shares are aggregated for purposes of reporting share ownership information are Advent Partners II Limited Partnership, Advent Partners II-A Limited Partnership, Advent Partners DMC III Limited Partnership, Digital Media & Communications III Limited Partnership, Digital Media & Communications III-A Limited Partnership, Digital Media & Communications III-B Limited Partnership, Digital Media & Communications III-C Limited Partnership, Digital Media & Communications III-D C.V. and Digital Media & Communications III-E C.V.
- (3) Affiliates of Camden Partners holding our securities whose shares are aggregated for purposes of reporting share ownership information include Camden Partners Strategic Fund III, L.P. and Camden Partners Strategic Fund III-A, L.P.

Stock Option Grants

Certain stock option grants to, and related option grant policies regarding, our directors and officers are described in this prospectus under the caption *Management*.

Indemnification Agreements

We have entered, or will enter, into an indemnification agreement with each of our directors and officers. The indemnification agreements and our certificate of incorporation and bylaws require us to indemnify our directors and officers to the fullest extent permitted by Delaware law. See *Executive Compensation Limitation on Liability and Indemnification Matters*.

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PRINCIPAL AND SELLING STOCKHOLDERS

The following table sets forth information regarding the number of shares of common stock beneficially owned on June 30, 2012, immediately following consummation of this offering, by:

Each person who is known by us to beneficially own 5% or more of our common stock;

Each of our directors and named executive officers;

All of our directors and executive officers as a group; and

All selling stockholders.

We have determined beneficial ownership in accordance with SEC rules. Except as indicated by the footnotes below, we believe, based on the information furnished to us, that the persons and entities named in the table below have sole voting and investment power with respect to all shares of common stock that they beneficially own, subject to applicable community property laws.

Beneficial ownership Before the Offering is based on 26,713,354 shares of common stock outstanding at June 30, 2012, but does not reflect the exercise of any warrants or options to purchase common stock. Beneficial ownership After the Offering, assuming the underwriters' option to purchase is not exercised, is based on 28,051,920 shares of common stock outstanding at June 30, 2012, after giving effect to the sale and issuance of 1,000,000 shares of our common stock by us and the sale of 5,000,000 shares of our common stock that we expect to be sold in this offering by certain selling stockholders, including 338,566 shares of our common stock that we expect to be issued upon the exercise of outstanding warrants concurrently with the consummation of this offering. Beneficial ownership After the Offering, assuming the underwriters' option to purchase is exercised in full, gives effect to the sale of an additional 900,000 shares of our common stock that we expect to be sold in this offering by certain selling stockholders, including 31,313 shares of our common stock that we expect to be issued upon the exercise of outstanding warrants concurrently with the exercise of the underwriters' overallotment option. In computing the number of shares of common stock beneficially owned by a person and the percentage ownership of that person, we deemed to be outstanding all shares of common stock subject to options, warrants or other convertible securities held by that person or entity that are currently exercisable or exercisable within 60 days of June 30, 2012. We did not deem these shares outstanding, however, for the purpose of computing the percentage ownership of any other person. Beneficial ownership representing less than one percent is denoted with an *.

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Except as otherwise set forth below, the address of each of the persons listed below is 1100 Park Place, 4th Floor, San Mateo, California 94403.

Name and Address of	Before the Offering		After the Offering						
	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned	Number of Shares Being Offered	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned	Assuming the Underwriters Option to Purchase Is Not Exercised	Assuming the Underwriters Option to Purchase Is Exercised in Full Shares Offered Pursuant to the Underwriters Option Purchase	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned
Beneficial Owner									
Executive Officers and Directors:									
Joseph L. Jackson(1)	1,500,000	5.3%		1,500,000	5.1%			1,500,000	5.1%
Richard M. Berkeley(2)	1,893,496	7.0%	405,470	1,488,026	5.3%	75,311	1,412,715	5.0%	
Thomas A. Bevilacqua(3)	19,500	*		19,500	*		19,500	*	
Bruce G. Bodaken(4)	81,000	*		81,000	*		81,000	*	
Mariann Byerwalter(5)	38,000	*		38,000	*		38,000	*	
Jerome D. Gramaglia(6)	80,161	*		80,161	*		80,161	*	
John W. Larson(7)	201,889	*		201,889	*		201,889	*	
Edward C. Nafus(8)	48,000	*		48,000	*		48,000	*	
Richard T. Green(9)	307,500	1.1%		307,500	1.1%		307,500	1.1%	
Edgar O. Montes(10)	215,000	*		215,000	*		215,000	*	
Kimberly L. Jackson(11)	145,000	*		145,000	*		145,000	*	
All Executive Officers and Directors as a group (11 persons)(12)	4,529,546	15.3%	405,470	4,124,076	13.5%	75,311	4,048,765	13.3%	
5% Stockholders:									
Funds managed by VantagePoint Capital Partners(13)	17,133,660	56.6%	3,914,564	13,219,096	41.8%	727,072	12,492,024	39.5%	
Funds managed by Advent International Corporation(14)	2,305,530	8.5%	525,569	1,779,961	6.2%	97,617	1,682,344	5.9%	
Entities affiliated with Camden Partners(2)	1,893,496	7.0%	405,470	1,488,026	5.3%	75,311	1,412,715	5.0%	
Other Selling Stockholders:									
Caisse de dépôt et placement du Québec(15)	615,102	2.3%	135,605	479,497	1.7%		479,497	1.7%	
All Other Selling Stockholders (2 Selling Stockholders)(16)	92,238	*	18,792	73,446	*		73,446	*	

(1) Consists of options to purchase 1,500,000 shares of our common stock exercisable within 60 days as of June 30, 2012.

(2) Includes 288,221 shares held by Camden Partners Strategic Fund II-A, LP, 17,097 shares held by Camden Partners Strategic Fund II-B, LP, 1,133,687 shares held by Camden Partners Strategic Fund III, LP and 47,112 shares held by Camden Partners Strategic Fund III-A, LP. Also includes 355,121 shares subject to warrants held by Camden Partners Strategic Fund III, LP and 14,758 shares subject to warrants held by Camden Partners Strategic Fund III-A, LP that are exercisable within 60 days of June 30, 2012. Camden Partners Strategic Manager, LLC, or Camden Partners Strategic Manager, is the managing member of Camden Partners Strategic III, LLC, or Camden Partners Strategic III, which is the general partner of Camden Partners Strategic Fund III, L.P.

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- and Camden Partners Strategic Fund III-A, L.P., or the Camden Funds. Because Richard M. Berkeley, Don Hughes and David Warnock are the managing members of Camden Partners Strategic Manager, Camden Partners Strategic Manager is managing member of Camden Partners Strategic III and Camden Partners Strategic III is the general partner of the Camden Funds, Messrs. Berkeley, Hughes and Warnock may be deemed to have voting and dispositive power over the shares held by the Camden Funds. Also includes 37,500 shares subject to options held by Mr. Berkeley that are exercisable within 60 days of June 30, 2012. Mr. Berkeley has voting and investment power over the shares subject to options held by him. Mr. Berkeley disclaims beneficial ownership of the shares held by the Camden Funds except to the extent of his pecuniary interest therein. The address of Camden Funds, their affiliated entities and Mr. Berkeley is 500 East Pratt Street, Suite 1200, Baltimore, Maryland 21202. In connection with this offering, we expect the underwriters to purchase from certain of the Camden Funds warrants to purchase 338,566 shares of common stock at a price per share equal to the public offering price on the cover page of this prospectus, less \$1,550,633, the exercise price of such warrants, and the underwriting discounts and commissions for the underlying shares. If the underwriters exercise the overallotment option, we expect the underwriters to purchase from certain of the Camden Funds additional warrants to purchase 31,313 shares of common stock at a price per share equal to the public offering price on the cover page of this prospectus, less the exercise price of such warrants and the underwriting discounts and commissions per underlying shares. In each case, the underwriters will immediately exercise such warrants by paying us the aggregate exercise price of the warrants, and will include in the offering the shares of common stock issuable as a result of such exercises.
- (3) Includes 19,500 shares subject to options held by Mr. Bevilacqua that are exercisable within 60 days of June 30, 2012. VantagePoint Management, Inc. has the authority to direct the exercise of the options held by Mr. Bevilacqua. Mr. Bevilacqua disclaims beneficial ownership of the options and the shares underlying the options, except to the extent of his pecuniary interests in the shares. The address of Mr. Bevilacqua is 1001 Bayhill Drive, Suite 300, San Bruno, California 94066.
 - (4) Includes options to purchase 43,500 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (5) Consists of options to purchase 38,000 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (6) Includes options to purchase 43,500 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (7) Includes options to purchase 69,750 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (8) Includes options to purchase 38,000 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (9) Consists of options to purchase 307,500 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (10) Consists of options to purchase 215,000 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (11) Consists of options to purchase 145,000 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (12) Includes 369,879 shares subject to warrants that are exercisable within 60 days of June 30, 2012 and options to purchase 2,457,250 shares of our common stock exercisable within 60 days as of June 30, 2012.
 - (13) Includes 12,193,635 shares held by VantagePoint Venture Partners IV (Q), L.P., 1,227,870 shares held by VantagePoint Venture Partners IV, L.P., 150,649 shares held by VantagePoint Venture Partners IV Principals Fund, L.P., and 7,834 shares held by VantagePoint Venture Associates IV, L.L.C. Also includes 3,183,804 shares subject to warrants held by VantagePoint Venture Partners IV (Q), L.P., 318,731 shares subject to warrants held by VantagePoint Venture Partners IV, L.P. and 11,596 shares subject to warrants held by VantagePoint Venture Partners IV Principals Fund, L.P. that are exercisable within 60 days of June 30, 2012. VantagePoint Venture Associates IV, L.L.C. is the general partner of these VantagePoint limited partnerships and may be deemed to have beneficial ownership of these shares and warrants. Also includes 19,500 shares subject to options held by Mr. Bevilacqua, 7,583 shares subject to options held by Ms. Annette Bianchi, a former member of our board of directors, and 12,458 shares subject to options held

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- by J. Stephan Dolezalek that are exercisable within 60 days of June 30, 2012. VantagePoint Management, Inc. has the authority to direct the exercise of the options held by Mr. Bevilacqua, Ms. Bianchi and Mr. Dolezalek. Alan E. Salzman, CEO of VantagePoint Management, Inc. and Managing Member of VantagePoint Venture Associates IV, L.L.C., may be deemed to beneficially own the shares subject to these shares, warrants and options. Mr. Bevilacqua, Ms. Bianchi, and Mr. Dolezalek each disclaim beneficial ownership of all options or shares beneficially owned by entities affiliated with VantagePoint Capital Partners, except to the extent of their respective pecuniary interests therein. The address of VantagePoint Capital Partners, Mr. Bevilacqua, Ms. Bianchi, Mr. Dolezalek and Mr. Salzman is 1001 Bayhill Drive, Suite 300, San Bruno, California 94066.
- (14) Includes 25,184 shares held by Advent Partners DMC III Limited Partnership, 23,559 shares held by Advent Partners II-A Limited Partnership, 7,945 shares held by Advent Partners II Limited Partnership, 401,342 shares held by Digital Media & Communications III Limited Partnership, 194,222 shares held by Digital Media & Communications III-A Limited Partnership, 59,396 shares held by Digital Media & Communications III-B Limited Partnership, 886,344 shares held by Digital Media & Communications III-C Limited Partnership, 140,886 shares held by Digital Media & Communications III-D C.V. and 93,916 shares held by Digital Media & Communications III-E C.V. Also includes 6,496 shares subject to warrants held by Advent Partners DMC III Limited Partnership, 6,077 shares subject to warrants held by Advent Partners II-A Limited Partnership, 2,049 shares subject to warrants held by Advent Partners II Limited Partnership, 103,519 shares subject to warrants held by Digital Media & Communications III Limited Partnership, 50,096 shares subject to warrants held by Digital Media & Communications III-A Limited Partnership, 15,320 shares subject to warrants held by Digital Media & Communications III-B Limited Partnership, 228,616 shares subject to warrants held by Digital Media & Communications III-C Limited Partnership, 36,339 shares subject to warrants held by Digital Media & Communications III-D C.V., and 24,224 shares subject to warrants held by Digital Media & Communications III-E C.V. that are exercisable within 60 days of June 30, 2012. Advent International Corporation, the general partner of the above listed Funds has the sole ability to vote and dispose of these shares. The address for the funds managed by Advent International Corporation is 75 State Street, Boston, Massachusetts 02109.
- (15) The natural persons having voting control and dispositive power over the shares held by Caisse de dépôt et placement du Québec are comprised of an investment committee comprised of Normand Provost, Luc Houle, Robert Côté, Pierre Fortier, Marcel Gagnon, Cyrille Vittecoq and Frédéric Godbout. The address of Caisse de dépôt et placement du Québec is 1000 place Jean-Paul-Riopelle, Montreal, Quebec H2Z 2B3.
- (16) Represents shares held by two selling stockholders not listed above who, as a group, own less than 1% of our outstanding common stock prior to this offering.

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DESCRIPTION OF CAPITAL STOCK

General

The following is a summary of the rights of our common stock and preferred stock and certain provisions of our restated certificate of incorporation and amended and restated bylaws. For more detailed information, please see our amended and restated certificate of incorporation and amended and restated bylaws, which are filed as exhibits to the registration statement of which this prospectus is part.

Our authorized capital stock consists of 1,100,000,000 shares, with a par value of \$0.001 per share, of which:

1,000,000,000 shares are designated as common stock; and

100,000,000 shares are designated as preferred stock.

As of June 30, 2012, we had outstanding 26,713,354 shares of common stock, held of record by 109 stockholders. In addition, as of June 30, 2012, 5,242,621 shares of our common stock were subject to outstanding options, and warrants exercisable for up to an aggregate of 4,653,567 shares of our capital stock. For more information on our capitalization, see *Capitalization*.

Common Stock

Pursuant to our amended and restated certificate of incorporation, the holders of common stock are entitled to one vote per share on all matters submitted to a vote of stockholders. This amended and restated certificate of incorporation does not provide for cumulative voting in the election of directors. Subject to the rights, if any, of the holders of any outstanding series of preferred stock, the holders of common stock are entitled to receive ratably such dividends, if any, as may be declared by the board of directors out of legally available funds. However, the current policy of the board of directors is to retain earnings, if any, for operations and growth. Upon liquidation, dissolution or winding-up of our company, subject to rights, if any of the holders of our preferred stock, the holders of common stock are entitled to share ratably in all assets that are legally available for distribution. The holders of common stock have no preemptive, subscription, redemption or conversion rights. The rights, preferences and privileges of holders of common stock are subject to, and may be adversely affected by, the rights of the holders of any series of preferred stock, which may be designated solely by action of the board of directors and issued in the future.

Preferred Stock

The board of directors is authorized, subject to any limitations prescribed by law, without further vote or action by the stockholders, to issue from time-to-time shares of preferred stock in one or more series without stockholder approval. Each such series of preferred stock shall have such number of shares, designations, preferences, voting powers, qualifications, and special or relative rights or privileges as shall be determined by the board of directors, which may include, among others, dividend rights, voting rights, liquidation preferences, conversion rights and preemptive rights.

Warrants

At June 30, 2012, we had warrants outstanding to purchase 4,653,567 shares of our common stock at exercise prices ranging from \$4.58 to \$8.50 per share. Warrants to purchase 4,366,803 shares of common stock and 75,000 shares of common stock will terminate on June 30, 2014 and September 26, 2014, respectively. The warrant to purchase 211,764 shares of common stock will terminate on the date that is 18 months following the effective date of our initial public offering. Each warrant contains provisions for the adjustment of exercise price and the number of shares issuable upon exercise in the event of stock dividends, stock splits, reorganizations, and

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reclassifications, consolidations and the like. Each warrant holder, with the exception of the holder of the warrant to purchase 211,764 shares of common stock, was granted certain registration rights on the same terms as those held by preferred stockholders as described below.

In connection with this offering, we expect the underwriters to purchase from certain of the Camden Funds warrants to purchase 338,566 shares of common stock at a price per share equal to the public offering price on the cover page of this prospectus, less \$1,550,633, the exercise price of such warrants, and the underwriting discounts and commissions per underlying shares. If the underwriters exercise the overallotment option, we expect the underwriters to purchase from certain of the Camden Funds additional warrants to purchase 31,313 shares of common stock at a price per share equal to the public offering price on the cover page of this prospectus, less the exercise price of such warrants and the underwriting discounts and commissions for the underlying shares. In each case, the underwriters will immediately exercise such warrants by paying us the aggregate exercise price of the warrants, and will include in the offering the shares of common stock issuable as a result of such exercises.

Stockholder Agreement

We and VantagePoint entered into a stockholder agreement providing VantagePoint with the right to (i) designate (and remove or replace) up to three members of our board of directors, (ii) select one of its board designees to serve on our compensation committee, our nominating and corporate governance committee and any other special committee of our board of directors, (iii) approve certain corporate actions and certain amendments or modifications of our certificate of incorporation and bylaws and (iv) access our books and records, subject to customary confidentiality and non-disclosure provisions, all as described in more detail in the *Certain Relationships And Related Party Transactions* section above.

Registration Rights

Following this offering's completion, pursuant to the Amended and Restated Investors' Rights Agreement dated as of December 22, 2005, as amended, the holders of an aggregate of 17,240,809 shares of common stock (including shares issuable upon the exercise of all warrants) are entitled to rights with respect to the registration of these shares under the Securities Act of 1933, as amended. These rights include demand registration rights, short-form registration rights and piggyback registration rights. All fees, costs and expenses of underwritten registrations will be borne by us and all selling expenses, including underwriting discounts and selling commissions, will be borne by the holders of the shares being registered.

The registration rights terminate with respect to an individual holder after the date that is five years following the completion of our initial public offering or, with respect to the piggyback registration rights discussed below, at such time as the holders may sell all shares in any ninety day period under Rule 144.

Demand Registration Rights. Following this offering's completion, the holders of an aggregate of 17,054,415 shares of our common stock (including shares issuable upon the exercise of all warrants), or their permitted transferees, are currently entitled to demand registration rights. Under the terms of the investors' rights agreement, we will be required, at our expense, upon the written request of holders of a majority of these shares, to use our best efforts to register all or a portion of these shares for public resale. We are required to effect only two registrations pursuant to this provision of the investors' rights agreement. We are not required to effect a demand registration prior to 180 days after the effective date of this registration statement.

Short-Form Registration Rights. Following this offering's completion, the holders of an aggregate of 17,129,415 shares of our common stock (including shares issuable upon the exercise of all warrants), or their permitted transferees, are also currently entitled to short-form registration rights. If we are eligible to file a registration statement on Form S-3, these holders have the right, upon written request, to have such shares registered by us at our expense if the proposed aggregate offering price of the shares to be registered by the

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holders requesting registration, net of underwriting discounts and commissions, is at least \$2,000,000, subject to certain exceptions. We are required to effect only two registration statements on Form S-3 during a twelve month period.

Piggyback Registration Rights. Following this offering's completion, the holders of an aggregate of 17,240,809 shares of our common stock (including shares issuable upon the exercise of all warrants), or their permitted transferees, are currently entitled to piggyback registration rights. If we register any of our securities either for our own account or for the account of other security holders, the holders of these shares are entitled to include their shares in the registration at our expense. The underwriters of any underwritten offering have the right to limit the number of shares registered by these holders for marketing reasons, subject to certain limitations.

Anti-Takeover Effects of Delaware Law and Our Restated Certificate of Incorporation and Bylaws

Certain provisions of Delaware law and our amended and restated certificate of incorporation and bylaws contain provisions that could have the effect of delaying, deferring or discouraging another party from acquiring control of us. These provisions, which are summarized below, are expected to discourage certain types of coercive takeover practices and inadequate takeover bids. These provisions are also designed in part to encourage anyone seeking to acquire control of us to first negotiate with our board of directors. We believe that the advantages gained by protecting our ability to negotiate with any unsolicited and potentially unfriendly acquirer outweigh the disadvantages of discouraging such proposals, including those priced above the then-current market value of our common stock, because, among other reasons, the negotiation of such proposals could improve their terms.

Certificate of Incorporation and Bylaws. Our amended and restated certificate of incorporation and bylaws include provisions that:

authorize our board of directors to issue, without further action by the stockholders, up to 100,000,000 shares of undesignated preferred stock, which may contain voting, liquidation, dividend and other rights superior to our common stock;

limit the ability of stockholders to act by written consent to such periods during which VantagePoint Capital Partners and its affiliates hold 40% or more of our outstanding common stock;

limit the ability of our stockholders to call and bring business before special meetings of our stockholders;

establish an advance notice procedure for stockholder approvals to be brought before meetings of our stockholders, including proposed nominations of persons for election to our board of directors;

establish that our board of directors is divided into three classes, Class I, Class II and Class III, with each class serving staggered terms;

control the procedures for the conduct and scheduling of board of directors and stockholder meetings; and

provide the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

Delaware Anti-Takeover Statute. We are subject to the provisions of Section 203 of the Delaware General Corporation Law regulating corporate takeovers. In general, Section 203 prohibits a publicly-held Delaware corporation from engaging, under certain circumstances, in a business combination with an interested stockholder for a period of three years following the date the person became an interested stockholder unless:

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prior to the date of the transaction, the board of directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder;

upon completion of the transaction that resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the

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time the transaction commenced, excluding for purposes of determining the voting stock outstanding, but not the outstanding voting stock owned by the interested stockholder, (1) shares owned by persons who are directors and also officers, and (2) shares owned by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer; or

at or subsequent to the date of the transaction, the business combination is approved by the board of directors of the corporation and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least 66 2/3% of the outstanding voting stock which is not owned by the interested stockholder.

Generally, a business combination includes a merger, asset or stock sale, or other transaction resulting in a financial benefit to the interested stockholder. Generally, an interested stockholder is a person who, together with affiliates and associates, owns or, within three years prior to the determination of interested stockholder status, did own 15% or more of a corporation's outstanding voting stock. We expect the existence of this provision to have an anti-takeover effect with respect to transactions our board of directors does not approve in advance. We also anticipate that Section 203 may discourage business combinations or other attempts that might result in a premium over the market price for the shares of common stock held by our stockholders.

The provisions of Delaware law, our restated certificate of incorporation and our amended and restated bylaws could have the effect of discouraging others from attempting hostile takeovers and, as a consequence, they may also inhibit temporary fluctuations in the market price of our common stock that often result from actual or rumored hostile takeover attempts. These provisions may also have the effect of preventing changes in our management. It is possible that these provisions could make it more difficult to accomplish transactions that stockholders may otherwise deem to be in their best interests.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company, LLC. The transfer agent's address is 6201 15th Avenue, Brooklyn, New York 11219.

Listing

Our common stock is listed on the NYSE under the symbol WAGE.

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MATERIAL U.S. FEDERAL INCOME AND ESTATE TAX CONSIDERATIONS

FOR NON-U.S. HOLDERS

The following discussion is a summary of the material U.S. federal income and estate tax consequences of the ownership and disposition of our common stock by certain non-U.S. holders (as defined below). This discussion only applies to non-U.S. holders who purchase and hold our common stock as a capital asset for U.S. federal income tax purposes (generally property held for investment). This discussion does not describe all of the tax consequences that may be relevant to a non-U.S. holder in light of its particular circumstances.

For purposes of this discussion, a non-U.S. holder means a person that for U.S. federal income tax purposes is not a partnership (or entity treated as such for U.S. federal income tax purposes) and is not any of the following:

an individual citizen or resident of the United States;

a corporation (or any other entity treated as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;

an estate, the income of which is subject to U.S. federal income taxation regardless of its source; or

a trust, if it is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all substantial decisions of the trust, or if it has a valid election in effect under applicable Treasury regulations to be treated as a U.S. person.

This discussion is based on provisions of the Internal Revenue Code of 1986, as amended, or the Code, and Treasury regulations, administrative rulings and judicial decisions as of the date hereof. These authorities may change, perhaps retroactively, which could result in U.S. federal income and estate tax consequences different from those summarized below. No ruling has been or will be sought from the Internal Revenue Service, or the IRS, with respect to the matters discussed below, and there can be no assurance that the IRS will not take a contrary position regarding the tax consequences of the ownership or disposition of our common stock, or that any such contrary position would not be sustained by a court. This discussion does not address all aspects of U.S. federal income and estate tax law and does not describe any other U.S. federal, non-U.S., state, local or other tax considerations that may be relevant to non-U.S. holders in light of their particular circumstances. In addition, this discussion does not describe the U.S. federal income and estate tax consequences applicable to a non-U.S. holder who is subject to special treatment under U.S. federal income tax laws (including, without limitation, certain former citizens and former long-term residents, a controlled foreign corporation, a passive foreign investment company, a corporation that accumulates earnings to avoid U.S. federal income tax, a partnership or other entity treated as such for U.S. federal income tax purposes or an investor in any such entity, a tax-exempt organization, a bank or other financial institution, a broker, dealer or trader in securities, commodities or currencies, a person holding our common stock as part of a hedging, conversion, straddle, constructive sale or other risk reduction transaction or an insurance company). We cannot assure you that a change in law will not significantly alter the tax considerations that we describe in this discussion.

If a partnership (or any other entity treated as a partnership for U.S. federal income tax purposes) holds our common stock, the U.S. federal income tax treatment of a partner of that partnership will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our common stock, you should consult your tax advisors.

YOU SHOULD CONSULT YOUR OWN TAX ADVISOR REGARDING THE PARTICULAR U.S. FEDERAL, STATE AND LOCAL AND NON-U.S. INCOME AND OTHER TAX CONSEQUENCES TO YOU OF THE OWNERSHIP AND DISPOSITION OF OUR COMMON STOCK.

Distributions on Common Stock

As described in the section titled *Dividend Policy*, we currently do not anticipate paying dividends on our common stock in the foreseeable future. If, however, we make cash or other property distributions on our

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common stock, such distributions will be treated as dividends to the extent of our current and accumulated earnings and profits as determined for U.S. federal income tax purposes and will be subject to withholding as discussed below. Any portion of a distribution that exceeds our current and accumulated earnings and profits will first be applied to reduce the non-U.S. holder's basis in the common stock, but not below zero, and, to the extent such portion exceeds the non-U.S. holder's basis, the excess will be treated as gain from the disposition of stock, the tax treatment of which is discussed below under *Disposition of Common Stock*.

Dividends paid to a non-U.S. holder of our common stock generally will be subject to withholding of U.S. federal income tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. However, dividends that are effectively connected with the conduct of a trade or business by the non-U.S. holder within the United States (and, where an income tax treaty applies, are attributable to a permanent establishment maintained by the non-U.S. holder in the United States) are not subject to the withholding tax, provided that the non-U.S. holder furnishes to us or our paying agent a valid IRS Form W-8ECI (or other applicable form). Instead, such dividends are subject to U.S. federal income tax on a net income basis in the same manner as if the non-U.S. holder were a U.S. person as defined under the Code. Any such effectively connected dividends received by a non-U.S. holder that is a corporation may be subject to an additional branch profits tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty.

A non-U.S. holder of our common stock who wishes to claim the benefit of an applicable income tax treaty for dividends will be required to (a) furnish to us or our paying agent a valid IRS Form W-8BEN (or other applicable form) and certify under penalty of perjury that such holder is not a U.S. person as defined under the Code and is eligible for treaty benefits, or (b) if our common stock is held through certain foreign intermediaries, satisfy the relevant certification requirements of applicable Treasury regulations.

A non-U.S. holder of our common stock eligible for a reduced rate of U.S. withholding tax pursuant to an income tax treaty may obtain a refund of any excess amounts withheld by timely filing an appropriate claim for refund with the IRS.

Disposition of Common Stock

Any gain realized by a non-U.S. holder on the disposition of our common stock generally will not be subject to U.S. federal income or withholding tax unless:

the gain is effectively connected with a trade or business of the non-U.S. holder in the United States (and, if required by an applicable income tax treaty, is attributable to a permanent establishment maintained by the non-U.S. holder in the United States);

the non-U.S. holder is an individual who is present in the U.S. for 183 days or more in the calendar year of that disposition, and certain other conditions are met; or

we are or have been a U.S. real property holding corporation for U.S. federal income tax purposes, as such term is defined in section 897(c) of the Code during the shorter of the five-year period ending on the date of disposition or your holding period of our common stock. As long as our common stock is regularly traded on an established securities market, within the meaning of section 897(c)(3) of the Code, these rules will apply only if you actually or constructively hold more than five percent of such regularly traded common stock at any time during the applicable period that is specified in the Code. We believe we are not and do not expect to become a U.S. real property holding corporation.

A non-U.S. holder described in the first bullet point immediately above will be subject to tax on the net gain derived from the sale under regular graduated U.S. federal income tax rates, and if it is a corporation, may be subject to the branch profits tax equal to 30% of its effectively connected earnings and profits or at such lower rate as may be specified by an applicable income tax treaty.

An individual non-U.S. holder described in the second bullet point immediately above will be subject to a flat 30% tax on the gain derived from the sale (or such lower rate as specified by an applicable income tax

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treaty), which may be offset by U.S. source capital losses, even though the individual is not considered a resident of the United States, provided that the non-U.S. holder has timely filed U.S. federal income tax returns with respect to such losses.

A non-U.S. holder described in the third bullet point above will be subject to U.S. federal income tax under regular graduated U.S. federal income tax rates with respect to the gain recognized.

U.S. Federal Estate Tax

Our common stock beneficially owned by an individual who is not a citizen or resident of the United States (as defined for U.S. federal estate tax purposes) at the time of death will generally be includable in the decedent's gross estate for U.S. federal estate tax purposes, unless an applicable estate tax treaty provides otherwise.

Information Reporting and Backup Withholding

We must report annually to the IRS and to each non-U.S. holder the amount of dividends paid to such non-U.S. holder and the tax withheld with respect to such dividends, regardless of whether withholding was required. Copies of the information returns reporting such dividends and withholding may also be made available to the tax authorities in the country in which the non-U.S. holder resides under the provisions of an applicable income tax treaty or tax information exchange agreement.

A non-U.S. holder will be subject to backup withholding (currently at a rate of 28%, but scheduled to increase to 31% for taxable years beginning on or after January 1, 2013) for dividends paid to such non-U.S. holder unless such non-U.S. holder certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that such non-U.S. holder is a U.S. person as defined under the Code), or such non-U.S. holder otherwise establishes an exemption.

Information reporting and, depending on the circumstances, backup withholding will apply to the proceeds of a sale of our common stock within the U.S. or conducted through certain U.S.-related financial intermediaries, unless the beneficial owner certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that the beneficial owner is a U.S. person as defined under the Code), or such owner otherwise establishes an exemption.

Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules may be allowed as a refund or a credit against a non-U.S. holder's U.S. federal income tax liability provided the required information is timely furnished to the IRS.

Legislation Relating to Foreign Accounts

Legislation enacted in 2010 may impose withholding taxes on certain types of payments made to foreign financial institutions (as specially defined under those rules) and certain other non-U.S. entities if additional certification, information reporting and other specified requirements are not met. The legislation may impose a 30% withholding tax on dividends on, or gross proceeds from the sale or other disposition of, our common stock paid to a foreign financial institution or to a non-financial foreign entity, unless (i) the foreign financial institution undertakes certain diligence and reporting obligations, (ii) the non-financial foreign entity either certifies it does not have any substantial U.S. owners or furnishes identifying information regarding each substantial U.S. owner, or (iii) the foreign financial institution or non-financial foreign entity otherwise qualifies for an exemption from these rules. If the payee is a foreign financial institution and is subject to the diligence and reporting requirements in clause (i) above, it must enter into an agreement with the U.S. Treasury requiring, among other things, that it undertake to identify accounts held by certain U.S. persons or U.S.-owned foreign entities, annually report certain information about such accounts and withhold 30% on payments to non-compliant foreign financial institutions and certain other account holders.

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Although this legislation currently applies to applicable payments made after December 31, 2012, the IRS has recently issued proposed Treasury regulations that provide for a phased implementation of the withholding provisions described above. Withholding will generally apply to payments of dividends on our common stock made on or after January 1, 2014 and to payments of gross proceeds from a sale or other disposition of our common stock on or after January 1, 2015. Prospective investors should consult their tax advisors regarding the potential impact of these rules on their investment in our common stock.

The preceding discussion of U.S. federal tax considerations is for general information only. It is not tax advice. Each prospective investor should consult its own tax advisor regarding the particular U.S. federal, state and local and non-U.S. tax consequences of purchasing, owning and disposing of our common stock, including the consequences of any proposed change in applicable laws.

Table of Contents**SHARES ELIGIBLE FOR FUTURE SALE**

Future sales of substantial amounts of shares of our common stock, including shares issued upon the exercise of outstanding options and warrants, in the public market after this offering, or the possibility of these sales occurring, could cause the prevailing market price for our common stock to fall or impair our ability to raise equity capital in the future.

Upon the completion of this offering a total of 27,713,354 shares of common stock will be outstanding, assuming that there are no exercises of options or warrants after June 30, 2012. Of these shares, all shares of common stock sold in this offering by us and the selling stockholders, plus any shares sold upon exercise of the underwriters' option to purchase additional shares, and all 7,475,000 shares of common stock sold in our initial public offering will be freely tradable in the public market without restriction or further registration under the Securities Act, unless these shares are held by affiliates, as that term is defined in Rule 144 under the Securities Act of 1933, as amended, or the Securities Act.

The remaining 14,238,354 shares of common stock will be restricted securities, as that term is defined in Rule 144 under the Securities Act. These restricted securities are eligible for public sale only if they are registered under the Securities Act or if they qualify for an exemption from registration under Rules 144 or 701 under the Securities Act, which are summarized below.

Subject to the lock-up agreements described below and the provisions of Rules 144 and 701 under the Securities Act, these restricted securities will be available for sale in the public market as follows:

Date	Number of Shares
On the date of this prospectus	542,525
At various times beginning on November 6, 2012, the day after 180 days following the date of our initial public offering prospectus	883,290
At various times beginning more than 90 days after the date of this prospectus	12,812,539
In addition, of the 5,242,621 shares of our common stock that were subject to stock options outstanding as of June 30, 2012, options to purchase 3,649,303 shares of common stock were vested as of June 30, 2012 and will be eligible for sale following the effective date of this offering, subject to the lock-up agreements as described below.	

Rule 144

In general, under Rule 144, a person who is not our affiliate and has not been our affiliate at any time during the preceding three months will be entitled to sell any shares of our common stock that such person has beneficially owned for at least six months, including the holding period of any prior owner other than one of our affiliates, without regard to volume limitations. Sales of our common stock by any such person would be subject to the availability of current public information about us if the shares to be sold were beneficially owned by such person for less than one year.

In addition, under Rule 144, a person may sell shares of our common stock acquired from us immediately upon the closing of this offering, without regard to volume limitations or the availability of public information about us, if:

the person is not our affiliate and has not been our affiliate at any time during the preceding three months; and

the person has beneficially owned the shares to be sold for at least six months, including the holding period of any prior owner other than one of our affiliates.

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Our affiliates who have beneficially owned shares of our common stock for at least six months, including the holding period of any prior owner other than one of our affiliates, would be entitled to sell within any three-month period a number of shares that does not exceed the greater of:

1% of the number of shares of our common stock then-outstanding, which will equal approximately 277,133 shares immediately after this offering; and

the average weekly trading volume in our common stock on the NYSE during the four calendar weeks preceding the date of filing of a Notice of Proposed Sale of Securities Pursuant to Rule 144 with respect to the sale.

Sales under Rule 144 by our affiliates are also subject to manner of sale provisions and notice requirements and to the availability of current public information about us.

Rule 701

In general, under Rule 701 as currently in effect, any of our employees, consultants or advisors who purchase shares from us in connection with a compensatory stock or option plan or other written agreement in a transaction before the effective date of this offering that was completed in reliance on Rule 701 and complied with the requirements of Rule 701 will, subject to the lock-up restrictions described below, be eligible to resell such shares 90 days after the effective date of this offering in reliance on Rule 144, but without compliance with certain restrictions, including the holding period, contained in Rule 144.

Lock-Up Agreements

In connection with our initial public offering we and our officers, directors, and holders of substantially all of our common stock agreed with the underwriters, subject to certain exceptions, not to dispose of or hedge any of our common stock or securities convertible into or exchangeable for shares of common stock, file or cause to be filed a registration statement covering shares of common stock or any securities that are convertible into, exchangeable for, or represent the right to receive, common stock or any substantially similar securities, or publicly disclose the intention to do any of the foregoing restrictions, during the period from the date of our initial public offering prospectus continuing through the date 180 days after the date of our initial public offering prospectus, except with the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated. This agreement does not apply to the issuance by us of shares under any existing employee benefit plans. This agreement is subject to certain exceptions, and is also subject to extension for up to an additional 34 days, as set forth in *Underwriting*.

In connection with this offering, we, the selling stockholders and our officers and directors have agreed with the underwriters, subject to certain exceptions, not to dispose of or hedge any of our common stock or securities convertible into or exchangeable for shares of common stock, file or cause to be filed a registration statement covering shares of common stock or any securities that are convertible into, exchangeable for, or represent the right to receive, common stock or any substantially similar securities, or publicly disclose the intention to do any of the foregoing restrictions, during the period from the date of this prospectus continuing through the date 90 days after the date of this prospectus, except with the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated. This agreement does not apply to the issuance by us of shares under any existing employee benefit plans. This agreement is subject to certain exceptions, and is also subject to extension for up to an additional 34 days, as set forth in *Underwriting*.

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Registration Rights

Upon completion of this offering, the holders of 17,240,809 shares of common stock or their transferees (including shares issuable upon the exercise of all warrants) will be entitled to various rights with respect to the registration of these shares under the Securities Act. Registration of these shares under the Securities Act would result in these shares becoming fully tradable without restriction under the Securities Act immediately upon the effectiveness of the registration, except for shares purchased by affiliates. See *Description of Capital Stock Registration Rights* for additional information.

Registration Statements

On May 10, 2012, we filed a registration statement on Form S-8 under the Securities Act covering all of the shares of common stock subject to options outstanding or reserved for issuance under our stock plans. However, none of the shares registered on Form S-8 will be eligible for resale until the expiration of the lock-up agreements to which they are subject.

Table of Contents**UNDERWRITING**

The underwriters named below, for which William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated are acting as representatives, have severally agreed, subject to the terms and conditions set forth in the underwriting agreement by and among the underwriters, us and the selling stockholders to purchase from us and the selling stockholders, directly or through the exercise of warrants, the respective number of shares of common stock set forth opposite each underwriter's name in the table below.

Underwriter	Number of Shares
William Blair & Company, L.L.C.	2,400,000
Stifel, Nicolaus & Company, Incorporated	2,100,000
JMP Securities LLC	750,000
Needham & Company, LLC	750,000
 Total	 6,000,000

The underwriting agreement provides that the underwriters are obligated to purchase all the shares of common stock (directly or through the purchase and exercise of warrants) in the offering if any are purchased, other than those shares covered by the overallotment option described below. With respect to the shares of common stock obtained from the purchase and exercise of warrants, the underwriters will remit the exercise price of those warrants to us. The underwriting agreement also provides that if an underwriter defaults the purchase commitments of non-defaulting underwriters may be increased or the offering may be terminated.

Certain selling stockholders have granted to the underwriters a 30-day option to purchase on a pro rata basis up to 900,000 additional shares, including 31,313 shares of common stock to be issued upon the exercise of outstanding warrants, from them at the public offering price less the underwriting discounts and commissions. The option may be exercised only to cover any overallotments of common stock.

The underwriters propose to offer the shares of common stock initially at the public offering price on the cover page of this prospectus and to selling group members at that price less a selling concession of \$0.63 per share. After the offering the representatives may change the public offering price and concession.

The following table summarizes the compensation and estimated expenses we and the selling stockholders will pay:

	Per Share		Total	
	Without Overallotment	With Overallotment	Without Overallotment	With Overallotment
Underwriting Discounts and Commissions paid by us	\$ 1.05	\$ 1.05	\$ 1,050,000	\$ 1,050,000
Underwriting Discounts and Commissions paid by the selling stockholders	\$ 1.05	\$ 1.05	\$ 5,250,000	\$ 6,195,000
Expenses payable by us	\$ 0.68	\$ 0.68	\$ 684,248	\$ 684,248
Expenses payable by the selling stockholders	\$	\$	\$	\$

The representatives have informed us that they do not expect sales to accounts over which the underwriters have discretionary authority to exceed 5% of the shares of common stock being offered. The underwriters will not confirm sales to any accounts over which they exercise discretionary authority without first receiving a written consent from those accounts.

We have agreed that we will not offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, or file with the Securities and Exchange Commission a registration statement under the Securities Act of 1933, as amended, or the Securities Act, relating to, any shares of our common stock or securities convertible

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into or exchangeable or exercisable for any shares of our common stock, or publicly disclose the intention to make any offer, sale, pledge, disposition or filing, without the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated for a period of 90 days after the date of this prospectus, subject to certain exceptions, including a limited number of shares which may be issued by us in connection with acquisitions of other businesses. However, in the event that either (1) during the last 17 days of the lock-up period, we release earnings results or material news or a material event relating to us occurs or (2) prior to the expiration of the lock-up period, we announce that we will release earnings results during the 16-day period beginning on the last day of the lock-up period, then in either case the expiration of the lock-up will be extended until the expiration of the 18-day period beginning on the date of the release of the earnings results or the occurrence of the material news or event, as applicable, unless William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated waive, in writing, such an extension.

Our directors, executive officers and the selling stockholders have entered into lock-up agreements with the underwriters prior to the commencement of this offering pursuant to which each of these persons or entities, with limited exceptions, for a period of 90 days after the date of this prospectus, may not, without the prior written consent of William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated, on behalf of the underwriters (1) offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase, or otherwise transfer or dispose of, directly or indirectly, any shares of our common stock (including, without limitation, common stock which may be deemed to be beneficially owned by such directors, executive officers, managers and members in accordance with the rules and regulations of the SEC and securities which may be issued upon exercise of a stock option or warrant), enter into a transaction which would have the same effect or engage in any transaction that would require a filing pursuant to §13 or §16 of the Securities Exchange Act of 1934, as amended, or the Exchange Act, (2) enter into any swap, hedge or other arrangement that transfers, in whole or in part, any of the economic consequences of ownership of the common stock, whether any such transaction described in clause (1) or (2) above is to be settled by delivery of common stock or such other securities, in cash or otherwise, (3) publicly disclose the intention to make any such offer, sale, pledge or disposition, or to enter into any such transaction, swap, hedge or other arrangement, or (4) make any demand for or exercise any right with respect to the registration of any shares of our common stock or any security convertible into or exercisable or exchangeable for our common stock, in each case other than certain limited exceptions. Notwithstanding the foregoing, if (1) during the last 17 days of the 90-day restricted period, we issue an earnings release or material news or a material event relating to our company occurs or (2) prior to the expiration of the 90-day restricted period, we announce that we will release earnings results during the 16-day period beginning on the last day of the 90-day period, the restrictions described above shall continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or the occurrence of the material news or material event, unless William Blair & Company, L.L.C. and Stifel, Nicolaus & Company, Incorporated waive, in writing, such extension and, provided further, that such extension shall not apply only to the extent that FINRA has amended or repealed NASD Rule 2711(f)(4) or has otherwise provided interpretive guidance regarding such rule, in each case, so as to eliminate the prohibition of any broker, dealer, or member of a national securities association from publishing or distributing any research report, with respect to the securities of an emerging growth company (as defined in the Jumpstart our Business Startups Act of 2012) prior to or after the expiration of the lock-up agreement or has indicated that FINRA will not enforce such prohibition.

The warrants being purchased by the underwriters from certain selling stockholders will be purchased at a price per underlying share equal to the public offering price on the cover page of this prospectus less the exercise price of each such warrant and the underwriting discounts and commissions per underlying share. The underwriters will immediately exercise such warrants by paying us the aggregate exercise price of the warrants, and will include in the offering the 338,566 shares of common stock issuable as a result of such exercise.

We and the selling stockholders have agreed to indemnify the underwriters against liabilities under the Securities Act, or contribute to payments that the underwriters may be required to make in that respect.

The shares of our common stock are listed on the NYSE under the symbol WAGE.

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The underwriters and their respective affiliates are full service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. Certain of the underwriters and their respective affiliates have, from time-to-time, performed, and may in the future perform, various financial advisory, lending and investment banking services for us and our affiliates, for which they received or will receive customary fees and expenses. In the ordinary course of their various business activities, the underwriters and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers, and such investment and securities activities may involve securities and/or instruments of the issuer. The underwriters and their respective affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or instruments and may at any time hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

In connection with the offering, the underwriters may engage in stabilizing transactions, overallotment transactions, syndicate covering transactions, and penalty bids and passive market making in accordance with Regulation M under the Exchange Act.

Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum.

Overallotment involves sales by the underwriters of shares in excess of the number of shares the underwriters are obligated to purchase, which creates a syndicate short position. The short position may be either a covered short position or a naked short position. In a covered short position, the number of shares over-allotted by the underwriters is not greater than the number of shares that they may purchase in the overallotment option. In a naked short position, the number of shares involved is greater than the number of shares in the overallotment option. The underwriters may close out any covered short position by either exercising their overallotment option and/or purchasing shares in the open market.

Syndicate covering transactions involve purchases of the common stock in the open market after the distribution has been completed in order to cover syndicate short positions. In determining the source of shares to close out the short position, the underwriters will consider, among other things, the price of shares available for purchase in the open market as compared to the price at which they may purchase shares through the overallotment option. If the underwriters sell more shares than could be covered by the overallotment option, a naked short position, the position can only be closed out by buying shares in the open market. A naked short position is more likely to be created if the underwriters are concerned that there could be downward pressure on the price of the shares in the open market after pricing that could adversely affect investors who purchase in the offering.

Penalty bids permit the representatives to reclaim a selling concession from a syndicate member when the common stock originally sold by the syndicate member is purchased in a stabilizing or syndicate covering transaction to cover syndicate short positions.

In passive market making, market makers in the common stock who are underwriters or prospective underwriters may, subject to limitations, make bids for or purchases of our common stock until the time, if any, at which a stabilizing bid is made. These stabilizing transactions, syndicate covering transactions and penalty bids may have the effect of raising or maintaining the market price of our common stock or preventing or retarding a decline in the market price of the common stock. As a result the price of our common stock may be higher than the price that might otherwise exist in the open market. These transactions may be effected on the NYSE or otherwise and, if commenced, may be discontinued at any time.

A prospectus in electronic format may be made available on the websites maintained by one or more of the underwriters, or selling group members, if any, participating in this offering and one or more of the underwriters

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participating in this offering may distribute prospectuses electronically. The representatives may agree to allocate a number of shares to underwriters and selling group members for sale to their online brokerage account holders. Internet distributions will be allocated by the underwriters and selling group members that will make internet distributions on the same basis as other allocations.

The underwriters and their affiliates have provided certain commercial banking, financial advisory and investment banking services for us for which they receive fees. Affiliates of certain of the underwriters from time-to-time enter bids with respect to mortgage-backed security trades with us and the lowest bidder purchases those securities. The underwriters and their affiliates may from time-to-time in the future perform services for us and engage in other transactions with us.

The common stock is being offered for sale in those jurisdictions in the United States, the European Union and elsewhere where it is lawful to make such offers.

Each of the underwriters has represented and agreed that it has not offered, sold or delivered and will not offer, sell or deliver any of the shares of common stock directly or indirectly, or distribute this prospectus or any other offering material relating to the shares of common stock, in or from any jurisdiction except under circumstances that will result in compliance with the applicable laws and regulations thereof and that will not impose any obligations on us except as set forth in the underwriting agreement.

Notice to prospective investors in the European Economic Area

In relation to each Member State of the European Economic Area (the "EEA") which has implemented the Prospectus Directive (each, a "Relevant Member State") an offer to the public of any shares of common stock which are the subject of the offering contemplated by this prospectus may not be made in that Relevant Member State, except that an offer to the public in that Relevant Member State of any shares of common stock may be made at any time under the following exemptions under the Prospectus Directive, if they have been implemented in that Relevant Member State:

- (a) to legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;
- (b) to any legal entity which has two or more of: (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than 43,000,000; and (3) an annual net turnover of more than 50,000,000, as shown in its last annual or consolidated accounts;
- (c) by the underwriters to fewer than 100 natural or legal persons (other than "qualified investors" as defined in the Prospectus Directive) subject to obtaining the prior consent of the representatives for any such offer; or
- (d) in any other circumstances falling within Article 3(2) of the Prospectus Directive;

provided that no such offer of shares of common stock shall result in a requirement for the publication by us or any representative of a prospectus pursuant to Article 3 of the Prospectus Directive.

Any person making or intending to make any offer of shares of common stock within the EEA should only do so in circumstances in which no obligation arises for us or any of the underwriters to produce a prospectus for such offer. Neither we nor the underwriters have authorized, nor do they authorize, the making of any offer of shares of common stock through any financial intermediary, other than offers made by the underwriters which constitute the final offering of shares contemplated in this prospectus.

For the purposes of this provision, and your representation below, the expression an "offer to the public" in relation to any shares of common stock in any Relevant Member State means the communication in any form and

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by any means of sufficient information on the terms of the offer and any shares of common stock to be offered so as to enable an investor to decide to purchase any shares of common stock, as the same may be varied in that Relevant Member State by any measure implementing the Prospectus Directive in that Relevant Member State and the expression Prospectus Directive means Directive 2003/71/EC and includes any relevant implementing measure in each Relevant Member State.

Each person in a Relevant Member State who receives any communication in respect of, or who acquires any shares of common stock under, the offer of shares of common stock contemplated by this prospectus will be deemed to have represented, warranted and agreed to and with us and each underwriter that:

(a) it is a qualified investor within the meaning of the law in that Relevant Member State implementing Article 2(1)(e) of the Prospectus Directive; and

(b) in the case of any shares of common stock acquired by it as a financial intermediary, as that term is used in Article 3(2) of the Prospectus Directive, (i) the shares of common stock acquired by it in the offering have not been acquired on behalf of, nor have they been acquired with a view to their offer or resale to, persons in any Relevant Member State other than qualified investors (as defined in the Prospectus Directive), or in circumstances in which the prior consent of the representatives has been given to the offer or resale, or (ii) where shares of common stock have been acquired by it on behalf of persons in any Relevant Member State other than qualified investors, the offer of those shares of common stock to it is not treated under the Prospectus Directive as having been made to such persons.

Notice to prospective investors in the United Kingdom

Each of the underwriters severally represents, warrants and agrees as follows:

(a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000, or the FSMA) to persons who have professional experience in matters relating to investments falling with Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 or in circumstances in which section 21 of FSMA does not apply to us; and

(b) it has complied with, and will comply with all applicable provisions of FSMA with respect to anything done by it in relation to the shares of common stock in, from or otherwise involving the United Kingdom.

Notice to prospective investors in Japan

The shares of common stock have not been and will not be registered under the Financial Instruments and Exchange Law of Japan (the Financial Instruments and Exchange Law) and each underwriter has agreed that it will not offer or sell any shares of common stock, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Financial Instruments and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

Notice to prospective investors in Hong Kong

The shares of common stock may not be offered or sold by means of any document other than (i) in

circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance

(Cap. 32, Laws of Hong Kong), or (ii) to professional investors within the meaning of the Securities and

Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances

which do not result in the document being a prospectus within the meaning of the Companies Ordinance

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(Cap. 32, Laws of Hong Kong) and no advertisement, invitation or document relating to the shares of common stock may be issued or may be in the possession of any person for the purpose of the issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to

shares of common stock which are or are intended to be disposed of only to persons outside Hong Kong or only

to professional investors within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) or any rules made thereunder.

Notice to prospective investors in Singapore

This prospectus has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the shares of common stock may not be circulated or distributed, nor may the shares of common stock be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the SFA), (ii) to a relevant person, or any person pursuant to Section 275 (1A), and in accordance with the conditions, specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares of common stock are subscribed or purchased under Section 275 by a relevant person which is: (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (b) a trust (where the trustee is not an accredited investor) whose sole whole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest in that trust shall not be transferable for six months after that corporation or that trust has acquired the shares under Section 275 except: (i) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (ii) where no consideration is given for the transfer; or (iii) by operation of law.

By accepting this prospectus, the recipient hereof represents and warrants that he is entitled to receive it in accordance with the restrictions set forth above and agrees to be bound by limitations contained herein. Any failure to comply with these limitations may constitute a violation of law.

Notice to prospective investors in Germany

Each person who is in possession of this prospectus is aware of the fact that no German sales prospectus (Verkaufsprospekt) within the meaning of the Securities Sales Prospectus Act, Wertpapier-Verkaufsprospektgesetz, or the Act, of the Federal Republic of Germany has been or will be published with respect to our common stock. In particular, each underwriter has represented that it has not engaged and has agreed that it will not engage in a public offering in (offentliches Angebot) within the meaning of the Act with respect to any of our common stock otherwise than in accordance with the Act and all other applicable legal and regulatory requirements.

Notice to prospective investors in France

The shares of common stock are being issued and sold outside the Republic of France and that, in connection with their initial distribution, it has not offered or sold and will not offer or sell, directly or indirectly, any shares of common stock to the public in the Republic of France, and that it has not distributed and will not distribute or cause to be distributed to the public in the Republic of France this prospectus or any other offering material relating to the shares of common stock, and that such offers, sales and distributions have been and will

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be made in the Republic of France only to qualified investors (investisseurs qualifiés) in accordance with Article L.411-2 of the Monetary and Financial Code and décret no. 98-880 dated 1st October, 1998.

Notice to prospective investors in The Netherlands

Our common stock may not be offered, sold, transferred or delivered in or from The Netherlands as part of their initial distribution or at any time thereafter, directly or indirectly, other than to, individuals or legal entities situated in The Netherlands who or which trade or invest in securities in the conduct of a business or profession (which includes banks, securities intermediaries (including dealers and brokers), insurance companies, pension funds, collective investment institution, central governments, large international and supranational organizations, other institutional investors and other parties, including treasury departments of commercial enterprises, which as an ancillary activity regularly invest in securities) (hereinafter, the Professional Investors), provided that in the offer, prospectus and in any other documents or advertisements in which a forthcoming offering of our common stock is publicly announced (whether electronically or otherwise) in The Netherlands it is stated that such offer is and will be exclusively made to such Professional Investors. Individual or legal entities who are not Professional Investors may not participate in the offering of our common stock, and this prospectus or any other offering material relating to our common stock may not be considered an offer or the prospect of an offer to sell or exchange our common stock.

Notice to prospective investors in Italy

No prospectus has or will be registered in the Republic of Italy with the Italian Stock Exchange Commission (Commissione Nazionale per le Società di Borsa), or Consob, pursuant to the Prospectus Directive and Italian laws and regulations on financial products. Accordingly, the common stock may not be offered, sold or delivered in the Republic of Italy, and copies of this prospectus or any other document relating to the common stock may not be distributed in the Republic of Italy, except to (a) qualified investors (investori qualificati), or the Qualified Investors, pursuant to Article 100 of Legislative Decree no. 58 dated February 24, 1998, as amended, or the Financial Act, as defined in Article 34-ter of Consob Regulation no. 11971 dated May 14, 1999, as amended, Regulation no. 11971; or (b) in circumstances where there is an exemption from the rules governing an offer to the public of financial products pursuant to Article 94 et seq. of the Financial Act, and to Regulation no. 11971. Any offer, sale or delivery of the common stock in the Republic of Italy must be (a) made by an investment firm, a bank or financial intermediary authorized to engage in such activities in Italy, in compliance with the Financial Act and with Legislative Decree no. 385 dated September 1, 1993, as amended and Consob Regulation no. 16190 dated October 29, 2007, as amended, and any other applicable law and regulation, and (b) in compliance with any applicable Italian laws and regulations and any other condition or limitation that may be imposed by Consob, the Bank of Italy (Banca d Italia) and any other relevant Italian authorities.

Notice to prospective investors in Switzerland

This document, as well as any other material relating to the shares of common stock which are the subject of the offering contemplated by this prospectus, do not constitute an issue prospectus pursuant to Article 652a of the Swiss Code of Obligations. The shares of common stock will not be listed on the SWX Swiss Exchange and, therefore, the documents relating to the shares of common stock, including, but not limited to, this document, do not claim to comply with the disclosure standards of the listing rules of SWX Swiss Exchange and corresponding prospectus schemes annexed to the listing rules of the SWX Swiss Exchange. The shares of common stock are being offered in Switzerland by way of a private placement, i.e., to a small number of selected investors only, without any public offer and only to investors who do not purchase the shares of common stock with the intention to distribute them to the public. The investors will be individually approached by us from time to time. This document, as well as any other material relating to the shares of common stock, is personal and confidential and do not constitute an offer to any other person. This document may only be used by those investors to whom it has been handed out in connection with the offering described herein and may neither directly nor indirectly be distributed or made available to other persons without our express consent. It may not be used in connection with any other offer and shall in particular not be copied and/or distributed to the public in (or from) Switzerland.

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LEGAL MATTERS

The validity of the shares of common stock offered hereby will be passed upon for us by Wilson Sonsini Goodrich & Rosati, Professional Corporation, Palo Alto, California. Latham & Watkins LLP, Menlo Park, California is representing the underwriters in this offering. Certain members of, and investment partnerships comprised of members of, and persons associated with, Wilson Sonsini Goodrich & Rosati own an interest representing less than 0.1% of our common stock.

EXPERTS

The consolidated financial statements of WageWorks, Inc. and subsidiaries as of December 31, 2010 and 2011, and for each of the years in the three-year period ended December 31, 2011, have been included herein in reliance upon the reports of KPMG LLP, independent registered public accounting firm, appearing elsewhere herein, and upon the authority of said firm as experts in accounting and auditing.

The statements of revenue and direct expenses of FBMC Tax Favored Accounts Division, a division of Fringe Benefits Management Company, Inc., for the year ended December 31, 2009 and the eleven months ended November 30, 2010, have been included herein in reliance upon the report of Mayer Hoffman McCann P.C., independent public accounting firm, appearing elsewhere herein, and upon the authority of said firm as experts in accounting and auditing.

The balance sheets of TransitCenter, Inc. as of December 31, 2011 and 2010 and the related statements of activities and cash flows for each of the years in the two-year period ended December 31, 2011 have been audited by EisnerAmper LLP, an independent registered public accounting firm, as stated in their report which is included herein. Such financial statements have been included herein in reliance on the report of such firm given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed with the SEC a registration statement on Form S-1 under the Securities Act of 1933, as amended, with respect to the shares of common stock offered hereby. This prospectus, which constitutes a part of the registration statement, does not contain all of the information set forth in the registration statement or the exhibits and schedules filed therewith. For further information about us and the common stock offered hereby, we refer you to the registration statement and the exhibits and schedules filed thereto. Statements contained in this prospectus regarding the contents of any contract or any other document that is filed as an exhibit to the registration statement are not necessarily complete, and each such statement is qualified in all respects by reference to the full text of such contract or other document filed as an exhibit to the registration statement.

We are subject to the information and reporting requirements of the Exchange Act and, in accordance with this law, are required to file periodic reports, proxy statements and other information with the SEC. You may read and copy this information at the Public Reference Room of the SEC, 100 F Street, N.E., Room 1580, Washington D.C. 20549. You may obtain information on the operation of the public reference rooms by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet website that contains reports, proxy statements and other information about issuers, like us, that file electronically with the SEC. The address of that site is www.sec.gov. We also maintain a website at <http://www.wageworks.com>. You may access our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act with the SEC free of charge at our website as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. The information contained in, or that can be accessed through, our website is not part of this prospectus.

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Report of Independent Registered Public Accounting Firm

The Board of Directors

WageWorks, Inc.:

We have audited the accompanying consolidated balance sheets of WageWorks, Inc. and subsidiaries (the Company) as of December 31, 2010 and 2011, and the related consolidated statements of operations, stockholders' deficit, and cash flows for each of the years in the three-year period ended December 31, 2011. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of WageWorks, Inc. and subsidiaries as of December 31, 2010 and 2011, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2011, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

San Francisco, California

March 6, 2012, except for Note 16, as to which the date is September 25, 2012

Table of Contents**WAGWORKS, INC.****Consolidated Balance Sheets****(In thousands, except per share amounts)**

	December 31, 2010	2011	June 30, 2012 (unaudited)
Assets			
Current assets:			
Cash and cash equivalents	\$ 104,280	\$ 154,621	\$ 261,340
Restricted cash, current portion	3,575	2,383	2,363
Accounts receivable, less allowance for doubtful accounts of \$415 and \$69 at December 31, 2010 and 2011, and \$197 at June 30, 2012 (unaudited), respectively	14,591	15,647	18,026
Prepaid expenses and other current assets	1,891	7,178	13,001
Total current assets	124,337	179,829	294,730
Restricted cash, net of current portion		2,526	2,432
Property and equipment, net	18,693	19,014	23,157
Goodwill	46,806	46,233	75,822
Acquired intangible assets, net	15,230	12,555	34,535
Deferred tax asset		16,978	9,762
Other assets	1,765	1,561	1,763
Total assets	\$ 206,831	\$ 278,696	\$ 442,201
Liabilities, Redeemable Convertible Preferred Stock, and Stockholders Equity (Deficit)			
Current liabilities:			
Accounts payable and accrued expenses	\$ 20,900	\$ 21,415	\$ 35,371
Customer obligations	137,458	169,959	212,834
Short-term contingent payment	8,982	8,976	14,269
Short-term debt		14,901	44,560
Other current liabilities	308	394	972
Total current liabilities	167,648	215,645	308,006
Long-term debt	2,837		
Warrants	1,470	1,119	
Long-term contingent payment	6,952		6,805
Other noncurrent liabilities	3,347	1,820	2,619
Total liabilities	182,254	218,584	317,430
Redeemable convertible preferred stock:			
Redeemable convertible preferred stock, Series C (\$24,999 liquidation preference). Authorized 6,306 shares; issued and outstanding 5,882 shares at December 31, 2010 and 2011 and no shares outstanding at June 30, 2012 (unaudited), respectively	34,807	36,570	
Redeemable convertible preferred stock, Series D (\$15,998 liquidation preference). Authorized 2,465 shares; issued and outstanding 2,465 shares at December 31, 2010 and 2011 and no shares outstanding at June 30, 2012 (unaudited), respectively	17,947	17,771	
Redeemable convertible preferred stock, Series E (\$21,179 liquidation preference). Authorized 5,295 shares; issued and outstanding 5,295 shares at December 31, 2010 and 2011 and no shares outstanding at June 30, 2012 (unaudited), respectively	23,206	27,828	
Total redeemable convertible preferred stock	75,960	82,169	
Stockholders equity (deficit):	33,965	33,965	

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Convertible preferred stock, \$0.001 par value (\$31,916 liquidation preference). Authorized 26,392 shares, outstanding 17,645 shares at December 31, 2010 and 2011 and no shares outstanding at June 30, 2012 (unaudited), respectively

Common stock, \$0.001 par value. Authorized 1,000,000 shares; issued 1,718 shares and 1,738 shares at December 31, 2010 and 2011, and 26,909 shares at June 30, 2012 (unaudited), respectively

Treasury stock at cost 187 shares at December 31, 2010 and 192 shares at December 31, 2011 and 195 shares at June 30, 2012 (unaudited), respectively

Additional paid-in capital

Accumulated deficit

Total stockholders' equity (deficit)

Total liabilities, redeemable convertible preferred stock, and stockholders' equity (deficit)

	2	2	27
	(376)	(433)	(463)
	22,967	19,029	194,593
	(107,941)	(74,620)	(69,386)
	(51,383)	(22,057)	124,771
	\$ 206,831	\$ 278,696	\$ 442,201

See accompanying notes to consolidated financial statements.

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Table of Contents**WAGeworks, INC.****Consolidated Statements of Operations****(In thousands, except per share amounts)**

	Year Ended December 31,			Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2010	2011	2011 (unaudited)	2012 (unaudited)	2011 (unaudited)	2012 (unaudited)
Revenues:							
Healthcare	\$ 70,718	\$ 75,771	\$ 90,917	\$ 22,854	\$ 27,615	\$ 47,079	\$ 56,845
Commuter	27,603	29,304	33,325	8,382	13,220	16,589	25,212
Other	10,140	9,972	11,395	2,625	2,942	5,517	6,030
Total revenues	108,461	115,047	135,637	33,861	43,777	69,185	88,087
Operating expenses:							
Cost of revenues (excluding amortization of internal use software)	46,802	50,205	55,651	13,244	15,620	28,610	32,677
Technology and development	13,773	12,640	13,526	3,447	4,622	6,939	8,962
Sales and marketing	18,885	18,173	20,697	5,209	7,267	10,458	14,476
General and administration	20,134	18,231	20,876	5,104	7,325	10,466	14,803
Amortization and change in contingent consideration	8,398	7,764	11,327	2,682	4,094	5,175	8,532
Total operating expenses	107,992	107,013	122,077	29,686	38,928	61,648	79,450
Income from operations	469	8,034	13,560	4,175	4,849	7,537	8,637
Other income (expense):							
Interest income	851	220	36	9	9	20	19
Interest expense	(1,102)	(188)	(494)	(111)	(452)	(197)	(857)
Interest expense: amortization of convertible debt discount	(71)	(21,107)					
Loss on extinguishment of debt	(356)						
Gain (loss) on revaluation of warrants	70	(5,413)	351	51	407	(59)	381
Other income					12		27
Income (loss) before income taxes	(139)	(18,454)	13,453	4,124	4,825	7,301	8,207
Income tax (provision) benefit	(495)	1,204	19,868	(253)	(1,601)	(401)	(2,973)
Net income (loss)	(634)	(17,250)	33,321	3,871	3,224	6,900	5,234
Accretion of redemption premium (expense) benefit	1,037	(6,740)	(6,209)	(2,924)	(778)	(5,692)	(2,301)
Net income (loss) attributable to common stockholders	\$ 403	\$ (23,990)	\$ 27,112	\$ 947	\$ 2,446	\$ 1,208	\$ 2,933
Basic net income (loss) per share attributable to common stockholders	\$ 0.25	\$ (15.70)	\$ 17.65	\$ 0.62	\$ 0.17	\$ 0.79	\$ 0.37
Diluted net income (loss) per share attributable to common stockholders	\$ (0.04)	\$ (15.70)	\$ 1.43	\$ 0.06	\$ 0.10	\$ 0.07	\$ 0.13
Shares used in basic net income (loss) per share calculations	1,606	1,528	1,536	1,535	14,268	1,534	7,907
	16,864	1,528	20,086	16,450	24,349	16,376	20,683

Shares used in diluted net income (loss)
per share calculations

See accompanying notes to consolidated financial statements.

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Table of Contents**WAGWORKS, INC.****Consolidated Statements of Stockholders Equity (Deficit)**

(In thousands)

	Convertible Preferred Stock		Common Stock		Treasury Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders Equity (Deficit)
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance at December 31, 2008	17,645	\$ 33,965	1,676	\$ 2	(1)	\$ (5)	\$ (1,262)	\$ (90,057)	\$ (57,357)
Exercise of stock options			36				20		20
Share repurchases					(186)	(371)			(371)
Stock-based compensation							2,510		2,510
Beneficial conversion feature							10,800		10,800
Accretion of redemption premium							1,037		1,037
Net loss								(634)	(634)
Balance at December 31, 2009	17,645	33,965	1,712	2	(187)	(376)	13,105	(90,691)	(43,995)
Exercise of stock options			6				5		5
Stock-based compensation							2,404		2,404
Modification of warrants							14,193		14,193
Accretion of redemption premium							(6,740)		(6,740)
Net loss								(17,250)	(17,250)
Balance at December 31, 2010	17,645	33,965	1,718	2	(187)	(376)	22,967	(107,941)	(51,383)
Exercise of stock options			20				27		27
Share repurchases					(5)	(57)			(57)
Stock-based compensation							2,244		2,244
Accretion of redemption premium							(6,209)		(6,209)
Net income								33,321	33,321
Balance at December 31, 2011	17,645	33,965	1,738	2	(192)	(433)	19,029	(74,620)	(22,057)
Issuance of common stock in May 2012 initial public offering at \$9.00 per share, net of issuance costs of \$10,239			7,475	7			57,029		57,036
Conversion of preferred stock to common stock	(17,645)	(33,965)	17,688	18			118,416		84,469
Conversion of preferred stock warrants to common stock							738		738
Exercise of stock options			8				8		8
Share repurchases					(3)	(30)			(30)
Stock-based compensation							1,674		1,674
Accretion of redemption premium							(2,301)		(2,301)
Net income								5,234	5,234
Balance at June 30, 2012 (unaudited)		\$	26,909	\$ 27	(195)	\$ (463)	\$ 194,593	\$ (69,386)	\$ 124,771

See accompanying notes to consolidated financial statements.

Table of Contents**WAGWORKS, INC.****Consolidated Statements of Cash Flows****(In thousands)**

	Year Ended December 31,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012
				(unaudited)	
Cash flows from operating activities:					
Net income (loss)	\$ (634)	\$ (17,250)	\$ 33,321	\$ 6,900	\$ 5,234
Adjustments to reconcile net income (loss) to net cash provided by operating activities:					
Depreciation	4,564	4,164	3,199	1,744	1,446
Amortization and change in contingent consideration	8,398	7,764	11,327	5,175	8,532
Stock-based compensation	2,510	2,404	2,244	1,199	1,674
Revaluation of warrants	(70)	5,413	(351)	59	(381)
Loss on extinguishment of debt	183				
Amortization of debt discount	272	21,107			
Loss on disposal of fixed assets	23		51	6	24
Payment of contingent consideration in excess of initial measurement			(662)		(2,453)
Loss on impairment of long-lived assets	345	120	116		
Provision for doubtful accounts	(224)	66	61	126	13
Deferred taxes	446	(1,334)	(20,198)	195	2,527
Changes in operating assets and liabilities:					
Accounts receivable	2,394	(2,109)	475	(4,108)	(1,343)
Prepaid expenses and other current assets	448	(324)	(3,996)	(3,263)	(2,514)
Other assets	980	(303)	204	124	8
Accounts payable and accrued expenses	(418)	344	(29)	(1,876)	(159)
Customer obligations	12,942	1,522	28,917	12,246	2,160
Other liabilities	(1,084)	(1,108)	510	(14)	833
Net cash provided by operating activities	31,075	20,476	55,189	18,513	15,601
Cash flows used in investing activities:					
Purchases of property and equipment	(6,617)	(7,257)	(9,408)	(4,057)	(6,403)
Cash consideration for business acquisitions, net of cash acquired	(2,069)	(5,012)	(1,852)	(1,852)	8,551
Change in restricted cash	(567)	(30)	(1,334)	(200)	574
Net cash (used in) provided by investing activities	(9,253)	(12,299)	(12,594)	(6,109)	2,722
Cash flows from financing activities:					
Proceeds from convertible debt	20,000				
Proceeds from debt		2,837	12,064	9,219	29,659
Repayment of outstanding debt facilities	(20,000)				
Proceeds from initial public offering net of underwriters commissions and discounts					62,566
Principal payments on capital leases	(312)				
Proceeds from exercise of common stock	20	5	27	37	8
Payment of contingent consideration			(4,288)	(2,000)	(3,807)
Purchase of treasury stock	(371)		(57)	(21)	(30)
Net cash (used in) provided by financing activities	(663)	2,842	7,746	7,235	88,396
Net increase in cash and cash equivalents	21,159	11,019	50,341	19,639	106,719
Cash and cash equivalents at beginning of period	72,102	93,261	104,280	104,280	154,621
Cash and cash equivalents at end of period	\$ 93,261	\$ 104,280	\$ 154,621	\$ 123,919	\$ 261,340

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Supplemental cash flow disclosure:

Cash paid during the period for:

Interest	\$ 1,083	\$ 189	\$ 368	\$ 127	\$ 464
Taxes	149	383	442	48	486

Noncash financing and investing activities:

Conversion of convertible debt and accrued interest into Series E preferred stock		21,178			
Accretion of redemption premium	(1,037)	6,740	6,209	5,692	2,301
Reduction in FBM contingent consideration due to re-negotiated lease					528
Conversion of preferred stock to common stock					118,416
Conversion of preferred stock warrants to common stock warrants					738
PBS acquisition adjustment			590		
Modification of warrants		14,193			
Beneficial conversion feature	10,800				

See accompanying notes to consolidated financial statements.

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WAGWORKS, INC.

Notes to Consolidated Financial Statements

(1) Summary of Business and Significant Accounting Policies

(a) Business

WageWorks, Inc., or the Company, is a leading on-demand provider of tax-advantaged programs for consumer-directed health, commuter and other employee spending account benefits, or CDBs, in the United States. The Company is headquartered in San Mateo, California.

The Company operates as a single reportable segment on an entity level basis. The Company generates revenue from the administration of healthcare, commuter and other employer sponsored tax-advantaged benefit services. The entity level is the aggregation of these three revenue streams.

(b) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. Acquisitions are accounted for as business combinations, and accordingly, the results of operations of acquired businesses are included in the consolidated financial statements from the date of acquisition. All significant intercompany accounts and transactions have been eliminated in consolidation.

(c) Unaudited Interim Financial Statements

The accompanying interim consolidated balance sheet as of June 30, 2012, the consolidated statements of operations for the three and six months ended June 30, 2011 and June 30, 2012, the consolidated statements of cash flows for the six months ended June 30, 2011 and June 30, 2012, the consolidated statement of stockholders' deficit for the six months ended June 30, 2012 and the related interim information contained within the notes to the consolidated financial statements are unaudited. These unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America. In our opinion, the unaudited interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for fair presentation. The results of the interim period presented herein are not necessarily indicative of the results of future periods or annual results for the year ended December 31, 2012.

(d) Initial Public Offering (unaudited)

On May 15, 2012, the Company closed its initial public offering (IPO). The offer and sale of all of the shares in the IPO were registered under the Securities Act pursuant to a registration statement on Form S-1, which was declared effective by the SEC on May 9, 2012 (the Effective Date). In connection with the IPO the Company sold 7,475,000 shares of common stock to the public at a price of \$9.00 per share, which included 975,000 shares of common stock from the full exercise of the over-allotment option of shares granted to the underwriters. The Company received aggregate proceeds of \$62.6 million from the IPO and the underwriters' over-allotment option, net of underwriters' discounts and commissions. Upon the closing of the IPO, all shares of the Company's previously outstanding preferred stock automatically converted into shares of common stock and outstanding warrants to purchase the Company's preferred stock automatically became exercisable for shares of common stock. As a result, as of May 16, 2012, the Company had 26,711,408 shares of common stock issued and outstanding.

(e) Stock Split

On July 15, 2011, the Board of Directors approved a 1-for-2 reverse stock split of the Company's outstanding common stock that was effected on that date, and a proportional adjustment to the existing conversion ratios for each series of convertible preferred stock was made at the time of the effectiveness of the

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WAGWORKS, INC.

Notes to Consolidated Financial Statements

reverse stock split. Accordingly, all share and per share amounts for all periods presented in these consolidated financial statements and notes thereto, have been adjusted retroactively to reflect this reverse stock split, adjustment of the convertible preferred stock conversion and adjustment of the exercise prices of stock options and warrants.

(f) Reclassifications

The Company has reclassified the short-term contingent payment liability, which in the prior year was presented within the accounts payable and accrued expenses category, into its own category to conform to current period presentation.

(g) Liquidity

The Company has completed several rounds of private equity financing as well as an IPO to date. While the Company initially incurred losses for several years, it has experienced positive cash flow from operations since 2005. The Company believes that its existing cash and cash equivalents, cash generated from its operations, and unused borrowing capacity on its line of credit will be sufficient to fund its operations at least through December 31, 2012.

At December 31, 2011 and June 30, 2012, the Company's current liabilities exceeded its current assets by \$35.8 million and \$13.3 million (unaudited), respectively. The Company has historically been able to fulfill its obligations as they fall due and expects to be able to continue to do so in the future. This expectation is based on retaining the majority of its current client base as well as continuing its funding model whereby at the beginning of a plan year, most of the Company's enterprise clients provide it with pre-funds for their Flexible Spending Account, or FSA, programs based on a percentage of projected elections by the employee participants for the plan year ahead. During the plan year, the Company processes employee participants' claims as they are submitted and typically seeks reimbursement from its employer clients within one week after settling the claim. To the extent that this model is discontinued or the Company's client retention significantly deteriorates, its business, operating results and financial condition may be significantly impacted.

Future capital requirements also depend on other factors, including the required level of investment in technology, acquisitions and portfolio purchases. In the first quarter of 2012, the Company completed a portfolio purchase and an acquisition (see Note 3). The Company used its existing line of credit under its Revolver with Union Bank, N.A., or UB (see Note 8), to finance the acquisition and drew down an incremental \$29.6 million. As of June 30, 2012, any borrowing outstanding under the Revolver was due and payable on October 31, 2012. In September 2012, the Company entered into an amendment to extend the due date to October 31, 2013.

(h) Certain Risks

In addition to the liquidity risks discussed above, the Company delivers its CDB programs through a highly scalable Benefits-as-a-Service, or BaaS, delivery model that employer clients and their employee participants may access through a standard web browser on any internet-enabled device, including computers, smart phones and other mobile devices, such as tablet computers. The Company faces risks associated with ongoing sales acceptance, the realization of cost economies of scale, and existing and potential competition.

Additionally, the Company's business is dependent on the availability of tax-advantaged CDBs for employers and employees. Any diminution in, elimination of, or change in the availability of these benefits would significantly impact the Company's operations.

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WAGWORKS, INC.

Notes to Consolidated Financial Statements

(i) Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Significant estimates in these consolidated financial statements include allowances for doubtful accounts, estimates of future cash flows associated with assets, asset impairments, useful lives for depreciation and amortization, loss contingencies, expired and unredeemed products, deferred tax assets, reserve for income tax uncertainties, warrant valuations, and the assumptions used for stock-based compensation, contingent consideration associated with our acquisitions and purchase accounting. Actual results could differ from those estimates. In making its estimates, the Company considers the current economic and legislative environment in the estimates and has considered those factors when reviewing the assumptions and estimates.

(j) Cash, Cash Equivalents, and Restricted Cash

The Company considers all highly liquid investments with an original maturity of 90 days or less to be cash equivalents. Cash and cash equivalents, which consist of cash on deposit with banks and money market funds, are stated at cost. To the extent the Company's contracts do not provide for any restrictions on the Company's use of cash that it receives from clients the cash is recorded as a Company asset.

In all cases, the Company recognizes a related liability to its customers, classified as customer obligations in the accompanying consolidated balance sheets.

Restricted cash represents cash used to collateralize standby letters of credit. The current portion of restricted cash matures in 2012 and is therefore classified as a current asset at December 31, 2011 and June 30, 2012.

(k) Concentration of Credit Risk

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company deposits its cash with several financial institutions, and its deposits, at times, exceed insured amounts.

For the years ended December 31, 2009, 2010 and 2011 and for the unaudited six months ended June 30, 2011 and 2012, no customers accounted for greater than 10% of total revenue or 10% of accounts receivable.

(l) Fair Value of Financial Instruments

Financial Accounting Standards Board (FASB) ASC 820, *Fair Value Measurements and Disclosures*, or ASC 820, provides a consistent framework to define, measure, and disclose the fair value of assets and liabilities in financial statements. ASC 820 establishes a three-level hierarchy priority for disclosure of assets and liabilities recorded at fair value. The ordering of priority reflects the degree to which objective prices in external active markets are available to measure fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable.

The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The Company determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

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Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date.

Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date. The contingent consideration payable related to the Planned Benefits Systems (PBS), Fringe Benefits Management (FBM), Choice Strategies (CS) and TransitCenter (TC) acquisitions (see Note 3) were recorded at fair value on the acquisition date and are adjusted quarterly to fair value. The increases or decreases in the fair value of contingent consideration payable can result from changes in anticipated revenue levels and changes in assumed discount periods and rates. As the fair value measure is based on significant inputs that are not observable in the market, they are categorized as Level 3.

The Lender Warrant (see Note 9) was recorded at fair value on the grant date and is adjusted quarterly to fair value. The Company valued the Lender Warrant using a Black-Scholes option-pricing model, which incorporates assumptions about underlying asset value, volatility, expected remaining life, and risk-free interest rate. These valuation assumptions were estimated based upon management's judgment about the general industry environment. Since the valuation of the Lender Warrant involves significant unobservable inputs, it was categorized as Level 3 under the three-level hierarchy discussed above. Upon the completion of the Company's IPO in May 2012 and the conversion of the Company's outstanding shares of preferred stock into shares of common stock, the Lender Warrant, which was a warrant to purchase Series C redeemable convertible preferred stock, became exercisable for shares of common stock. As the warrant is no longer exercisable into shares of redeemable preferred stock, the warrant was reclassified from liability to equity and the Company will no longer record any mark-to-market changes in the fair value of the warrant in the statements of operations. The Company performed the final re-measurement of the Lender Warrant at the closing date of the Company's IPO on May 15, 2012. The Lender Warrant was then reclassified from liability to equity on that date.

The Investor Warrants (see Note 9) were recorded at fair value on the grant date and were adjusted quarterly to fair value until July 30, 2010. The estimated fair value of the Investor Warrants at December 31, 2010 was determined based upon the Noreen-Wolfson option pricing model, which incorporates assumptions about underlying asset value, volatility, expected remaining life, and risk-free interest rate. These valuation assumptions are estimated based upon management's judgment about the general industry environment and are outlined in Note 9(c).

At July 30, 2010, the Investor Warrant terms were changed from being exercisable for a redeemable preferred share to being exercisable for a preferred share that was not redeemable. Accordingly, the Investor Warrants are classified as equity, under FASB ASC 480, *Distinguishing Liabilities from Equity*, or ASC 480, and FASB ASC 815-40, or ASC 815, *Derivatives and Hedging*, at the date of change and no longer need to be marked-to-market. Since the valuation of the Investor Warrants involves significant unobservable inputs they were categorized as Level 3 under the three-level hierarchy discussed above.

Changes in fair value of the Investor Warrants, until the time they were reclassified as equity, and in fair value of the Lender Warrant are recorded as a separate line item under other income (expense) entitled Gain (loss) on revaluation of warrants in the consolidated statements of operations.

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Other financial instruments not measured at fair value on the Company's unaudited consolidated balance sheet at June 30, 2012, but which require disclosure of their fair values include: cash and cash equivalents (including restricted cash), accounts receivable, accounts payable and accrued expenses and debt under the line of credit with UB. The estimated fair value of such instruments at June 30, 2012 approximates their carrying value as reported on the unaudited consolidated balance sheet. The fair values of all of these instruments are categorized as Level 2 of the fair value hierarchy, with the exception of cash, which is categorized as Level 1.

The following table provides a reconciliation between the beginning and ending balances of items measured at fair value on a recurring basis that used significant unobservable inputs (Level 3) (dollars in thousands):

	Lender Warrant	Contingent Consideration PBS	Contingent Consideration FBM	Contingent Consideration CS	Contingent Consideration TC
Balances at December 31, 2010	\$ 1,470	\$ 6,361	\$ 9,573	\$	\$
Gains or losses included in earnings:					
Gain on revaluation of warrant	(351)				
Loss on revaluation of contingent consideration		1,437	1,255		
Payment of contingent consideration for PBS		(2,000)			
Payment of contingent consideration for FBM		(6,260)	(7,650)		
Balances at December 31, 2011	\$ 1,119	\$ 5,798	\$ 3,178	\$	\$
Initial fair value of contingent consideration				11,054	5,314
Gains or losses included in earnings:					
Gain on revaluation of warrant	(381)				
Loss on revaluation of contingent consideration		1,059	542	846	71
Payment of contingent consideration		(6,260)			
Reclassification of warrant to additional paid-in capital	(738)				
Reduction in FBM contingent consideration due to re-negotiated lease			(528)		
Balances at June 30, 2012 (unaudited)	\$	\$ 597	\$ 3,192	\$ 11,900	\$ 5,385

In the first quarter of 2012, the Company re-negotiated its lease with Fringe Benefits Management Company, or FBMC, from whom the Company leases a facility in Florida. Both parties agreed to a reduction in the rental rate for the remainder of the lease term and subsequently amended their Shared Services Agreement. In connection with this lease re-negotiation, FBMC and the Company agreed to reduce the amount of contingent consideration due to FBMC in 2012 by \$0.5 million. The Company is amortizing this amount over the remaining term of the lease.

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements***Quantitative Information About Level 3 Fair Value Measurements*

The significant unobservable inputs used in the fair value measurement of the Company's contingent consideration and Lender Warrant designated as Level 3 are as follows:

	Fair Value at June 30, 2012 (in thousands, unaudited)	Valuation Technique	Significant Unobservable Input
Contingent consideration FBM	\$ 3,192	Discounted cash flow	Annualized revenue and probability of achievement
Contingent consideration CS	\$ 11,900	Discounted cash flow	Annualized revenue and probability of achievement
Contingent consideration TC	\$ 5,385	Discounted cash flow	Annualized revenue and probability of achievement

Sensitivity To Changes In Significant Unobservable Inputs

As presented in the table above, the significant unobservable inputs used in the fair value measurement of contingent consideration related to the acquisitions are annualized revenue forecasts developed by the Company's management and the probability of achievement of those revenue forecasts. The significant unobservable inputs used in the fair measurement of the Lender Warrant are the volatility of the underlying stock value, expected term and the value of our common stock. Significant increases (decreases) in these unobservable inputs in isolation would result in a significantly lower (higher) fair value measurement.

(m) Accounts Receivable

Accounts receivable represent both amounts receivable in relation to fees for the Company's services and unpaid amounts by customers for benefit services of participants provided by third-party vendors, such as transit agencies and healthcare providers (see Note 5). The Company provides for an allowance for doubtful accounts by reference to reserves for specific accounts. The Company reviews its allowance for doubtful accounts monthly. Accounts more than 30 days past due are reviewed weekly for collectability. Account balances are written off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Write-offs for 2009, 2010 and 2011 and the unaudited three and six months ended June 30, 2011 and June 30, 2012 were not significant.

(n) Deferred Offering Costs

Deferred offering costs of \$3.9 million are included in the accompanying consolidated balance sheet within prepaid expenses and other current assets at December 31, 2011. In May 2012, the Company closed its IPO and offset \$5.5 million of offering costs against the proceeds it received in the offering. There were no deferred offering costs at December 31, 2010.

(o) Property and Equipment

Property and equipment are stated at cost. Depreciation on computer and equipment and furniture and fixtures is calculated on a straight-line basis over the estimated useful lives of those assets, ranging from three to five years. Leasehold improvements are amortized over the shorter of their estimated useful life or the lease term. Total depreciation expense, including amortization of internal use software, for the years ended December 31, 2009, 2010 and 2011 was \$9.6 million, \$9.7 million, and \$9.2 million respectively and for both the unaudited three months ended June 30, 2011 and 2012 was \$2.3 million. Total depreciation expense for the unaudited six months ended June 30, 2011 and 2012 was \$4.6 million and \$4.5 million, respectively.

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When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from their respective accounts, and any gain or loss on such sale or disposal is reflected in operating expenses.

Maintenance and repairs are expensed as incurred. Expenditures that substantially increase an asset's useful life are capitalized.

(p) Software and Web Site Development Costs

The Company recognizes internal use software and Web site development costs in accordance with FASB ASC Subtopic 350-40, *Internal-Use Software*, and FASB ASC Subtopic 350-50, *Intangibles - Website Development Costs*, respectively. As such, the Company expenses all costs incurred that relate to the planning and post implementation phases of development. Costs incurred in the development phase are capitalized and recognized over the technology's estimated useful life, generally four years, as amortization in the accompanying consolidated statements of operations. Amortization expense related to capitalized development costs was \$5.0 million, \$5.6 million, and \$6.0 million for 2009, 2010, and 2011 respectively. In the unaudited three months ended June 30, 2011 and June 30, 2012, the Company recorded \$1.5 million and \$1.6 million of amortization expense related to these costs, respectively. In the six months ended June 30, 2011 and June 30, 2012, the Company amortized \$2.9 million and \$3.0 million of capitalized software development costs, respectively. Costs associated with the platform content or the repair or maintenance of the existing platforms are expensed as incurred.

The Company accounts for interest costs related to internal use software and Web site development costs in accordance with the provisions of FASB ASC Subtopic 835-20, *Interest - Capitalization of Interest*, which require capitalization of interest on major construction or acquisition projects where the financial statement effect of capitalization versus current expense recognition is likely to be material. Capitalized interest related to software and development costs was immaterial for all years.

(q) Accounting for Impairment of Long-Lived Assets

In accordance with FASB ASC Subtopic 360-10, *Property, Plant and Equipment*, the Company evaluates the remaining useful life and recoverability of property and equipment and other assets, including identifiable intangible assets with definite lives, whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets held and used is measured by comparison of the carrying amount of an asset or an asset group to estimated undiscounted future net cash flows expected to be generated by the asset or asset group. If the carrying amount of an asset exceeds these estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the assets exceeds the fair value of the asset or asset group, based on discounted cash flows. Assets to be disposed of are reported at the lower of their carrying amount or fair value less cost to sell. The Company recorded impairment adjustments of \$345,000, \$120,000, and \$116,000 in 2009, 2010 and 2011, respectively, related to software development costs which are included in property and equipment, net in the accompanying consolidated financial statements. There were no impairment adjustments in the unaudited three and six months ended June 30, 2011 and 2012.

(r) Acquisitions and Goodwill

The Company has accounted for all of its acquisitions using the purchase method as required under the provisions of FASB ASC 805, *Business Combinations*, or ASC 805. The cost of acquisition is allocated to the assets acquired and liabilities assumed based on fair values at the date of acquisition. Goodwill represents the excess cost over the fair value of net assets acquired in the acquisition.

The Company performs a goodwill impairment test annually on December 31st and more frequently if events and circumstances indicate that the asset might be impaired. The following are examples of triggering

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WAGEWORKS, INC.

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events (none of which occurred in 2011 or in the six months ended June 30, 2012) that could indicate that the fair value of a reporting unit has fallen below the unit's carrying amount:

A significant adverse change in legal factors or in the business climate

An adverse action or assessment by a regulator

Unanticipated competition

A loss of key personnel

A more-likely than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of. The impairment test is performed in accordance with FASB ASC 350, *Intangibles - Goodwill and Other*, or ASC 350, and an impairment loss is recognized to the extent that the carrying amount exceeds the reporting unit's fair value. When reviewing goodwill for impairment, the Company assesses whether goodwill should be allocated to operating levels lower than the Company's single operating segment for which discrete financial information is available and reviewed for decision-making purposes. These lower levels are referred to as reporting units. The Company's chief operating decision maker, the Chief Executive Officer, does not allocate resources or assess performance at the individual healthcare, commuter or other revenue stream level, but rather at the operating segment level. Discrete financial information is therefore not maintained at the revenue stream level. The Company's operating segment is the aggregation of these three revenue streams and is the Company's one reporting unit.

The goodwill impairment analysis is a two-step process: first, the reporting unit's estimated fair value is compared to its carrying value, including goodwill. If the Company determines that the estimated fair value of the reporting unit is less than its carrying value, the Company moves to the second step to determine the implied fair value of the reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of the reporting unit in a manner similar to a purchase price allocation.

The fair value of the Company's reporting unit was determined using the market approach. In the application of the market approach, the Company is required to make estimates of future operating trends and judgments on discount rates and other variables. Actual future results related to assumed variables could differ from these estimates. Discount rates are based on a weighted average cost of capital, which represents the average rate a business must pay its providers of debt and equity capital. The Company used discount rates that are the representative weighted average cost of capital for its reporting unit in comparison with peer companies, with consideration given to the current condition of the global economy. The Company determines projected income based on the Company's best estimate of near term revenue and Earnings before Interest, Income Taxes, Depreciation and Amortization, or EBITDA, expectations and long-term projections; estimated Adjusted EBITDA for 2011 compared to 2010 indicated an increase. As a sensitivity analysis, a 100 basis point reduction in the assumed net sales growth beginning in fiscal 2012 would decrease minimally the overall valuation but it would not cause a change in the results of the Company's impairment testing that indicated no impairment of goodwill.

As of the end of the Company's fourth quarter of fiscal year 2011, the period of its last annual impairment test, the fair value of its reporting unit determined under the market approach exceeded the Company's aggregate carrying value by a significant amount. To date, the Company has not made any impairment adjustments to goodwill as the fair value of its reporting unit has always exceeded its carrying value.

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements****(s) Warrants**

The Company accounts for freestanding warrants exercisable into shares that are redeemable in accordance with ASC 480. Under ASC 480, warrants to acquire Preferred Stock where that stock is potentially redeemable must be reported as liabilities and marked to market at each reporting period from the warrant issuance date until the exercise date or expiration. If the warrants were issued in connection with a debt financing, the Company follows the guidance of FASB ASC 470, *Debt*, which requires that the proceeds from an issuance of debt with warrants, where the warrant is classified as a liability, be allocated first to the warrant based upon the warrant fair value and the residual amount of the proceeds are allocated to the debt. The warrant terms for the Investor Warrants were changed on July 30, 2010 and became exercisable for Preferred Stock that is not redeemable and for that reason the warrants are now classified as equity under ASC 480.

(t) Revenue Recognition

The Company reports revenue based on the following product lines: Healthcare, Commuter, and Other services. Healthcare and Commuter include revenues generated from benefit service fees based on client employee (known as participant) participation levels and interchange and other commission revenues. Interchange and other commission revenues are based on a percentage of total healthcare and commuter dollars transacted pursuant to written purchase agreements with certain vendors and banks. Other revenue includes services related to Consolidated Omnibus Budget Reconciliation Act, or COBRA, enrollment and eligibility, nonhealthcare, and employee account administration (i.e., tuition and health club reimbursements) and project-related professional services.

The Company recognizes all revenue streams in accordance with FASB ASC 605, *Revenue Recognition*. As such, the Company recognizes revenue when collectability is reasonably assured, service has been performed, persuasive evidence of an arrangement exists, and there is a fixed or determinable fee.

Benefit service fees are recognized on a monthly basis as services are rendered and earned under service arrangements where fees and commissions are fixed or determinable and collectability is reasonably assured. Benefit service fees are based on a fee for service model (e.g., monthly fee per participant) in which revenue is recognized on a monthly basis as services are rendered under price quotations or service agreements having stipulated terms and conditions, which do not require management to make any significant judgments or assumptions regarding any potential uncertainties. Fees received for initial setup of new clients and annual renewal fees are deferred and recognized on a monthly basis as services are rendered over the agreed benefit period. The initial setup fees are not considered separable from the ongoing services provided for which benefit service fees are earned.

Vendor and bank interchange revenues are attributed to revenue sharing arrangements the Company enters into with certain banks and card associations, whereby the Company shares a portion of the transaction fees earned by these financial institutions on debit cards the Company issues to its employee participants based on a percentage of total dollars transacted as reported on third-party reports. Commission revenue entails the Company purchasing passes on behalf of its employee participants from various transit agencies and due to the significant volume of purchases, the Company receives commissions on these passes which the Company records on a net basis. Commission revenue is recognized on a monthly basis as transactions are placed under written purchase agreements having stipulated terms and conditions, which do not require management to make any significant judgments or assumptions regarding any potential uncertainties. In addition, the Company recognizes revenue on our estimate of passes that will expire unused over the estimated useful life of the passes, as the amounts paid for these passes are nonrefundable to both the employer client and the employee participant.

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Professional service fees are related to projects provided to the Company's existing employer clients that last up to two months to accommodate their changing reporting and file transfer requirements and recognized upon completion of services and projects. These projects are discrete contracts and are not entered into contemporaneously with any other services the Company provides. The professional services are rendered with written price quotations or service agreements having stipulated terms and conditions, which do not require management to make any significant judgments or assumptions regarding any potential uncertainties and where fees are fixed or determinable and collectability is reasonably assured.

(u) Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB ASC 718, *Compensation - Stock Compensation*, or ASC 718. Under ASC 718, stock-based compensation cost is measured at the grant date, based on the estimated fair value of the award at that date, and is recognized as expense over the employee's requisite service period (generally over the vesting period of the award) on a straight-line basis.

ASC 718 requires the benefits of tax deductions in excess of the compensation cost recognized for those options to be classified as financing cash inflows rather than operating cash inflows. There were no material excess tax benefits in the years ended December 31, 2009, 2010 and 2011 and the unaudited six months ended June 30, 2011 and June 30, 2012.

(v) Advertising Costs

Advertising costs are charged to expense in the period incurred. Advertising costs consist of expenses incurred to run advertisements. The Company incurred \$126,000, \$280,000, and \$40,000, of advertising costs in 2009, 2010 and 2011, respectively, and \$11,000 and \$9,000 in the unaudited three months ended June 30, 2011 and June 30, 2012, respectively. The Company incurred \$38,000 and \$9,000 of advertising costs in the unaudited six months ended June 30, 2011 and June 30, 2012, respectively.

(w) Customer Obligations

Customer obligations represent liabilities incurred as a result of cash amounts received from customers and as a result of amounts billed to customers in which the Company has the legal right to bill and has yet to fulfill or initiate the related services.

(x) Leases

The Company leases various office space and equipment. The Company classifies its leases as either operating or capital lease arrangements in accordance with the criteria of FASB ASC 840, *Leases*. Certain of the Company's operating leases for office space contain provisions under which monthly rent escalates over time and certain leases also contain provisions for reimbursement of a specified amount of leasehold improvements. When lease agreements contain escalating rent clauses, the Company recognizes rent expense on a straight-line basis over the term of the lease. When lease agreements provide allowances for leasehold improvements, the Company capitalizes the leasehold improvement assets and amortizes them on a straight-line basis over the lesser of the lease term or the estimated useful life of the asset, and reduces rent expense on a straight-line basis over the term of the lease by the amount of the allowances provided.

(y) Income Taxes

The Company reports income taxes in accordance with FASB ASC 740, *Income Taxes*, which requires an asset and liability approach in accounting for income taxes. Deferred tax assets and liabilities arise from the

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differences between the tax basis of an asset or liability and its reported amount in the consolidated financial statements, as well as from net operating loss and tax credit carryforwards. Deferred tax amounts are determined by using the tax rates expected to be in effect when the taxes will actually be paid or refunds received, as provided under current enacted tax law. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance reduces the deferred tax assets to the amount that is more likely than not to be realized.

The Company uses financial projections to support its net deferred tax assets, which contain significant assumptions and estimates of future operations. If such assumptions were to differ significantly, it may have a material impact on the Company's ability to realize its deferred tax assets. At the end of each period, the Company assesses the ability to realize the deferred tax benefits. If it is more likely than not that the Company would not realize the deferred tax benefits, then the Company would establish a valuation allowance for all or a portion of the deferred tax benefits.

Under ASC Subtopic 740-10, the Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained on examination by the taxing authorities, based on the technical merits of the position. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

The Company records interest and penalties related to uncertain tax positions in income tax expense.

(z) Legal Matters and Contingencies

The Company accrues for estimated losses in accordance with FASB ASC 450, *Contingencies*, which requires an accrual for matters where the Company believes that the likelihood that a loss will occur is probable and the amount of loss is reasonably estimable. Legal costs incurred in connection with loss contingencies are expensed as incurred.

(aa) Reduction in Force

In accordance with FASB ASC 420, *Exit or Disposal Obligations*, restructuring costs are recorded as incurred. The Company accrues severances once the total severance pool has been calculated, approved, and communicated and recognizes the expense ratably over the required service period, from the communication date to the exit date. The Company took actions with reductions in force during 2009 and recorded approximately \$1.0 million in severance charges in 2009, which were fully paid out in 2009.

In the first quarter of 2012, the Company closed its Troy, Michigan facility and consolidated redundant activities within its operations, which resulted in charges for the remaining lease payments due on a lease and the elimination of certain personnel. The expenses related to these actions were approximately \$0.5 million.

(bb) Indemnification Agreements

In accordance with FASB ASC 460, *Guarantees*, the Company has disclosed and accounted for all guarantees. No amounts were recorded under these guarantees in 2009, 2010 and 2011 and in the unaudited six months ended June 30, 2012.

The Company has signed indemnification agreements with all board members. The agreements indemnify the members from claims and expenses on actions brought against the individuals separately or jointly with the

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WAGWORKS, INC.

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Company for Indemnifiable Events. Indemnifiable Events generally mean any event or occurrence related to the fact that the board member was or is acting in their capacity as a board member for the Company or was or is acting or representing the interests of the Company.

(cc) Recently Issued Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-11, *Disclosures about Offsetting Assets and Liabilities*, which creates new disclosure requirements about the nature of an entity's rights of offset and related arrangements associated with its financial instruments and derivative instruments. The disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods therein, with retrospective application required. The adoption of ASU 2011-11 may have a financial disclosure impact on the Company but will not have a material impact on the Company's financial position or results of operations.

In September 2011, the FASB issued Accounting Standards Update, or ASU 2011-08, *Intangibles - Goodwill and Other (Topic 350): Testing Goodwill for Impairment*. The guidance in ASU 2011-08 is intended to reduce complexity and costs by allowing an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it should calculate the fair value of a reporting unit. If impairment is deemed more likely than not, management would perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. The amendments also improve previous guidance by expanding upon the examples of events and circumstances that an entity should consider between annual impairment tests in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Also, the amendments improve the examples of events and circumstances that an entity having a reporting unit with a zero or negative carrying amount should consider in determining whether to measure an impairment loss, if any, under the second step of the goodwill impairment test. The amendments in this ASU are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The adoption of ASU 2011-08 is not expected to have a material impact on the Company's financial position or results of operations.

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements****(2) Net Income (Loss) per share**

The following table sets forth the computation of basic and diluted net income (loss) per share attributable to Common Stockholders:

	Year Ended December 31,		Three Months Ended June 30,			Six Months Ended June 30,	
	2009	2010	2011	2011	2012	2011	2012
	(in thousands, except per share data) (unaudited)						
Numerator (basic and diluted):							
Net income (loss)	\$ (634)	\$ (17,250)	\$ 33,321	\$ 3,871	\$ 3,224	\$ 6,900	\$ 5,234
Less: accretion of redemption premium (expense) benefit	1,037	(6,740)	(6,209)	(2,924)	(778)	(5,692)	(2,301)
Net income (loss) attributable to common stockholders for basic EPS	\$ 403	\$ (23,990)	\$ 27,112	\$ 947	\$ 2,446	\$ 1,208	\$ 2,933
Add back: accretion of redemption premium related to dilutive redeemable preferred stock	(1,037)		1,587		(86)		(260)
Net income attributable to common stockholders for diluted EPS	\$ (634)	\$ (23,990)	\$ 28,699	\$ 947	\$ 2,360	\$ 1,208	\$ 2,673
Denominator (basic):							
Weighted average common shares outstanding	1,606	1,528	1,536	1,535	14,268	1,534	7,907
Denominator (diluted):							
Weighted average common shares outstanding	1,606	1,528	1,536	1,535	14,268	1,534	7,907
Dilutive stock options and awards outstanding	218		1,010	1,195	1,305	1,122	1,109
Weighted average common shares from stock warrants			2,500	2,854	2,793	2,854	2,626
Weighted average common shares from preferred stock	15,040		15,040	10,866	5,983	10,866	9,041
Net weighted average common shares outstanding	16,864	1,528	20,086	16,450	24,349	16,376	20,683
Net income (loss) per share attributable to holders of common stock:							
Basic	\$ 0.25	\$ (15.70)	\$ 17.65	\$ 0.62	\$ 0.17	\$ 0.79	\$ 0.37
Diluted	\$ (0.04)	\$ (15.70)	\$ 1.43	\$ 0.06	\$ 0.10	\$ 0.07	\$ 0.13

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Diluted net income (loss) per share does not include the effect of the following anti-dilutive common equivalent shares:

	Year Ended		2011	Three Months Ended		Six Months	
	2009	December 31, 2010		2011	June 30, 2011	2012	Ended June 30, 2011
Stock options outstanding	2,810	4,507	152	135	61	135	60
Common equivalent shares from stock warrants	4,451	4,653					
Common shares from convertible debt	4,164						
Common shares from convertible preferred stock		17,688	2,648	5,586	2,764	5,586	4,176
Total common stock equivalents	11,425	26,848	2,800	5,721	2,825	5,721	4,236

(3) Acquisitions

On August 31, 2010, the Company acquired 100% of the outstanding common shares of Planned Benefits Systems (PBS). The results of operations of PBS have been included in the Company's consolidated results of operations since this date. PBS is engaged in the business of providing required health and flexible benefits administration and COBRA continuation services and is based in Denver, Colorado. This acquisition added a new regional base of customers and participant relationships. The aggregate noncontingent portion of the purchase price was \$2.9 million and was paid in cash on August 31, 2010.

The purchase price included a contingent consideration element that requires the Company to pay in 2011 and 2012 the former owners of PBS additional amounts based upon annualized revenues of PBS for 2011 and 2012, respectively. The initial fair value of the contingent consideration was determined from forecasts developed by management based upon existing business, customer relationships and historical growth rates. The Company discounted those forecasts using an 18.5% weighted average cost of capital. The Company measures acquired contingent consideration payable each reporting period at fair value, and recognizes changes in fair value in earnings each period in the amortization and change in contingent consideration line item on the statement of operations, until the contingency is resolved. The Company recorded a \$1.4 million charge related to the change in fair value of the contingent consideration during 2011. Increases or decreases in the fair value of the contingent consideration payable can result from changes in anticipated revenue levels and changes in assumed discount periods and rates. Significant judgment is employed in determining the appropriateness of these assumptions each period. The contingent payment for 2011 of \$2.0 million was paid in April 2011. The fair value of the contingent element at December 31, 2011 was estimated at \$5.2 million, which was an increase of \$1.4 million over the acquisition date fair value of the remaining payment due to increased revenue levels being achieved. The Company recorded \$0.1 million in charges related to the change in fair value of the contingent consideration during the unaudited three and six months ended June 30, 2011 as a result of the passage of time. The Company recorded a \$0.1 million credit during the unaudited three months ended June 30, 2012 related to the change in fair value of the contingent consideration, due to a final valuation of the amount to be paid out to the former owners of PBS. The Company recorded \$1.1 million in charges during the unaudited six months ended June 30, 2012 related to the change in fair value of the contingent consideration due to increased revenue levels being achieved. The contingent payment for 2012 of \$6.3 million was paid in May 2012. There is also an amount of \$0.6 million, which was held back from the initial consideration paid, to account for possible future contingencies and is expected to be paid in the third quarter of 2012. As the fair value measure is based on significant inputs that are not observable in the market, the Company categorizes the inputs as Level 3 inputs under ASC 820.

Since the acquisition was a stock purchase, goodwill and intangibles cannot be amortized for tax purposes; accordingly, a deferred tax liability of \$1.8 million was recorded at the date of acquisition for the book tax cost basis difference related to the intangibles.

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On November 30, 2010, the Company acquired a division, or FBM, in a carve-out from Fringe Benefits Management Company, a Florida corporation, or FBMC. The acquired division related to the tax-advantaged business of providing flexible benefits administration, commuter, and COBRA continuance services for public service entities. This acquisition added a new regional base of clients and participant relationships. The results of FBM's operations have been included in the consolidated financial statements since that date. The aggregate noncontingent portion of the purchase price was \$7.2 million and was paid in cash in two installments: at November 30, 2010 (\$2.5 million) and January 14, 2011 (\$4.7 million). The Company has determined that FBM represented a business which the Company obtained control on November 30, 2010. On that date, the Company also entered into a Shared Services Agreement, or SSA, with FBMC to provide operational continuity to both parties as acquired customer contracts assumed by the Company were being assigned to the Company and to provide ongoing support to FBMC for the processing of certain tax favored business bundled as part of FBMC's offerings as part of their ongoing business.

The purchase price included a contingent consideration element that required the Company to pay in 2011 and requires the Company to pay in 2012 FBMC additional amounts based upon annualized revenues of FBM for 2011 and 2012, respectively. The initial fair value of the contingent consideration was determined from forecasts developed by management based upon existing business, customer relationships and historical growth rates. Since FBM was a carve-out, some historical revenue details were not available and the forecasts relied upon FBMC management's best estimates based upon current business and their understanding of retention rates and the marketplace. The Company discounted those forecasts using an 18% weighted average cost of capital. The Company measures acquired contingent consideration payable each reporting period at fair value, and recognizes changes in fair value in earnings each period in the amortization and change in contingent consideration line item on the statement of operations, until the contingency is resolved. The Company recorded a \$1.3 million charge related to the change in fair value of the contingent consideration during 2011. Increases or decreases in the fair value of the contingent consideration payable can result from changes in anticipated revenue levels and changes in assumed discount periods and rates. Significant judgment is employed in determining the appropriateness of these assumptions each period. The contingent payment for 2011 of \$3.0 million was paid in August 2011. The fair value of the contingent element at December 31, 2011 was estimated at \$3.2 million, which was an increase of \$0.7 million over the acquisition date fair value of the remaining payment due to increased revenue levels being achieved. The Company recorded \$0.5 million and \$0.8 million in charges related to the change in fair value of the contingent consideration during the unaudited three and six months ended June 30, 2011, respectively, due to increased revenue levels being achieved. The Company recorded \$0.1 million and \$0.5 million in charges related to the change in fair value of the contingent consideration during the unaudited three and six months ended June 30, 2012, respectively, due to increased revenue levels estimated to be achieved. In addition, there was a \$0.5 million reduction to the contingent consideration element in connection with a lease re-negotiation (see Note 1 (I)). The fair value of the contingent element at June 30, 2012 was estimated at \$3.2 million. As the fair value measure is based on significant inputs that are not observable in the market, the Company categorizes the inputs as Level 3 inputs under ASC 820.

The Choice Care Card, LLC Acquisition (unaudited)

On January 3, 2012, the Company acquired the operating assets and certain liabilities of The Choice Care Card, LLC, or CS, a Vermont limited liability company. CS administers tax-advantaged, consumer-driven health care programs, primarily HRAs, through a debit card or direct-pay to provider or member platform. This acquisition added a new regional base of customers and participant relationships. The aggregate non-contingent portion of the purchase price paid in cash was \$8.7 million of which \$8.3 million was paid at closing.

The Company accounted for the acquisition of CS as a purchase of a business under ASC 805. The results of operations for CS have been included in the Company's financial results since the acquisition. The financial results of this acquisition are considered insignificant for purposes of pro forma financial statement disclosures.

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The purchase price included a contingent consideration element that requires the Company to pay in 2012 and 2013 the former owners of CS additional amounts based upon annualized revenues of CS for 2012 and 2013 respectively. The Company determined that the total initial fair value for both contingent payments as of the acquisition date was \$11.1 million. The Company recorded its estimate of the fair value of the contingent consideration based on a weighted average probability evaluation of various revenue forecasts developed by management. The resultant liability was discounted to present value at 5.3% to reflect the time value of money. Significant judgment is employed in determining the fair value each period. In the unaudited three and six months ended June 30, 2012, the Company recorded \$0.7 million and \$0.8 million in charges, respectively, in the amortization and change in contingent consideration line item in the Company's accompanying consolidated statements of operations related to the change in fair value of the contingent consideration due to increased revenue levels estimated to be achieved. As the fair value measure is based on significant inputs that are not observable in the market, the Company categorizes the inputs as Level 3 inputs under ASC 820.

The following table summarizes the allocation of the purchase price at the date of acquisition (in millions):

	Amount	Weighted Average Useful Life (in years)
Net tangible assets acquired	\$ 0.6	
Customer relationships	9.2	10
Developed technology	0.6	2
Goodwill	9.4	
Total allocation of purchase price	\$ 19.8	

As part of the purchase price allocation, the Company determined that CS's separately identifiable intangible assets were its customer relationships and developed technology. The Company used the income approach to value the customer relationships. This approach calculates fair value by discounting the after-tax cash flows back to a present value. The baseline data for this analysis was the cash flow estimates used to price the transaction. Cash flows were forecasted and then discounted using a discount rate for customer relationships of 13%, based on the estimated weighted average cost of capital, which employs an estimate of the required equity rate of return and after-tax cost of debt.

Goodwill recognized from the transaction results from the acquired workforce, the opportunity to expand our client base and achieve greater long-term growth opportunities than either company had operating alone. All of the recognized goodwill is expected to be deductible for tax purposes.

TransitChek Acquisition (unaudited)

On February 1, 2012, the Company acquired the commuter benefit services business TransitChek, or TC, from TransitCenter, Inc., or TCI, a New York-based not for profit entity that provided commuter benefit services predominantly to SMB employer clients in the New York tri-state area. This acquisition added a new base of transit customers and participant relationships. The aggregate non-contingent portion of the purchase price was \$31.1 million of which \$30.8 million was paid at closing.

The Company accounted for the acquisition of TC as a purchase of a business under ASC 805. The results of operations for TC have been included in the Company's financial results since the acquisition. The Company concluded that the acquisition of TC represented a material business combination for the purposes of pro forma financial statement disclosure and therefore, pro forma financial information has been provided herein.

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The purchase price included an additional future payment of \$0.7 million that was discounted to present value and will be paid over the next four years to a promotional fund in furtherance of TCI's mission of raising awareness of the benefits of mass transit. The purchase price also included a contingent consideration element that requires the Company to pay an additional amount in July 2012 to the former owners of TCI, based on the achievement of certain revenue levels for the six months following the closing. The Company determined that based on the probability of achievement that the full contingent payment would be payable. The resultant liability of \$5.3 million was discounted to present value at 3.25%, to reflect the time value of money. In the unaudited three and six months ended June 30, 2012, the Company recorded less than \$0.1 million and \$0.1 million in charges, respectively, related to the change in fair value of the contingent consideration as a result of the passage of time, in the amortization and change in contingent consideration line item in the Company's accompanying consolidated statements of operations. As the fair value measure is based on significant inputs that are not observable in the market, the Company categorizes the inputs as Level 3 inputs under ASC 820.

As part of the purchase price allocation, the Company determined that TC's separately identifiable intangible assets were its customer relationships, developed technology, trade names and a favorable lease. The Company used the income approach to value the customer relationships and trade name. This approach calculates fair value by discounting the after-tax cash flows back to a present value. The baseline data for this analysis was the cash flow estimates used to price the transaction. Cash flows were forecasted and then discounted using a discount rate for customer relationships and trade name of 16% and 15%, respectively, based on the estimated weighted average cost of capital, which employs an estimate of the required equity rate of return and after-tax cost of debt.

The following table summarizes the allocation of the purchase price at the date of acquisition (in millions):

	Amount	Weighted Average Useful Life (in years)
Net tangible assets acquired	\$ 1.7	
Customer relationships	8.8	8.7
Developed technology	4.4	3.0
Trade names	0.9	10.0
Favorable lease	1.1	11.0
Goodwill	20.2	
Total allocation of purchase price	\$ 37.1	

Net tangible assets acquired in the acquisition of TC primarily related to the following (in millions):

	Amount
Cash	\$ 48.3
Restricted cash	0.5
Accounts receivable	0.9
Inventory	3.9
Prepays and other assets	0.1
Property and equipment	1.4
Customer obligations	(51.0)
Accounts payable and accrued expenses	(2.4)
Total allocation of purchase price	\$ 1.7

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The Company used a replacement cost approach to estimate the fair value of developed technology in which estimates of development time and cost per man month are used to calculate total replacement cost. The Company estimated the fair value of the favorable lease terms by discounting the amount by which the stated lease payments differ from current estimated market rates at the acquisition date over the remaining lease term.

Goodwill recognized from the transaction results from the acquired workforce, the opportunity to expand our client base and achieve greater long-term growth opportunities than either company had operating alone. All of the recognized goodwill is expected to be deductible for tax purposes.

The following unaudited pro forma financial information presents the consolidated results of operations of the Company and TC as if the acquisition had occurred at the beginning of fiscal 2011 with pro forma adjustments to give effect to amortization of intangible assets and an increase in interest expense due to financing costs in connection with the acquisition. The pro forma financial information is presented for informational purposes only and may not be indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of the related fiscal years.

	Three Months ended June 30,	2011	2012	Six Months ended June 30,	2011	2012
	(unaudited)		(unaudited)			
	(in thousands, except per share data)					
Total revenue	\$ 38,990	\$ 43,777	\$ 79,966	\$ 89,887		
Net income attributable to common stockholders	\$ 204	\$ 2,446	\$ 581	\$ 2,662		
Net income per share attributable to common stockholders:						
Basic	\$ 0.13	\$ 0.17	\$ 0.38	\$ 0.34		
Diluted	\$ 0.01	\$ 0.10	\$ 0.04	\$ 0.13		

Aflac Channel Partner Arrangement

In April 2012, the Company entered into a channel partner arrangement with American Family Life Assurance Company, or Aflac, pursuant to which Aflac's FSA and commuter account administration business will be transitioned to the Company from July 2012 through the end of December 2012. In conjunction with the transition, Aflac and the Company also entered into a separate reseller arrangement pursuant to which Aflac agents will sell the Company's FSA, HRA, HSA, commuter and COBRA at agreed prices and commission levels to new employers going forward.

The timing of the transition of revenue to the Company and the one time conversion payments to Aflac are dependent upon the employer clients executing new agreements, a process controlled by the Company's new channel partner and the particular employer client. The conversion payments will be calculated as a function of the expected annual revenue for each employer client. These one-time conversion payments will be capitalized and amortized over the expected life of the relationships. The Company will also incur approximately \$0.5 million to \$0.8 million of one-time transition costs predominately in the third quarter of 2012, which are primarily cost of revenue expenses, in advance of revenue.

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements****(4) Goodwill and Intangible Assets**

The changes in the carrying amount of goodwill for the years ended December 31, 2010 and 2011 and for the unaudited six months ended June 30, 2012 are as follows (dollars in thousands):

	December 31,		June 30,
	2010	2011	2012 (unaudited)
Balance at beginning of year	\$ 33,767	\$ 46,806	\$ 46,233
Additions	13,039	17	29,589
PBS acquisition adjustment		(590)	
Balance at end of year	\$ 46,806	\$ 46,233	\$ 75,822

At December 31, 2011, the Company recorded a \$0.6 million PBS acquisition adjustment related to customer obligation balances recorded as of the acquisition date. This adjustment was primarily due to the Company's reliance on reports that incorrectly stated customer obligations at the acquisition date. The correction of these balances is considered a purchase price adjustment.

Acquired intangible assets at December 31, 2010 and 2011 and June 30, 2012 were comprised of the following (dollars in thousands):

	December 31,			2011			June 30,		
	2010		Net	2011		Net	2012		Net
	Gross carrying amount	Accumulated amortization		Gross carrying amount	Accumulated amortization		Gross carrying amount	Accumulated amortization (unaudited)	
Amortized intangible assets:									
Client contracts and broker relationships	\$ 26,534	\$ 13,224	\$ 13,310	\$ 26,534	\$ 15,206	\$ 11,328	\$ 44,424	\$ 17,079	\$ 27,345
Trade names	1,020	388	632	1,020	542	478	2,010	663	1,347
Technology	2,580	1,678	902	2,580	2,177	403	7,542	3,104	4,438
Noncompete agreements	2,011	1,625	386	2,011	1,665	346	2,011	1,685	326
Favorable lease							1,121	42	1,079
Total	\$ 32,145	\$ 16,915	\$ 15,230	\$ 32,145	\$ 19,590	\$ 12,555	\$ 57,108	\$ 22,573	\$ 34,535

Amortization expense for acquired intangible assets totaled \$3.4 million, \$2.2 million, and \$2.7 million in 2009, 2010 and 2011, respectively. Amortization expense for acquired intangible assets totaled \$0.7 million and \$1.7 million for the unaudited three months ended June 30, 2011 and 2012, respectively. Amortization expense for acquired intangible assets totaled \$1.4 million and \$3.0 million for the unaudited six months ended June 30, 2011 and 2012, respectively.

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The estimated amortization expense for each of the five succeeding years and thereafter at December 31, 2011 is as follows (dollars in thousands):

2012	\$ 2,413
2013	2,226
2014	1,680
2015	1,530
2016	1,381
Thereafter	3,325
Total	\$ 12,555

(5) Accounts Receivable

Accounts receivable at December 31, 2010 and 2011 and June 30, 2012 were comprised of the following (dollars in thousands):

	December 31,		June 30,
	2010	2011	2012
			(unaudited)
Trade receivables	\$ 9,438	\$ 11,128	\$ 12,534
Unpaid amounts for benefit services	5,568	4,588	5,689
	15,006	15,716	18,223
Less allowance for doubtful accounts	(415)	(69)	(197)
Accounts receivable, net	\$ 14,591	\$ 15,647	\$ 18,026

(6) Property and Equipment

Property and equipment at December 31, 2010 and 2011 and June 30, 2012 were comprised of the following (dollars in thousands):

	December 31,		June 30,
	2010	2011	2012
			(unaudited)
Computers and equipment	\$ 8,487	\$ 8,799	\$ 9,871
Software and development costs	36,373	43,922	49,691
Furniture and fixtures	3,143	3,046	3,265
Leasehold improvements	6,320	6,752	6,964

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Less accumulated depreciation and amortization	\$ 54,323 (35,630)	\$ 62,519 (43,505)	\$ 69,791 (46,634)
Property and equipment, net	\$ 18,693	\$ 19,014	\$ 23,157

During 2009, 2010 and 2011 the Company capitalized software development costs of \$5.6 million, \$5.5 million, \$8.3 million, respectively. In the unaudited six months ended June 30, 2012, the Company capitalized software development costs of \$5.3 million. In 2009, 2010 and 2011, the Company has amortized \$5.0 million, \$5.6 million, and \$6.0 million, respectively, of these costs. In the unaudited three months ended June 30, 2011 and 2012, the Company amortized \$1.5 million and \$1.6 million of capitalized software development costs,

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respectively. In the unaudited six months ended June 30, 2011 and 2012, the Company amortized \$2.9 million and \$3.0 million of capitalized software development costs, respectively. These costs are included in amortization and change in contingent consideration in the accompanying consolidated statements of operations. At December 31, 2010 and 2011, the unamortized software development costs included in property and equipment in the accompanying consolidated balance sheets were \$13.2 million and \$15.0 million, respectively.

(7) Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses at December 31, 2010 and 2011 and June 30, 2012 were comprised of the following (dollars in thousands):

	December 31,		June 30,
	2010	2011	2012
			(unaudited)
Accounts payable	\$ 1,214	\$ 910	\$ 1,543
Payable to benefit providers and transit agencies	7,908	6,491	17,121
Accrued payables	4,224	5,843	5,288
Accrued compensation and related benefits	6,378	6,926	7,651
Other accrued expenses	987	792	1,726
Deferred revenue	189	453	2,042
Accounts payable and accrued expenses	\$ 20,900	\$ 21,415	\$ 35,371

The increase in payable to benefit providers and transit agencies is due to the TransitChek acquisition.

(8) Debt**(a) Revolver**

On August 30, 2010, the Company entered into a Commercial Credit Agreement, or Revolver, with UB, to borrow an aggregate principal amount of up to \$15.0 million. In November 2011, the Company entered into an amendment to the Revolver with UB to increase the aggregate principal amount to \$50.0 million. The proceeds from this facility are primarily used to fund permitted acquisitions. The Company borrowed \$2.9 million during 2010 and \$12.1 million during 2011, and had \$35 million available under the Revolver as of December 31, 2011. The Company borrowed \$29.6 million during the unaudited three months ended March 31, 2012 and had UB issue a letter of credit for \$5.4 million related to a potential payment in 2012 for the TC acquisition. All of the Company's obligations under the credit facility are secured by substantially all of its property. All of the Company's existing and future subsidiaries are required to guaranty its obligations under the credit facility, other than certain non-material subsidiaries. Such guarantees by existing and future subsidiaries are and will be secured by substantially all of the property of such subsidiaries.

The interest rate for each draw for the Revolver is based on the London Interbank Offered Rate, or LIBOR, plus three percent. The interest rate at December 31, 2011 ranged from 3.42% to 3.54% and at June 30, 2012 ranged from 3.47% to 3.79% (unaudited). LIBOR loans may be prepaid, in whole or in part, upon five business days' notice to the lender and payment of a prepayment fee to the lender. Such prepayment fee is calculated as the present value of the difference between the return that the lender could obtain if it used the amount of such prepayment of principal to purchase regularly quoted securities issued by the United States at bid price, minus the return the lender would have received had the prepayment not been made. The Revolver has financial covenants including quick ratio, monthly minimum 3-month EBITDA coverage, and a quarterly cash flow

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coverage ratio. The Revolver also contains a covenant to provide audited financial statements within 90 days after each year end. To maintain availability of funds under the Revolver, the Company pays a commitment fee on the unused portion of the Revolver. The commitment fee is equal to one quarter of one percent (0.25%) per annum and is recorded as interest expense.

As of June 30, 2012, any obligations outstanding under the Revolver were due and payable on October 31, 2012. In September 2012, the Company entered into an amendment to extend the due date to October 31, 2013. See Note 16 for further detail on the amendment to extend the maturity date.

(b) Convertible Debt

On December 28, 2009, the Company entered into certain convertible note agreements, or Investor Notes, with several existing Preferred Stockholders for which it received proceeds of \$20 million. The Investor Notes were automatically convertible into Series E Preferred Stock at the earlier of (a) the next qualified financing or (b) April 2010. The April 2010 conversion date could be extended by agreement of the Company and the noteholders. The Investor Notes bore interest at 10% per annum and were repayable on January 2, 2011.

In connection with the issuance of the Investor Notes, the same Preferred Stockholders received warrants to purchase shares of Series E Preferred Stock (see Note 9). The Investor Warrants were valued at \$9.2 million, which was recorded as a discount to the Investor Notes. In addition, the Investor Notes contained a beneficial conversion feature in the amount of \$10.8 million, which was also recorded as a discount to the Investor Notes resulting in the carrying value of the Investor Notes initially being zero. Both discounts were then charged to interest expense through the contractual maturity date of January 2011.

No qualified financing occurred in 2010 and the automatic conversion date was extended through July 31, 2010. On July 31, 2010, the Investor Notes (including accrued interest of approximately \$1.2 million) were converted into 5,294,514 shares of Series E Preferred Stock and the Investor Warrants became exercisable to purchase shares of Series E-1 Preferred Stock (see Note 9). At the time of conversion, there remained an amount of approximately \$8.4 million of unamortized debt discount. This amount was recorded as incremental interest expense upon conversion. As a result, there are no incremental charges to interest expense related to these Investor Notes after July 31, 2010.

These amounts are included within interest expense in the accompanying consolidated statement of operations as follows (in thousands):

	Year Ended December 31,		
	2009	2010	2011
Noncash interest expense	\$ 16	\$ 1,162	\$
Beneficial conversion feature	30	10,770	
Warrant-related discount	25	9,175	
	\$ 71	\$ 21,107	\$

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements****(9) Warrants****(a) Warrant to Purchase Common Stock**

On September 27, 2007, the Company granted ORIX a warrant for 75,000 shares of Common Stock at a purchase price of \$8.20 per share in connection with a debt facility that was repaid in December 2009.

The warrant is exercisable, in whole or in part, for a period of seven years through September 26, 2014. The warrant does not entitle the holder to any voting rights or other rights as a stockholder of the Company prior to exercise. The fair value of the warrant was determined as approximately \$216,000 and was recorded as a debt discount. The Company was amortizing the fair value of the warrant over the life of the loan as interest expense. The Company recorded \$54,000 in interest expense in 2009. The unamortized balance at December 28, 2009 of \$95,000 was included as part of the debt extinguishment. The fair value of the warrant was determined using the Black-Scholes valuation model.

Assumptions used were as follows: fair value of the underlying stock of \$8.20; risk-free interest rate of 4.27%; term of 7.0 years; dividend of 0%; and volatility of 22%. This warrant is classified as equity.

(b) Lender Warrant

On May 23, 2005, the Company entered into a Senior Loan and Security Agreement, or Hercules Debt, with Hercules to borrow an aggregate principal amount of up to \$20 million. On September 27, 2007, the Company repaid the loan to Hercules. In connection with the Hercules Debt financing, the Company granted Hercules a warrant to purchase 423,529 shares of Series C Preferred Stock at a purchase price of \$4.25 per share. The warrant is exercisable, in whole or in part, for a period ending November 2013. The purchase price may be settled either by cash or by surrender of all or a portion of the warrant in exchange for shares of Series C Preferred Stock. The maximum number of preferred shares that the Company could be required to issue for settlement is 423,529. The warrant does not entitle the holder to any voting rights or other rights as a stockholder of the Company prior to exercise. The fair value of the warrant at December 31, 2011 was approximately \$1.1 million and is recorded as Warrants on the accompanying consolidated balance sheet.

The Company accounts for freestanding warrants, on shares that are redeemable, in accordance with ASC 480 pursuant to which any change in the fair value of the warrants is recorded in the consolidated statement of operations. The Company recorded a mark-to-market gain of \$0.1 million for the year ended December 31, 2009 and a mark-to-market loss of \$0.4 million for the year ended December 31, 2010 related to the change in fair value of these warrants. The Company recorded a mark-to-market gain of \$0.4 million for the year ended December 31, 2011 related to the change in fair value of these warrants.

Upon the automatic conversion of the Company's preferred stock into common stock in connection with the closing of the Company's IPO on May 15, 2012, the Lender Warrant became exercisable for 211,764 shares of common stock at a purchase price of \$8.50 per share. The Company performed the final re-measurement of the Lender Warrant at the closing date and the Lender Warrant was then reclassified from liability to equity. As the warrant is no longer exercisable into shares of redeemable preferred stock but into shares of common stock which is non-redeemable, the Company will no longer record any mark-to-market changes in the fair value of the warrant in the statements of operations. The fair value of the Lender Warrant at the final re-measurement date was approximately \$0.7 million (unaudited). The Company recorded a mark-to-market gain of \$0.4 million for the unaudited three and six months ended June 30, 2012. The Company recorded a mark-to-market gain of \$0.1 million and a loss of \$0.1 million for the unaudited three and six months ended June 30, 2011, respectively. This revaluation is included in other income (expense) as separate line item entitled Gain (loss) on revaluation of warrants. The warrant does not entitle the holder to any voting rights or other rights as a stockholder of the Company prior to exercise.

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The Company values the warrants using a Black-Scholes option pricing model, at each reporting date, which incorporates assumptions about underlying asset value, volatility, expected remaining life, and risk-free interest rate. These valuation adjustments are estimated based upon management's judgment about the general industry environment. The assumptions used at December 31, 2009, 2010 and 2011, respectively, were as follows:

	2009	December 31, 2010	2011
Fair value of underlying stock per share	\$ 5.14	\$ 7.34	\$ 6.31
Risk-free interest rate	1.56%	0.61%	0.22%
Expected term	3.5 years	2 years	1.75 years
Dividend yield	%	%	%
Volatility	56.40%	43.70%	50.40%

(c) Investor Warrants

Effective December 28, 2009, in connection with the Investor Notes described in Note 8(b) the Company granted to the instrument holders warrants, or Investor Warrants, to purchase \$20 million worth of Series E Preferred Stock (later amended to Series E-1 Preferred Stock see below.) The Investor Warrants are exercisable, in whole or in part, after the Automatic Conversion Date (originally April 30, 2010 and amended and extended to July 31, 2010) and expire on December 28, 2017 (later amended to June 30, 2014). All unexercised warrants upon expiration will automatically be exercised unless the Investor Notes holders provide written notice to the Company of their intent to have the warrants expire unexercised. The Investor Warrants do not entitle the holder to any voting rights or other rights as a stockholder of the Company prior to exercise.

At December 31, 2009, the Company accounted for the Investor Warrants as liabilities in accordance with ASC 480. This was due to the fact that these warrants were exercisable into a series of Preferred Stock that was redeemable. Any change in the fair value of the warrants at each reporting period was recorded in the consolidated statement of operations as a gain (loss) on revaluation of warrants. The initial fair value of the Investor Warrants was determined to be approximately \$9.2 million using an expected value approach based on the Noreen-Wolfson option pricing valuation model. Assumptions used were as follows: weighted fair value of the implied value of the underlying shares of \$3.98; weighted risk-free interest rate of 2.68%; weighted term of 6.1 years; dividend of 0%; and volatility of 48.40% determined by reference to the average asset volatility of comparable public companies. The initial fair value was recorded as a discount on the Investor Notes. The Company was amortizing the discount over the life of the Investor Notes as interest expense. The amount of the mark-to-market adjustment related to the Investor Warrants for the year ended December 31, 2009 was immaterial.

At July 30, 2010, the terms of the Investor Warrants were amended to allow for conversion to 8,733,617 Series E-1 Preferred Stock with an adjusted strike price of \$2.29 (the original strike price was \$2.40). The Series E-1 Preferred Stock is not redeemable and accordingly under ASC 480 and ASC 815 the Investor Warrants were determined to be equity classified and no longer classified as a liability. The fair value of the warrants at July 30, 2010 was determined to be \$14.2 million and was determined using an expected value approach based on the Noreen-Wolfson option pricing valuation model. Assumptions used were as follows: weighted fair value of the implied value of the underlying shares of \$3.42; weighted risk-free interest rate of 0.84%; weighted term of 2.89 years; dividend of 0%; and volatility of 66.10% determined by reference to the average asset volatility of comparable public companies. As a result of the valuation, the Company recorded a mark-to-market loss of \$5.0 million for the year ended December 31, 2010 related to the change in fair value of these warrants. This revaluation was recorded in the consolidated statement of operations as a gain (loss) on revaluation of warrants.

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Upon the automatic conversion of the Company's preferred stock into common stock in connection with the closing of the Company's IPO on May 15, 2012, the Investor Warrants became exercisable for 4,366,803 shares of common stock.

(10) Redeemable and Convertible Preferred Stock

Upon the closing of the IPO in May 2012, all outstanding redeemable and convertible preferred stock was converted into shares of common stock which are non-redeemable as shown below. The Company performed the final re-measurement of the redemption value of the redeemable preferred stock at the date when redemption was no longer probable and the redeemable preferred stock was then reclassified from the mezzanine level of the consolidated balance sheet into equity. Subsequent to this date, the Company will no longer record accretion of redeemable preferred shares. The convertible preferred stock was converted into shares of common stock at the following contractual conversion ratios:

	Shares Outstanding	Number of Shares of Common Stock Received Upon Conversion
Series A	50,000	42,603
Series A-1	1,725,792	2,537,916
Series A-2	998,661	850,923
Series B	14,870,179	7,435,088
Series C	5,882,353	2,941,171
Series D	2,465,514	1,232,659
Series E	5,294,514	2,647,252

As of the closing date of the IPO, no dividends were ever declared or paid.

On July 30, 2010, the certificate of incorporation was amended to authorize the issuance of 40.5 million shares of Preferred Stock. The Preferred Stock was divided into series with 50,000 shares designated as Series A Preferred Stock, 1.7 million shares designated as Series A-1 Preferred Stock, 1.0 million shares designated as Series A-2 Preferred Stock, 14.9 million shares designated as Series B Preferred Stock, 6.3 million shares designated as Series C Preferred Stock, 2.5 million shares designated as Series D Preferred Stock, 5.3 million shares designated as Series E Preferred Stock, and 8.7 million shares designated as Series E-1 Preferred Stock.

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As of December 31, 2011 and March 31, 2012, the rights, preferences, and privileges of the holders of Preferred Stock were as follows:

(a) Dividends

The holders of Series A, A-1, A-2, B, C, D, E, and E-1 Preferred Stock were entitled to receive noncumulative dividends (as adjusted for any stock dividends, combinations, or splits with respect to such shares) annually payable out of funds legally available, when and if declared by the board of directors as follows:

Preferred stock	Dividend rates
Series A	\$ 0.3200
Series A-1	0.3200
Series A-2	0.3200
Series B	0.1120
Series C	0.3400
Series D	0.5192
Series E	0.3200
Series E-1	0.1800

Payment of Series A, A-1, A-2, B, C, D, E, and E-1 dividends were to be paid prior to payment of any dividends on the Common Stock.

As of December 31, 2011 and March 31, 2012, no dividends had been declared or paid.

(b) Liquidation

In the event of any liquidation, the holders of Series E and Series E-1 Preferred Shares were entitled to a preference on liquidation equal to \$4.00 and \$2.29 per share, respectively (as adjusted for any stock dividends, combinations, or splits with respect to such shares), plus declared but unpaid dividends prior to any payments to the Series A, A-1, A-2, B, C, and D Preferred Stock, or the Common Stock holders.

In the event of any liquidation, the holders of Series D were entitled to a preference on liquidation equal to \$6.49 per share (as adjusted for any stock dividends, combinations, or splits with respect to such shares) plus declared but unpaid dividends prior to any payments to the Series A, A-1, A-2, B, and C Preferred Stock, or the Common Stock holders.

In the event of any liquidation, the holders of Series C were entitled to a preference on liquidation equal to \$4.25 per share (as adjusted for any stock dividends, combinations, or splits with respect to such shares) plus declared but unpaid dividends prior to any payments to the Series A, A-1, A-2, and B Preferred Stock, or the Common Stock holders.

In the event of any liquidation, the holders of Series B were entitled to a preference on liquidation equal to \$1.40 per share (as adjusted for any stock dividends, combinations, or splits with respect to such shares) plus declared but unpaid dividends prior to any payments to the Series A, A-1, and A-2 Preferred Stock, or the Common Stock holders.

In the event of any liquidation, the holders of Series A, A-1, and A-2 Preferred Stock were entitled to a preference on liquidation equal to \$4.00 per share (as adjusted for any stock dividends, combinations, or splits with respect to such shares) plus declared but unpaid dividends prior to any payments to the Common Stock holders.

All further remaining proceeds would have been distributed ratably to the Common Stock holders and the Series A, A-1, A-2, B, C, D, E, and E-1 stockholders on an as-converted basis, provided that the distributions

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described above on the shares of Series A, A-1, A-2, B, C, D, E, and E-1 Preferred Stock are capped at \$14.14, \$21.50, \$14.14, \$7.35, \$10.20, \$12.98, \$8.00, and \$4.58, respectively. Should the distributions have been capped, each series of Preferred Stock was convertible to Common Stock at the election of the holder thereof.

(c) Conversion

Each share of Series A, A-1, A-2, B, C, D, E, and E-1 was to be converted to shares of Common Stock at a conversion ratio as outlined in the table below.

Preferred stock class	Conversion ratio
Series A	0.85
Series A-1	1.47
Series A-2	0.85
Series B	0.50
Series C	0.50
Series D	0.50
Series E	0.50
Series E-1	0.50

Each share of Series A, A-1, A-2, B, C, D, E, and E-1 was to be automatically converted to shares of Common Stock immediately prior to the earlier to occur of (i) the closing of a firm commitment, underwritten public offering registered under the Securities Act of 1933, in which the net proceeds to the Company from the sale of the Company's Common Stock is \$40 million or greater, and the offering price per share is at least \$20.78 (as adjusted for any stock dividends, combinations, or splits with respect to such shares), or Qualified IPO, or (ii) the effective date upon which a defined voting percentage, as outlined below, of the outstanding shares of such indicated class voting as a class, approve such conversion.

Preferred stock class	Defined voting percentage
Series A	Majority of Series B
Series A-1	Majority of Series B
Series A-2	Majority of Series B
Series B	Majority of Series B
Series C	Majority of Series C
Series D	Majority of Series D
Series E	80.8% of Series E
Series E-1	80.8% of Series E

Each series of Preferred Stock was convertible to Common Stock at the election of the holder thereof.

All Preferred Stock was entitled to proportional adjustments for stock splits, stock dividends, and the like.

(d) Redemption

Series A Preferred Stock, Series A-1 Preferred Stock, Series A-2 Preferred Stock, Series B Preferred Stock, and Series E-1 Preferred Stock were not redeemable. Series C, D, and E Preferred Stock were redeemable, at any time after December 31, 2012 if, prior to such date, the Company had not consummated a Qualified IPO, (i) the holders of not less than a majority of the issued and outstanding Series C Preferred Stock requested, by written notice, that the Company redeem all shares of Series C Preferred Stock then held by such holders and/or (ii) the

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holders of not less than a majority of the issued and outstanding Series D Preferred Stock requested, by written notice, that the Company redeem all shares of Series D Preferred Stock then held by such holders and/or (iii) the holders of not less than a majority of the issued and outstanding Series E Preferred Stock requested, by written notice, that the Company redeem all shares of Series E Preferred Stock then held by such holders.

The redemption price per share was to be payable in cash and shall be equal to the greater of (i) the fair market value of such shares as determined in good faith by an appraiser of national standing chosen by the redeeming preferred stockholders that is satisfactory to the Company or (ii) \$4.25 per share, with respect to Series C Preferred Stock, \$6.49 per share, with respect to Series D Preferred Stock and \$4.00 per share, with respect to Series E Preferred Stock (each as adjusted for any stock dividends, combinations, or splits with respect to such shares).

The Company recorded accretion related to this redemption premium, using the interest method, as an increase or decrease to the liquidation value of the redeemable Preferred Stock and a decrease or increase to additional paid-in capital based on the excess of the estimated fair value of each redeemable Preferred Stock, as determined by the Company, over the stated minimum redemption price per share for each redeemable Preferred Stock over the period of time up to the redemption date. The Company recorded the following dividend amounts for each redeemable Preferred Stock in 2009, 2010 and 2011 (in thousands):

	Series C	Series D	Series E
Redemption value at December 31, 2009	\$ 30,984	\$ 17,059	\$
Conversion of investor notes and accrued interest			21,178
Accretion of preferred stock	3,823	888	2,028
Redemption value at December 31, 2010	34,807	17,947	23,206
Accretion of preferred stock	1,763	(176)	4,622
Redemption value at December 31, 2011	\$ 36,570	\$ 17,771	\$ 27,828

The Company estimated the remaining aggregate accretion to be recorded over the remaining redemption period was approximately \$4.0 million at December 31, 2011. Upon the completion of the Company's IPO in May 2012, the redeemable preferred shares converted to common shares that are not redeemable. The Company performed the final re-measurement of the redeemable preferred stock at the date when redemption was deemed not probable and recorded \$0.7 million of accretion of redemption premium expense. The preferred stock was then reclassified from the mezzanine to equity. Subsequent to this date, the Company will no longer record accretion of redeemable preferred shares.

(e) Voting Rights

All holders of Preferred Stock were entitled to vote on an as-converted basis.

(f) Anti-Dilution Protection

Subject to the following paragraphs below, each series of Preferred Stock was entitled to weighted average anti-dilution protection for issuances of Company securities at a price per share that was less than the conversion price then in effect for such series.

(g) Protective Provisions

Approval of the holders of a majority of Series A, A-1, A-2, B, and C Preferred Stock voting together as a single class was required on the following matters: (i) create a non wholly owned subsidiary; (ii) voluntary

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liquidation, winding-up, or dissolution; (iii) amendment of any stock option or stock purchase plan to modify the number of shares covered thereby; (iv) increase number of directors above nine; (v) any change to counsel or auditors; (vi) any material change in the nature of the Company's business; (vii) declare, pay, or make any dividend or distribution on any shares of Common Stock; (viii) redeem, purchase, or acquire any shares of Common Stock; and (ix) sell any material assets or grant any exclusive license to intellectual property outside the ordinary course if the value of such assets or rights, when aggregated with all other such transfers in the preceding 12 months would meet certain materiality thresholds.

Approval of the holders of a majority of Series A, A-1, A-2, and B Preferred Stock voting together as a single class was required on the following matters: (i) create, designate, authorize, or issue any security that is senior to, or on par with, any such securities with respect to voting, dividends, and liquidation; or (ii) amend or repeal the Certificate of Incorporation or Bylaws in a manner that disproportionately affects such securities relative to other series of Preferred Stock.

Approval of the holders of a majority of Series C Preferred Stock voting together as a single class was required on the following matters: (i) create, designate, authorize, or issue any security that is senior to, or on par with, such securities with respect to voting, dividends, and liquidation; (ii) agree to any liquidation event that would result in a liquidation preference to the Series C of less than \$5.6525 per share; (iii) increase number of directors above nine; (iv) amend or repeal the certificate of incorporation or bylaws in a manner that materially adversely changes the rights of such securities; (v) declare, pay, or make any dividend or distribution on any shares of Common Stock or Preferred Stock; (vi) redeem, purchase, or acquire any shares of Common Stock or Preferred Stock; (vii) incur debt that results in aggregate outstanding indebtedness in excess of \$25 million; or (viii) engage in certain related-party transactions.

Approval of the holders of a majority of Series D Preferred Stock voting together as a single class was required to amend or repeal the Certificate of Incorporation or Bylaws in a manner that materially adversely changes the rights of the Series D Preferred Stock in a manner that disproportionately affects such securities relative to other series of Preferred Stock.

Approval of the holders of a majority of Series E Preferred Stock voting together as a single class was required to amend or repeal the Certificate of Incorporation or Bylaws in a manner that materially adversely changes the rights of the Series E Preferred Stock or the Series E-1 Preferred Stock in a manner that disproportionately affects any such securities relative to other series of Preferred Stock.

(h) Investor Notes

On December 28, 2009, the Company entered into Investor Notes with preferred shareholders holding more than 90% of the preferred shares to borrow an aggregate principal amount of \$20 million. Under the Agreement, each investor received a note. Each investor also received a warrant to purchase Series E Preferred Stock (see Note 9). The interest on the notes was accrued but was unpaid and converted with the Investor Notes on the conversion date. On July 31, 2010, the Investor Notes converted into Series E Preferred Stock under the automatic conversion date provision.

(11) Common Stock***(a) Initial Public Offering (unaudited)***

On May 15, 2012, the Company closed its IPO. In connection with the IPO, the Company sold 7,475,000 shares of common stock to the public at a price of \$9.00 per share, which included 975,000 shares of common

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WAGWORKS, INC.

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stock from the full exercise of the overallotment option of shares granted to the underwriters. The Company received aggregate proceeds of \$62.6 million from the initial public offering and the underwriters' overallotment option, net of underwriters' discounts and commissions.

Additionally, the Company incurred aggregate offering costs of \$5.5 million related to the IPO. The aggregate proceeds from the IPO have been recorded in stockholders' equity, net of the offering costs, which have been reclassified from prepaid expenses and other current assets and offset against additional paid-in capital.

Upon the closing of the IPO, the Company's certificate of incorporation and bylaws and the stockholder agreement between the Company and VantagePoint, provide for a number of board of directors, stockholder and related governance matters. Funds affiliated with VantagePoint, own approximately 50.8% of the Company's outstanding common stock at June 30, 2012.

The following actions by the Company will require the approval of VantagePoint for so long as VantagePoint owns at least 25% or more of the Company's outstanding shares of common stock: (i) any amendment of the Company's bylaws; (ii) the issuance of any securities with economic rights senior to the Company's common stock or with voting rights different than the Company's common stock, subject to certain exceptions; (iii) the incurrence or guarantee of any debt in excess of \$20.0 million; (iv) the issuance of equity or debt, or any securities convertible into equity or debt, for consideration in excess of 12.5% of the Company's market capitalization (as determined by the average trading price of the Company's common stock over the 30 trading days prior to approval by the Company's board of directors of such issuance); (v) the acquisition or disposition of stock or assets, including through a license or lease, for consideration in excess of 12.5% of the Company's market capitalization (as determined by the average trading price of the Company's common stock over the 30 trading days prior to approval by the Company's board of directors of such transaction); (vi) the adoption of a stockholder rights plan; (vii) the approval of any golden parachute or other compensatory plan contingent upon a change in control of the Company for any of the Company's executive officers valued in excess of \$1.0 million for an individual officer or \$5.0 million for a group of officers, at the time such compensatory arrangement is adopted; and (viii) any change in the number of authorized directors.

Amendments or modifications of the Company's certificate of incorporation and bylaws relating to VantagePoint's rights can occur only with the approval of VantagePoint. VantagePoint and its representatives will have access to the Company's books and records, subject to customary confidentiality and non-disclosure provisions and so long as VantagePoint owns more than 30% of the Company's outstanding voting stock, a special meeting of the Company's stockholders may be called by either VantagePoint or any two members of the Company's board of directors, whether or not VantagePoint designees. So long as VantagePoint owns at least 40% of the Company's outstanding voting stock, the Company's stockholders may act by written consent to change the number of authorized directors, remove a director without cause or fill a vacancy on the Company's board of directors.

VantagePoint will have the right to designate (and remove or replace) three members of the Company's board of directors if VantagePoint owns at least 50% or more of the Company's outstanding shares. VantagePoint will continue to have a right to designate (and remove or replace) two members of the Company's board of directors if VantagePoint owns between 20% and 50% of the Company's outstanding shares and will have a right to designate (and remove or replace) one member of the Company's board of directors if VantagePoint owns between 10% and 20% of the Company's outstanding shares. VantagePoint shall also have the right to select one of its board designees to serve on the Company's compensation committee, the Company's nominating and corporate governance committee and any other special committee of the Company's board of directors so long as it continues to hold at least 10% of the Company's outstanding shares.

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(b) Authorized Shares

On May 15, 2012, the certificate of incorporation was amended to authorize the issuance of 1.1 billion shares of capital stock. The total number of shares of common stock authorized was 1.0 billion shares.

(c) Dividends

Subject to the prior rights of the holders of all classes of stock having prior rights as to dividends, the holders of the Common Stock are entitled to receive out of any assets of the Company legally available, such dividends as may be declared from time to time by the board of directors.

(d) Liquidation

Upon the liquidation, dissolution, or winding up of the Company, the assets of the Company shall be distributed as provided in the amended and restated certificate of incorporation.

(e) Redemption

The Common Stock shall not be redeemable other than by the repurchase of shares of Common Stock by the Company from employees, officers, directors, consultants or other persons performing services for the Company pursuant to agreements under which the Company has the option to repurchase such shares at cost upon the occurrence of certain events, such as the termination of employment. As of December 31, 2011 and June 30, 2012, there are currently no shares outstanding where the Company has such an option.

(e) Voting Rights

The holders of each share of Common Stock shall have the right to one vote, and shall be entitled to notice of any stockholders' meeting in accordance with the Bylaws of the Company, and shall be entitled to vote upon such matters and in such manner as may be provided by law.

(12) Employee Benefit Plans

(a) Employee Stock Option Plan

The Company's stock option program is a long-term retention program that is intended to attract, retain, and provide incentives for talented employees, officers, and directors, and to align stockholder and employee interests. The Company considers its option program critical to its operation and productivity.

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Stock-based compensation is classified in the consolidated statement of operations in the same expense line items as cash compensation. In accordance with ASC 718, the Company recorded \$2.5 million, \$2.4 million and \$2.2 million of stock-based compensation expense in its consolidated statements of operations for the years ended December 31, 2009, 2010 and 2011, respectively, relating to options and \$0.6 million and \$1.1 million for the unaudited three months ended June 30, 2011 and 2012, respectively. The Company recorded \$1.2 million and \$1.7 million of stock-based compensation expense for the unaudited six months ended June 30, 2011 and 2012, respectively. None of the stock-compensation cost was capitalized as amounts were immaterial. Amounts recorded as expense in the consolidated statement of operations are as follows (in thousands):

	2009	Year Ended December 31,		Three Months Ended June 30,		Six Months Ended June 30,	
		2010	2011	2011 (unaudited)	2012 (unaudited)	2011 (unaudited)	2012 (unaudited)
Cost of revenue	\$ 373	\$ 312	\$ 219	\$ 59	\$ 104	\$ 123	\$ 151
Technology and development	323	282	256	67	79	134	137
Sales and marketing	461	422	391	104	136	213	224
General and administration	1,353	1,388	1,378	345	796	729	1,162
Total	\$ 2,510	\$ 2,404	\$ 2,244	\$ 575	\$ 1,115	\$ 1,199	\$ 1,674

As of December 31, 2011, there was \$3.3 million of total unrecognized compensation cost related to nonvested stock-based employee compensation arrangements that is expected to vest. The cost is expected to be recognized over a weighted average period of 3.28 years, as of December 31, 2011.

The Company's 2000 Stock Option/Stock Issuance Plan adopted in June 2000, as amended and restated, or the 2000 Plan, provides for the issuance of options and other stock-based awards. On May 6, 2010, the shares of Common Stock reserved for issuance under the 2000 Plan were increased by 298,602 shares to 5.1 million shares and the plan was terminated in June 2010. The Company issues new shares upon the exercise of stock options. Any forfeitures or shares remaining under the plan are canceled and not available for reissue.

The Company's 2010 Equity Incentive Plan was adopted on May 26, 2010, or the 2010 Plan, and the Company initially reserved for issuance under the 2010 Plan 0.8 million shares with an automatic annual increase on the first day of each of the Company's fiscal years beginning in 2011 by an amount equal to the lesser of 1,500,000 shares, 3% of the outstanding shares of the Company's common stock as of the last day of the Company's immediately preceding fiscal year, or such other amount as the Company's board of directors may determine. Options become vested and exercisable at such times and under such conditions as determined by the board of directors. In January 2011, the shares of Common Stock reserved for issuance under the 2010 Plan were increased by 192,195 shares.

Options under the 2000 and the 2010 Plan, or the Plans, are generally for periods not to exceed 10 years and must be issued at prices not less than 85% of the estimated fair value of the shares of Common Stock on the date of grant as determined by the plan administrator. Options become vested and exercisable at such times and under such conditions as determined by the board of directors. Options generally vest over four years with 25% vesting after one year and the balance vesting monthly over the remaining period. In May and November 2010, the Company granted a total of 418,500 performance option awards to certain executives of the Company. During the three months ended March 31, 2012, the Company granted a total of 320,000 (unaudited) performance option awards to certain executives of the Company. No performance option awards were granted during the three months ended June 30, 2012. The performance option awards are subject to potential early vesting based upon the achievement of certain milestones as follows: 25% to vest upon an initial public offering, 25% to vest upon achieving a revenue growth rate of at least 8% per year for two consecutive years, and an additional 50% will vest upon the achievement on an initial public offering and achieving consecutive growth rates.

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The following table summarizes the weighted-average fair value of stock options granted:

	Year Ended December 31,			Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2010	2011	2011 (unaudited)	2012 (unaudited)	2011 (unaudited)	2012 (unaudited)
Stock options granted (in thousands)	924	1,137	139	32	79	138	871
Weighted average fair value at date of grant	\$ 2.83	\$ 2.88	\$ 6.09	\$ 6.42	\$ 5.46	\$ 6.09	\$ 5.35

Stock option activity for the year ended December 31, 2011 and the six months ended June 30, 2012 is as follows (shares in thousands):

	Shares	Weighted average exercise price	Remaining contractual term (years)	Aggregate intrinsic value (dollars in thousands)
December 31, 2010	4,507	\$ 7.16	7.51	\$ 17,213
Granted	139	11.24		
Exercised	(20)	1.33		
Forfeited	(86)	7.89		
Outstanding as of December 31, 2011	4,540	\$ 7.29	6.62	\$ 10,888
Vested and expected to vest at December 31, 2011	4,327	\$ 7.28	6.54	\$ 10,008
Exercisable at December 31, 2011	4,540	\$ 7.29	6.62	\$ 10,888
Granted	871	9.69		
Exercised	(8)	1.00		
Forfeited	(160)	7.86		
Outstanding as of June 30, 2012 (unaudited)	5,243	\$ 7.68	6.72	\$ 38,665

The total intrinsic value of options exercised during the years ended December 31, 2009, 2010 and 2011 was \$273,000, \$33,375, and \$161,000, respectively. The Company received \$20,200, \$5,000, and \$25,700 of cash upon the exercise of these options for the years ended December 31, 2009, 2010 and 2011, respectively. The Company also recorded \$80,000, \$1,300, and \$64,000 in tax benefits as a result of the exercise of these options for the years ended December 31, 2009, 2010 and 2011, respectively.

The Plans provides for grants of immediately exercisable options; however, the Company has the right to repurchase any unvested Common Stock upon the termination of employment at the original exercise price. There were no early exercises and the Company did not repurchase any unvested Common Stock during 2009, 2010 or 2011.

(b) Valuation Assumptions

The Company calculated the fair value of each option award on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions (annualized percentages):

December 31,

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	2009	2010	2011
Fair value of underlying stock per share	\$6.14-7.42	\$5.32-6.18	\$10.98-12.10
Expected volatility	47.0%	46.0-50.9%	54.72-56.09%
Risk-free interest rate	2.13-2.72%	1.13-3.12%	2.18-2.72%
Expected term	4.95-6.06 years	5.26-8.50 years	5.47-6.08 years
Dividend yield	0.00%	0.00%	0.00%

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	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2012	2011	2012
	(unaudited)		(unaudited)	
Fair value of underlying stock per share	\$12.10	\$10.66	\$10.98-12.10	\$9.59-10.66
Expected volatility	54.72-54.77%	54.63-54.75%	54.72-56.09%	54.63-56.14%
Risk-free interest rate	2.18-2.23%	0.95-0.98%	2.18-2.72%	0.94-1.74%
Expected term	5.90-6.07 years	5.94-6.08 years	5.47-6.08 years	5.27-8.50 years
Dividend yield	0.00%	0.00%	0.00%	0.00%

The determination of the fair value of stock-based awards on the date of grant using an option pricing model is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables. Expected volatility is determined using average volatility of peer publicly traded companies. The risk-free interest rate is determined by using published zero coupon rates on treasury notes for each grant date given the expected life. The dividend yield of zero is based on the fact that the Company expects to invest cash in operations and has never paid cash dividends on Common Stock. The Company changed its method of estimating expected term in 2010 from using historical exercises to the simplified method as determined under SAB 107 due to the low frequency of option exercises.

As stock-based compensation expense recognized in the consolidated statements of operations in 2009, 2010 and 2011 is based on awards ultimately expected to vest, it is reduced for estimated prevest forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In addition, ASC 718 requires that compensation cost recognized at any date must be at least equal to the amount attributable to options that are vested at that date. The Company calculates a true-up of its compensation costs to the vested amounts on a quarterly basis. Prevesting forfeitures were estimated to be approximately nine percent in 2009 and approximately eight percent in 2010 and 2011 based on weighted average historical forfeiture rates. Under the provisions of ASC 718, the Company will record additional expense if the actual forfeiture rate is lower than estimated, and will record a recovery of prior expense if the actual forfeiture rate is higher than estimated.

(c) Restricted Stock Agreements

The Company issues stock under purchase agreements, which includes stock pursuant to the Company's option plans, which include restrictions on the transfer of the Company's Common Stock. Before selling Common Stock, the stockholder must first offer the Company the right of first refusal. In the event of a voluntary or involuntary termination (including death and disability), the Company has the right to repurchase the exercised unvested shares at the original price paid. The Company had no exercised and unvested shares in 2009, 2010 and 2011.

The Company has a co-sale agreement, which includes restrictions on the transfer of the Company's Common Stock issued pursuant to the Company's stock purchase agreement. Before selling Common Stock, the stockholder must first offer the Company the right of first refusal. The Company did not exercise these rights for the years ended December 31, 2009, 2010 and 2011.

(d) Employee Stock Purchase Plan

Concurrent with the closing of the Company's IPO in May 2012, the Company established the 2012 Employee Stock Purchase Plan (ESPP) which is intended to qualify under Section 423 of the Internal Revenue Code of 1986. The Company's executive officers and all of its other employees are allowed to participate in the ESPP. A total of 500,000 shares of the Company's common stock was made available for sale under the ESPP.

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WAGWORKS, INC.

Notes to Consolidated Financial Statements

In addition, the ESPP provides for annual increases in the number of shares available for issuance under the ESPP on the first day of each fiscal year beginning with the 2012 fiscal year, equal to the least of:

500,000 shares of common stock;

1% of the outstanding shares of the Company's common stock as of the last day of the Company's immediately preceding fiscal year; or

such other amount as may be determined by the board.

Under the ESPP, employees are eligible to purchase common stock through payroll deductions of up to 25% of their eligible compensation, subject to any plan limitations. The ESPP has four consecutive offering periods of approximately three months in length during the year and the purchase price of the shares will be 85% of the lower of the fair value of the Company's common stock on the first trading day of the offering period or on the last day of the offering period.

(e) 401(k) Plan

The Company participates in the WageWorks 401(k) Plan, or 401(k) Plan, a tax-deferred savings plan covering all of its employees working more than 1,000 hours per year. Employees become participants in the 401(k) Plan on the first day of any month following the first day of employment. Eligible employees may contribute up to 85% of their compensation to the 401(k) Plan, limited to the maximum allowed under the Internal Revenue Code, or the Code. The Company, at its discretion, may match up to 25% of the first 4% of employees' contributions and may make additional contributions to the 401(k) Plan. The Company contributed approximately \$255,000, \$292,000 and \$312,000 in 2009, 2010 and 2011, respectively and \$361,000 in the unaudited six months ended June 30, 2012.

(13) Income Taxes

The Company provides for income taxes using an asset and liability approach, under which deferred income taxes are provided based upon enacted tax laws and rates applicable to periods in which the taxes become payable.

The Company follows FASB ASC 740-270, Income Taxes - Interim Reporting, for the computation and presentation of its interim period tax provision. Accordingly, management estimated the effective annual tax rate and applied this rate to the year-to-date pre-tax book income to determine the interim provision for income taxes.

Loss before income taxes for the years ended December 31, 2009 and 2010 and profit before income taxes for the year ended December 31, 2011 was all incurred in the United States of America.

The income tax provision for the three months ended June 30, 2011 and 2012 was \$0.3 million and \$1.6 million, respectively, and the income tax provision for the six months ended June 30, 2011 and 2012 was \$0.4 million and \$3.0 million, respectively. The change is primarily due to having no valuation allowance as of June 30, 2012 compared to having a full valuation allowance as of June 30, 2011. The tax provision for the three months and six months ended June 30, 2012 includes a discrete deferred tax benefit of \$0.5 million related to the increase of federal income tax rate from 34% to 35% due to an increase in estimated taxable future earnings.

The Company is subject to income taxes in the U.S. federal and various state jurisdictions. Presently, there is no income tax examination going on in the jurisdictions where the Company operates.

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As of June 30, 2012, the Company remains in a net deferred tax asset position. The realization of the Company's deferred tax assets depends primarily on its ability to generate sufficient U.S. taxable income in future periods. The amount of deferred tax assets considered realizable may increase or decrease in subsequent quarters as management reevaluates the underlying basis for the estimates of future domestic taxable income.

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Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements**

The components of the provision for income taxes for the years ended December 31, 2009, 2010 and 2011 are as follows (dollars in thousands):

	2009	2010	2011
Current:			
Federal	\$ 48	\$	\$
State	(97)	(130)	(330)
	(49)	(130)	(330)
Deferred:			
Federal	(423)	1,404	17,854
State	(23)	(70)	2,344
	(446)	1,334	20,198
Total (provision) benefit for income taxes	\$ (495)	\$ 1,204	\$ 19,868

Deferred tax assets (liabilities) as of December 31, 2010 and 2011 consist of the following (dollars in thousands):

	2010	2011
Deferred tax assets:		
Current:		
Prepays	\$ 373	\$
Accruals and reserves	2,571	1,291
Deferred tax assets - current	2,944	1,291
Noncurrent:		
Net operating loss carryforwards	22,002	17,139
Stock-based compensation	2,750	3,534
R&D and other credits	1,137	1,261
Property and equipment	1,009	1,000
Reserves - noncurrent		525
Other	57	
Deferred tax assets - noncurrent	26,955	23,459
Gross deferred tax assets	29,899	24,750
Valuation allowance	(25,931)	
Total deferred tax assets	3,968	24,750
Deferred tax liabilities:		
Noncurrent		

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Intangibles	(3,968)	(4,065)
Goodwill	(1,929)	(2,416)
Gross deferred tax liabilities	(5,897)	(6,481)
Net deferred tax assets and liabilities:		
Net deferred tax liabilities	\$ (1,929)	\$
Net deferred tax assets - current		1,291
Net deferred tax assets - noncurrent		16,978
Total net deferred tax assets		\$ 18,269

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(Continued)

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements**

The current portion of net deferred tax assets is included in the prepaid expenses and other current assets line item in the consolidated balance sheets.

Reconciliation of the statutory federal income tax rate to the Company's effective tax rate for the years ended December 31, 2009, 2010 and 2011:

	2009	2010	2011
Tax provision (benefit) at U.S. statutory rate	(34)%	(34)%	34%
State income taxes, net of federal benefit	8	4	4
Warrants	(17)	31	(1)
Permanent items	34		8
R&D credits	(59)		(1)
Change in valuation allowance	424	(8)	(193)
Other			1
Provision (benefit) for tax	356%	(7)%	(148)%

The Company's accounting for deferred taxes involves the evaluation of a number of factors concerning the realizability of the Company's deferred tax assets. Assessing the realizability of deferred tax assets is dependent upon several factors, including the likelihood and amount, if any, of future taxable income in relevant jurisdictions during the periods in which those temporary differences become deductible. The Company's management forecasts taxable income by considering all available positive and negative evidence including its history of operating income or losses and its financial plans and estimates which are used to manage the business. These assumptions require significant judgment about future taxable income. The amount of deferred tax assets considered realizable is subject to adjustment in future periods if estimates of future taxable income are reduced.

The Company provided a valuation allowance for all of its net deferred tax assets as of December 31, 2010 due to the uncertainty regarding their future realization.

In the fourth quarter of fiscal year 2011, the Company's management determined that the positive evidence of taxable income coupled with its forecasted profitability outweighed the negative evidence of prior losses. The Company deferred action on the release of the valuation allowance until the fourth quarter of 2011 when it had visibility into its 2012 enrollment levels, including enrollment and a full year of results from the Company's 2010 portfolio purchases. The Company believes this information provides the basis for reliable forecasts of 2012 pre-tax income due to the fixed monthly fees that form the majority of its revenue. Accordingly, in the fourth quarter of 2011, the Company released the valuation allowance on its deferred tax assets. Accordingly, in the fourth quarter of fiscal year 2011, the Company released \$25.9 million of the valuation allowance on its deferred tax assets, primarily related to its federal deferred tax assets.

Any subsequent increases in the valuation allowance will be recognized as an increase in deferred tax expense. Any decreases in the valuation allowance will be recorded either as a reduction of the income tax provision or as a credit to paid-in capital if the associated deferred tax asset relates to windfall stock option deductions on the exercise of stock options.

At December 31, 2011, unrecognized tax benefits approximated \$2.3 million, which would impact the provision if recognized. Included in the balance at December 31, 2011 is \$0.3 million of current year tax positions, which would affect the Company's income tax expense if recognized. As of December 31, 2011, the Company has no uncertain tax positions that would be reduced as a result of a lapse of the applicable statute of limitations in the following year. The Company does not anticipate that any adjustments would result in a

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements**

material change to its financial position. For the years ended December 31, 2009, 2010 and 2011, the Company did not recognize interest or penalties related to unrecognized tax benefits. A reconciliation of the beginning and ending balances of the total amounts of gross unrecognized tax benefits is as follows:

	Year ended December 31,		
	2009	2010	2011
	(In thousands)		
Balance, beginning of year	\$ 1,434	\$ 1,630	\$ 1,994
Increase in tax positions for prior years		117	24
Decrease in tax positions for prior years			
Settlements			
Lapse in statute of limitations			
Increase in tax positions for current year	196	247	303
Balance, end of year	\$ 1,630	\$ 1,994	\$ 2,321

The Company files income tax returns in the U.S. federal jurisdiction and various states jurisdictions. As a result of the Company's net operating loss carryforwards, the 2000 through 2010 tax years are open and may be subject to potential examination in one or more jurisdictions.

At December 31, 2011, the Company had federal and state operating loss carryforwards of approximately \$47.9 million and \$38.9 million, respectively, available to offset future regular and alternative minimum taxable income. The Company's federal net operating loss and tax credit carryforwards expire in the years 2023 through 2029 and 2022 through 2031, respectively, if not utilized. The state net operating loss carryforwards expire in the years 2012 through 2031. The federal amount includes tax deductions benefits related to stock options in the amount of \$3.8 million that will be booked to additional paid-in capital and that will benefit the tax provision when utilized.

The Company also has tax deductible goodwill related to asset acquisitions. When the Company utilizes these loss carryforwards, a portion of these amortization deductions will be booked to goodwill and will not benefit the tax provision. The cumulative amount of amortization deductions through 2011 is \$6.6 million, of which \$200,000 relates to amounts that will be booked to goodwill and will not benefit the tax provision.

In addition, the Company had federal and California research and development credit carryforwards of approximately \$2.6 million and \$1.1 million respectively, available to offset future tax liabilities. The federal research credit carryforwards expire beginning in the years 2022 through 2031, if not fully utilized. The California tax credit carryforward can be carried forward indefinitely.

The Company's ability to utilize the net operating losses and tax credit carryforwards in the future may be subject to a reduction in the event of future ownership changes as defined in Section 382 of the Code and similar state tax law.

(14) Commitments and Contingencies**(a) Operating Leases**

The Company leases office space and equipment under noncancelable operating leases with various expiration dates through 2015.

Table of Contents**WAGWORKS, INC.****Notes to Consolidated Financial Statements**

Future minimum lease payments under noncancelable operating leases are as follows (dollars in thousands):

	Operating leases As of December 31, 2011
2012	\$ 4,551
2013	3,378
2014	2,554
2015	1,354
2016	
Thereafter	
Total minimum lease payments	\$ 11,837

Rent expense in 2009, 2010 and 2011 was \$2.5 million, \$2.3 million and \$3.2 million, respectively. Rent expense in the unaudited three months ended June 30, 2011 and 2012 was \$0.8 million and \$1.1 million, respectively, and \$1.6 million and \$2.3 million for the unaudited six months ended June 30, 2011 and 2012, respectively.

(b) Legal Matters

The Company is involved from time to time in claims that arise in the normal course of its business. The Company is not presently subject to any material litigation nor, to management's knowledge, is any litigation threatened against the Company that collectively is expected to have a material adverse effect on the Company's cash flows, financial condition or results of operations.

(15) Related Party

In December 2009, the Company entered into a Note and Warrant Purchase Agreement with certain of the Company's stockholders pursuant to which we issued convertible promissory notes in an aggregate principal amount of \$20,000,000 and warrants to purchase shares of preferred stock. In July 2010, the Company entered into an amendment to the Note and Warrant Purchase Agreement. The convertible promissory notes accrued interest at the rate of 10% per annum. In July 2010, the convertible promissory notes were converted into an aggregate of 5,294,514 shares of the Company's Series E preferred stock at a conversion price of \$4.00 per share and the warrants to purchase shares of preferred stock became exercisable to purchase an aggregate of 8,733,617 shares of the Company's Series E-1 preferred stock at exercise prices of \$2.29 per share (see Notes 8(b) and 9(c)).

The National Flex Trust, or the Trust, established by a subsidiary of the Company, is to provide reimbursement of qualified expenses to plan participants under certain employer plans that have contracted with the Company to provide the plan services using a custodial account, or the Trust Account, maintained by the Company. The client is responsible for maintaining the employer plan for their participants, including the establishment of eligibility and paying all eligible claim amounts owed to their participants. The Company is an independent contractor engaged to perform administration services. As an administrator, the Company does not have the power to direct the activities of the Trust that would most significantly impact the Trust's economic performance.

Under a Management Agreement for Services to the Trust, the Company is to provide services to the Trust, including accounting, treasury, tax, administration, and management. The Trust is to pay the Company monthly

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WAGEWORKS, INC.

Notes to Consolidated Financial Statements

for the services provided based on plan participants and/or debit cards administered. For the past several years, the Trust's earnings have been insufficient to cover these costs and, consequently, the Company has not recognized these fees during this period. Amounts due to the Company from the Trust for management services have been fully written off as of December 31, 2011. Trust expenses subsidized by the Company were \$64,000, \$84,000 and \$112,000 in 2009, 2010 and 2011, respectively. Trust expenses subsidized by the Company were \$34,000 and \$29,000 for the unaudited quarters ended June 30, 2011 and 2012, respectively and \$58,000 and \$55,000 for the unaudited six months ended June 30, 2011 and 2012, respectively.

The Company has a long-term receivable due from the Trust totaling \$1.0 million which the Trust holds with its banks, as a security deposit for the settlement of participant claims. The Company has recorded this receivable within Other Assets.

(16) Subsequent Events

In September 2012, the Company entered into an amendment to its credit facility with UB to extend the maturity date from October 31, 2012 to October 31, 2013. In conjunction with the amendment, the Company paid UB a commitment extension fee of \$125,000.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors of TransitCenter, Inc.

We have audited the accompanying statements of financial position of TransitCenter, Inc. (the Company) as of December 31, 2011 and 2010, and the related statements of activities and cash flows for each of the years in the two-year period ended December 31, 2011. The financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of TransitCenter, Inc. as of December 31, 2011 and 2010, and the changes in its net assets and cash flows for each of the years in the two-year period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America.

As discussed further in Note 10, effective February 1, 2012, the Company sold substantially all of its assets to another entity.

/s/ EisnerAmper LLP

Edison, New Jersey

March 5, 2012

Table of Contents**TRANSITCENTER, INC.****STATEMENTS OF FINANCIAL POSITION****DECEMBER 31,**

	2011	2010
Assets		
Cash and cash equivalents	\$ 74,461,286	\$ 82,336,838
Restricted investments	459,743	2,063,154
Accounts receivable, net of allowance for doubtful accounts of \$1,063,153 and \$1,255,903, respectively	863,983	3,802,747
Other accounts receivable	293,420	177,473
Inventory	6,514,329	6,482,132
Prepaid expenses and other assets	1,008,406	241,147
Fixed assets, net	2,545,951	2,536,080
 Total Assets	 \$ 86,147,118	 \$ 97,639,571
Liabilities and Unrestricted Net Assets		
Amounts payable to transit operators	\$ 54,895,627	\$ 79,249,018
Accounts payable and other accrued liabilities	3,639,261	3,002,761
Deferred rent credits	130,081	71,075
 Total Liabilities	 58,664,969	 82,322,854
Commitments and Contingencies		
Unrestricted Net Assets	27,482,149	15,316,717
 Total Liabilities and Unrestricted Net Assets	 \$ 86,147,118	 \$ 97,639,571

The accompanying notes are an integral part of these financial statements.

Table of Contents**TRANSITCENTER, INC.****STATEMENTS OF ACTIVITIES****FOR THE YEARS ENDED DECEMBER 31,**

	2011	2010
Unrestricted revenue		
Commissions	\$ 19,230,909	\$ 20,103,874
Interest income	41,427	54,750
Packaging and other fees	1,046,535	880,328
Expired products	10,863,766	1,355,135
 Total Unrestricted Revenue	 31,182,637	 22,394,087
Expenses		
Program services:		
Promotion of mass transportation	1,937,768	1,900,288
Operation of transit fare system	13,369,162	13,519,210
 Total Program Services	 15,306,930	 15,419,498
Supporting Services:		
Management and general	3,710,275	3,308,267
 Total Expenses	 19,017,205	 18,727,765
Change in unrestricted net assets	12,165,432	3,666,322
Unrestricted Net Assets		
Beginning of year	15,316,717	11,650,395
 End of year	 \$ 27,482,149	 \$ 15,316,717

The accompanying notes are an integral part of these financial statements.

Table of Contents**TRANSITCENTER, INC.****STATEMENTS OF CASH FLOWS****FOR THE YEARS ENDED DECEMBER 31,**

	2011	2010
Cash Flows From Operating Activities		
Change in unrestricted net assets	\$ 12,165,432	\$ 3,666,322
Adjustments to reconcile change in unrestricted net assets to cash flows used in operating activities:		
Depreciation and amortization	937,971	976,995
Deferred rent expense (amortization)	59,006	(32,684)
Change in operating assets and liabilities:		
Accounts receivable	2,938,764	1,069,807
Other accounts receivable	(115,947)	(45,855)
Inventory	(32,197)	(2,678,167)
Prepaid expenses and other assets	(767,259)	(144,616)
Amounts payable to transit operators	(24,353,391)	(7,219,038)
Accounts payable and other accrued liabilities	636,500	(253,862)
 Net Cash Used in Operating Activities	 (8,531,121)	 (4,661,098)
Cash Flows From Investing Activities		
Proceeds from restricted investments	1,603,411	(160)
Purchase of fixed assets	(947,842)	(812,753)
 Net Cash Provided by (Used in) Investing Activities	 655,569	 (812,913)
 Decrease in Cash and Cash Equivalents	 (7,875,552)	 (5,474,011)
Cash and Cash Equivalents		
Beginning of year	82,336,838	87,810,849
 End of year	 \$ 74,461,286	 \$ 82,336,838

The accompanying notes are an integral part of these financial statements.

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TRANSITCENTER, INC.

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011 AND 2010

NOTE 1 NATURE OF OPERATIONS

TransitCenter, Inc. (TransitCenter or the Company) was incorporated on May 23, 2000. Previous to that date, TransitCenter was a staff unit of the Port Authority of New York and New Jersey (the Port Authority). TransitCenter did not have any financial operations from May 23, 2000 through January 1, 2001. The Port Authority provided funding in 2001 in order to cover amounts payable to transit operators and a contribution to help TransitCenter fund unrestricted current and future operations.

TransitCenter is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

The philanthropic mission of TransitCenter is to promote the conservation of natural resources, reduce traffic congestion and combat air pollution as follows:

Support and promote the use of mass transportation;

Lessen the burden of governmental agencies which operate transit services by providing services at employer work sites, including transit fare media and information distribution activities and by relieving these agencies of the burden of undertaking regional efforts individually;

Support governmental programs whose aims are to reduce congestion and improve air quality;

Promote communication and understanding among public transit providers, the business community and the public; and

Develop and operate financial and other incentive programs that encourage greater use of mass transportation, including transit pass and voucher programs that facilitate employers use of federal and state tax benefits that provide tax savings to employees who commute by transit.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Statements

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Net Asset Clarifications

Net assets, revenue, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Permanently Restricted Net Assets

Net assets subject to donor-imposed restrictions which stipulate that they be maintained permanently by TransitCenter.

Temporarily Restricted Net Assets

Net assets subject to donor-imposed restrictions that may or will be met by actions of TransitCenter or that expire by the passage of time.

Unrestricted Net Assets

Net assets that are not subject to donor-imposed restrictions.

TransitCenter did not have permanently or temporarily donor-imposed restricted net assets as of or for the years ended December 31, 2011 and 2010.

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TRANSITCENTER, INC.

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011 AND 2010

Revenue Recognition

TransitCenter's revenue primarily comes from commissions and fees which, in accordance with Accounting Standards Codification (ASC) Topic 605-45, are recorded net of the gross bookings as the Company is not the primary obligor. The Company's products consist of TransitChek vouchers and cards, TransitChek QuickPay cards, Premium TransitChek MetroCards, TransitChek MetroCards and ticket by mail (the Products). Additionally, TransitCenter receives discounts and other income from the sale or use of various products that are distributed to its customers under its programs. Commission and fee revenues are recognized when TransitCenter ships or fulfills the orders as evidence that an arrangement has been obtained, service has been completed, fees are fixed and determinable and payment is reasonably assured.

Beginning in fiscal 2006, TransitCenter began to purchase certain fare cards from the transit operators which were subsequently sold to customers. Revenue and expense are recognized when these cards are shipped or fulfilled in accordance with the criteria discussed in the previous paragraph.

TransitCenter recognizes revenue for certain of its Products that have expired and will not be redeemed based on current information and trends regarding these products. See Note 8 for further discussion regarding the treatment of these expired products.

The Company generally bills and collects for its Products in advance of shipment or fulfillment and accounts for collections as customer advances (See Note 5). Certain of these funds are invested in two money market accounts, earning interest at rates of 0.30% and 0.06% as of December 31, 2011 and 0.30% and 0.05% as of December 31, 2010. The interest income is unrestricted as to TransitCenter's use.

Cash and Cash Equivalents

Cash and cash equivalents includes various interest and noninterest-bearing accounts. TransitCenter considers all short-term investments with maturities of three months or less, at time of purchase, to be cash equivalents. At December 31, 2011 and 2010, TransitCenter's cash and cash equivalents was maintained primarily with two banks and exceeded federally insured limits.

Restricted Investments

TransitCenter is required to have liquid assets of \$459,743 available as defined in its office lease agreement and restricted as to use. The required liquid assets are invested in a one-year certificate of deposit, earning interest at a rate of approximately 0.20% at December 31, 2011 and 2010. Additionally, the Company maintained an escrow account for the Metropolitan Transportation Authority (the MTA) of approximately \$1.6 million that was invested in a money market account earning interest at a rate of approximately 0.00% at December 31, 2010. In December 2011, the escrow account with the MTA was closed and the funds were returned to TransitCenter.

Accounts Receivable and Allowance for Doubtful Accounts

The Company's accounts receivable are recorded at amounts billed to customers, and are presented on the statements of financial position net of the allowance for doubtful accounts. The allowance is determined by a variety of factors, including the age of the receivables, current economic conditions, historical losses and other information management obtains regarding the financial condition of customers. The policy for determining the past due status of receivables is based on how recently payments have been received.

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TRANSITCENTER, INC.

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011 AND 2010

Inventory

Inventory is recorded in the statements of financial position at the lower of cost or market and accounted for on an average cost basis. Raw materials consist of materials to produce vouchers and various MetroCard and debit card products. Finished goods consist primarily of purchased fare media, including MetroCards, which are held for sale.

Fixed Assets

Fixed assets are stated at cost less accumulated depreciation and amortization. Depreciation and amortization expense is calculated on the straight-line method based upon estimated useful lives from 3 to 5 years. Leasehold improvements are amortized over the shorter of the life of the lease or the estimated useful life of the asset. Costs associated with the application, development and installation stages of significant new computer software applications for internal use are deferred and amortized over the expected useful life of the software application which ranges from 3 to 5 years.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from estimates. On an on-going basis, the Company re-evaluates its judgments and estimates including those related to expired and unredeemed products, allowance for doubtful accounts and amounts payable to transit operators.

Allocation of Expenses

TransitCenter allocates total costs to various functional expense categories.

Promotion of transportation includes all expenses associated in promoting communication and understanding among public transit providers, the business community and the public. Operation of transit fare system includes all expenses associated with administering the Products.

Income Taxes

U.S. GAAP requires entities to evaluate, measure, recognize and disclose any uncertain income tax positions taken on their federal or state tax returns. Management has evaluated the impact of this standard on its financial statements and believes that there are no uncertain tax positions. The Company's federal and state information returns are subject to examination by the Internal Revenue Service and the various states the Company files in for three years from the date the returns are filed. The 2008, 2009 and 2010 information returns are available for such examination.

Subsequent Events

The Company has evaluated material subsequent events through March 5, 2012, the date these financial statements were available to be issued, and determined that any events or transactions that would require recognition or disclosure are appropriately reflected in these financial statements.

Table of Contents**TRANSITCENTER, INC.****NOTES TO FINANCIAL STATEMENTS****DECEMBER 31, 2011 AND 2010****NOTE 3 INVENTORY**

Inventory consists of the following:

	December 31,	
	2011	2010
Raw materials	\$ 210,171	\$ 230,632
Finished goods	6,304,158	6,251,500
	\$ 6,514,329	\$ 6,482,132

NOTE 4 FIXED ASSETS

Fixed assets consist of the following:

	Estimated Useful Life in Years	December 31,	
		2011	2010
Computer hardware	3	\$ 1,064,023	\$ 980,702
Computer software	3-5	12,615,640	12,587,879
Furniture and fixtures	5	1,253,807	555,513
Office equipment	5	73,480	34,825
Leasehold improvements	Shorter of life of lease or estimated useful life	1,637,507	800,886
		16,644,457	14,959,805
Less: Accumulated depreciation and amortization		14,098,506	13,160,535
		2,545,951	1,799,270
Furniture and fixtures and leasehold improvements related to lease of new office space (see Note 6)			736,810
		\$ 2,545,951	\$ 2,536,080

Depreciation and amortization expense for the years ended December 31, 2011 and 2010 totaled \$937,971 and \$976,995, respectively. There was no impairment of assets as of December 31, 2011 and 2010.

NOTE 5 AMOUNTS PAYABLE TO TRANSIT OPERATORS

Amounts payable to transit operators consisted of the following as of December 31, 2011 and 2010:

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	2011	2010
Amounts payable on Products	\$ 28,661,698	\$ 43,798,772
Customer advances	15,233,819	20,669,839
Amounts due to the MTA	10,971,502	14,765,201
All other	28,608	15,206
	\$ 54,895,627	\$ 79,249,018

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(Continued)

Table of Contents**TRANSITCENTER, INC.****NOTES TO FINANCIAL STATEMENTS****DECEMBER 31, 2011 AND 2010****NOTE 6 COMMITMENTS AND CONTINGENCIES***Leases*

The Company amended its office lease agreement during 2010 to consolidate its offices within the same building it currently occupies. The effective date of this amendment is as of January 19, 2011 and expires on February 28, 2023. As of January 19, 2011, the old lease obligations terminated and the new lease agreement began.

In June 2011, the Company entered into a sublease agreement for a portion of its office space. The lease has a three year term expiring on June 8, 2014.

The minimum annual rental payments for all noncancelable operating leases and related sublease income are as follows for the years ending December 31:

Year	Minimum Rental Commitments	Sublease Rental Income	Net
2012	\$ 1,417,330	\$ (162,239)	\$ 1,255,091
2013	1,413,307	(162,239)	1,251,068
2014	1,402,327	(71,097)	1,331,230
2015	1,472,631		1,472,631
2016	1,484,271		1,484,271
2017-2023	9,503,487		9,503,487
	\$ 16,693,353	\$ (395,575)	\$ 16,297,778

Occupancy expense was \$1,386,721 and \$1,161,667, net of sublease income of \$81,133 and \$0, for the years ended December 31, 2011 and 2010, respectively. In accordance with U.S. GAAP, rent expense is recognized on a straight-line basis over the term of the lease. The difference between the lease payment and expense is reported as a deferred rent credit on the statements of financial position.

Legal Proceedings

TransitCenter is subject to various legal proceedings and claims that arise in the ordinary course of business. Management believes that the ultimate liability with respect to these matters is not material to the financial position, changes in net assets or cash flows of TransitCenter.

Major Customer

For the year ended December 31, 2010, approximately 13% of the Company's unrestricted revenue directly or indirectly was associated with sales to one customer. Effective in February 2011, due to the nonrenewal of a contract, a majority of the revenue associated with this customer did not continue. No other customer accounted for more than 10% of revenues in 2011 and 2010.

NOTE 7 EMPLOYEE BENEFIT PLANS

TransitCenter makes available to its employees a 401(k) benefit plan. During 2011 and 2010, TransitCenter matched 50% and 100%, respectively, of the employee voluntary contributions up to 6% of the base salary and in accordance with applicable Internal Revenue Code

limitations. TransitCenter s match vests to the employee 50%

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TRANSITCENTER, INC.

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011 AND 2010

after 2 full years of service and 100% after 3 full years of service. The expense for the plan was \$137,148 and \$304,708 for the years ended December 31, 2011 and 2010, respectively. The Company also maintains a non-qualified deferred compensation plan under Internal Revenue Code 457(b) for certain of its managers and executives. Contributions for these accounts are made at the discretion of the Company and are fully vested at the end of each calendar year. The liability associated with this plan was \$623,031 and \$543,281 as of December 31, 2011 and 2010, respectively, and is included in accounts payable and other accrued liabilities. The expense for this plan was \$205,476 and \$122,038 for the years ended December 31, 2011 and 2010, respectively.

As part of the transaction discussed in Note 10, the assets and liabilities associated with the 401(k) benefit plan were transferred to the purchaser. The Company is also in the process of terminating the non-qualified deferred compensation plan.

NOTE 8 EXPIRED PRODUCTS

During 2008, the New York State Office of Comptroller informed TransitCenter that the Office of the Comptroller will not assert a claim under New York State escheatment laws for expired and unredeemed transit vouchers issued by the Company. Based on this oral statement from the Office of the Comptroller, the Company, upon completion of service, records as revenue an estimate of the amount of transit vouchers that it expects will expire and not be redeemed in the future. The estimate of the percentage of expired and unredeemed vouchers, in relation to voucher sales, is based on current information and trends.

During 2011, the Company completed its analysis with respect to the recognition of revenue related to TransitChek cards (TC cards) that have expired, or are expected in the future to expire and not be redeemed, concluding that the unused pretax funds remaining on these cards would not be escheatable to the State. The Company subsequently received confirmation from the issuing bank of the TC cards that it agreed with its conclusion. As a result, the Company concluded that the uncertainty in recording revenue no longer exists. The estimate of the percentage of expired and unredeemed TC cards and vouchers, in relation to sales of those products, is based on the sales value of each issued product multiplied by a historically developed expiration percentage.

For the year ended December 31, 2011, the Company recorded revenue from expired and unredeemed vouchers and TC cards totaling \$10,863,766, of which \$2,722,361 relates to vouchers and TC cards issued during 2011 and the balance relates to TC cards issued prior to 2011.

NOTE 9 RELATED PARTY TRANSACTIONS

A member of the Board of Directors is the CEO and founder of a technology consulting firm. After review and in accordance with TransitCenter's conflict of interest policy including recusal of the interested party from voting, TransitCenter's Board of Directors approved the use of this board member's firm to provide software development services to TransitCenter in connection with a major change in technology systems. TransitCenter paid \$37,273 to this firm for the year ended December 31, 2010. No amounts were paid or incurred in 2011.

NOTE 10 SUBSEQUENT EVENT

On November 16, 2011, TransitCenter entered into an asset purchase agreement providing for the sale of substantially all of its assets, excluding certain cash and cash equivalents, and the assumption of certain of its liabilities by an unrelated entity. This transaction was subject to regulatory approval which was completed in January 2012. The transaction closed on February 1, 2012. Included in prepaid expenses and other assets as of December 31, 2011 is approximately \$642,000 of direct costs related to this transaction.

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On the date of the closing, after consummation of the transaction, the Company would have approximately \$60 million in cash and cash equivalents including amounts held in escrow subject to meeting certain revenue thresholds and the set-off of any indemnified claims, as defined, and \$1 million in liabilities, primarily consisting of employee related costs. TransitCenter expects to record a gain of approximately \$32 million. Total cash consideration is expected to be \$37 million, which includes the acquirer paying \$200,000 per year for five years to be used to further the Company's philanthropic mission.

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Unaudited Pro Forma Condensed Consolidated Financial Statement Information

Introductory Note

The following unaudited pro forma condensed consolidated balance sheet presents the financial position as of December 31, 2011 of WageWorks, Inc., (the Company), assuming that the acquisition of all of the operating assets of TransitCenter, Inc. (TCI), a not for profit entity based in New York that conducted a business we refer to as TransitChek (TC), had been completed as of December 31, 2011.

The unaudited pro forma condensed consolidated statement of operations for the year ended December 31, 2011 includes the results of operations of the Company and TC, as if the acquisition had been consummated on January 1, 2011, the first day of the Company's fiscal year 2011.

The historical financial information has been adjusted to give effect to pro forma events that are directly attributable to the acquisition and factually supportable. The Company's unaudited pro forma condensed consolidated financial information and explanatory notes present how the Company's financial statements may have appeared had the businesses actually been combined as of the dates noted above. The unaudited pro forma condensed consolidated financial information shows the impact on the combined balance sheet and the combined statement of operations under the purchase method of accounting under Financial Accounting Standards Board ASC 805, *Business Combinations*, which are subject to change and interpretation, with the Company treated as the acquirer. Under the purchase method of accounting, the total purchase price is allocated to the assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date. The excess purchase price over the amounts assigned to tangible or intangible assets acquired and liabilities assumed is recognized as goodwill.

The following unaudited pro forma condensed consolidated financial information is presented for illustrative purposes only and does not purport to reflect the results the consolidated company may achieve in future periods or the historical results that would have been obtained had the Company and TC been a consolidated company during the relevant period presented.

The unaudited pro forma condensed consolidated financial information is derived from and should be read in conjunction with the historical financial statements and related notes included elsewhere in this prospectus.

Table of Contents**Unaudited Pro Forma Condensed Consolidated Balance Sheet**

(In thousands, except per share amounts)

	WageWorks Historical December 31, 2011	TransitCenter Historical December 31, 2011	Pro Forma Adjustments	Pro Forma Footnotes	Pro Forma Combined
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 154,621	\$ 74,461	\$ (24,779) (36,200) 35,000	(1) (2) (2)	\$ 203,103
Restricted cash, current portion	2,383	460			2,843
Accounts receivable, net	15,647	864			16,511
Inventory		6,514			6,514
Prepaid expenses and other current assets	7,178	1,302	(1,065)	(1)	7,415
Total current assets	179,829	83,601	(27,044)		236,386
Restricted cash, net of current portion	2,526				2,526
Property and equipment, net	19,014	2,546			21,560
Goodwill	46,233		23,254	(3)	69,487
Acquired intangible assets, net	12,555		11,200	(3)	23,755
Deferred tax asset	16,978				16,978
Other assets	1,561				1,561
Total assets	\$ 278,696	\$ 86,147	\$ 7,410		\$ 372,253
LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS DEFICIT					
Current liabilities:					
Accounts payable and accrued expenses	\$ 21,415	\$ 3,639	\$ (908)	(1)	\$ 24,146
Customer obligations	169,959	54,896			224,855
Short-term contingent payment	8,976				8,976
Short-term debt	14,901		35,000	(4)	49,901
Other current liabilities	394	130			524
Total current liabilities	215,645	58,665	34,092		308,402
Long-term obligation			800	(5)	800
Warrants	1,119				1,119
Long-term contingent payment, net of current portion					
Other non-current liabilities	1,820				1,820
Total liabilities	218,584	58,665	34,892		312,141
Redeemable convertible preferred stock:					
Redeemable convertible preferred stock, Series C	36,570				36,570
Redeemable convertible preferred stock, Series D	17,771				17,771
Redeemable convertible preferred stock, Series E	27,828				27,828
Total redeemable convertible preferred stock	82,169				82,169
Stockholders deficit:					
Convertible preferred stock	33,965				33,965

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Common stock	2				2
Treasury stock	(433)				(433)
Additional paid- in capital	19,029				19,029
Accumulated deficit	(74,620)	27,482	(27,482)	(1)	(74,620)
Total stockholders' equity (deficit)	(22,057)	27,482	(27,482)		(22,057)
Total liabilities, redeemable convertible preferred stock, and stockholders' deficit	\$ 278,696	\$ 86,147	\$ 7,410		\$ 372,253

The accompanying notes are an integral part of these unaudited pro forma condensed consolidated financial statements

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Table of Contents**Unaudited Pro Forma Condensed Consolidated Statement of Operations****(In thousands, except per share amounts)**

	WageWorks Fiscal Year Ended December 31, 2011	TransitCenter Fiscal Year Ended December 31, 2011		Pro Forma Adjustments	Pro Forma Footnotes	Pro Forma Combined
Revenues:						
Healthcare	\$ 90,917	\$		\$		\$ 90,917
Commuter	33,325	31,183	Note 4			64,508
Other	11,395					11,395
Total revenue	135,637	31,183				166,820
Operating expenses	122,077	19,017		1,723 (467)	(6) (1)	142,350
Income from operations	13,560	12,166	Note 4	(1,256)		24,470
Other income (expense)	(107)			(1,225)	(7)	(1,332)
Income before income taxes	13,453	12,166		(2,481)		23,138
Income tax benefit	19,868			(3,680)	(8)	16,188
Net income	33,321	12,166		(6,161)		39,326
Accretion of redemption premium expense	(6,209)					(6,209)
Net income attributable to common stockholders	\$ 27,112	\$ 12,166	Note 4	\$ (6,161)		\$ 33,117
Diluted net income per share attributable to common stockholders	\$ 1.43					\$ 1.73
Shares used in diluted net income per share calculations	20,086					20,086

The accompanying notes are an integral part of these unaudited pro forma condensed consolidated financial statements

Table of Contents**Notes to unaudited pro forma condensed consolidated financial statements****Note 1 Basis of Pro Forma Presentation**

On February 1, 2012, the Company acquired all of the operating assets of TCI for a total purchase price of \$37.0 million, with \$36.2 million payable in 2012 and \$0.8 million paid over the next four years as contributions to a promotional fund in furtherance of TCI's mission of raising awareness of the benefits of mass transit. The Company is contractually obligated to pay a contingent payment to TCI which is determined based on TC maintaining revenue levels six months following the close of the acquisition that are comparable to what was recorded in January 2012. In accordance with the terms of the contract, the contingent payment would be due in July 2012. For pro forma purposes, the total purchase price payable in 2012 assumes the full payment of the contingent consideration to TC of \$5.4 million. For the purposes of the pro forma presentation of the consolidated balance sheet, the Company has assumed the full payment of the \$36.2 million was made as of December 31, 2011. This payment will be primarily financed through the Company's revolving credit facility with UB. For purposes of the pro forma presentation of additional interest expense recorded related to the transaction, the Company has assumed an incremental draw down of this facility as of January 1, 2011 in an amount of \$35.0 million with \$1.2 million paid from cash balances, which represents the actual financing used by the Company in February 2012.

The unaudited pro forma adjustments are based upon available information and certain assumptions that are factually supportable and that the Company believes are reasonable under the circumstances.

Certain financial statements classifications of TCI have been reclassified to conform to the Company's presentation.

Note 2 Purchase Price and Purchase Price Allocation

The purchase method of accounting is dependent on certain valuations that have yet to commence or progress to a stage where there is sufficient information for definitive measurement. Accordingly, the pro forma adjustments are preliminary and have been made solely for the purpose of providing unaudited pro forma combined financial information. Differences between these preliminary estimates, including the estimates of the purchase consideration and allocation of the purchase price to operating assets, including intangible assets, and the final acquisition accounting will occur and these differences could have a material impact on the accompanying unaudited pro forma condensed consolidated financial statements and the combined company's future results of operations and financial position.

The following table summarizes the preliminary allocation of the purchase price based on the fair value of the acquired assets (in millions):

Goodwill	\$ 23.3
Property and equipment and net tangible assets	2.5
Intangibles (primarily customer relationships)	11.2
	\$ 37.0

Property and equipment. The valuation of the property and equipment acquired was based on the net book values of the assets as a proxy for fair value.

Goodwill and Intangibles. For the preliminary allocation of the purchase price to acquired intangibles, the Company used the average historical ratio of acquired intangibles to projected revenue for the last four portfolio purchases. Ultimately, the valuation of the identifiable acquired intangible assets will be based on management's estimates, information and reasonable and supportable assumptions utilizing a discounted cash flow method based on the identifiable future revenues projected. The excess of the purchase price (consideration transferred) over the estimated amounts of identifiable assets and liabilities of the TCI acquisition as of the effective date of

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the acquisition will be allocated to goodwill in accordance with ASC 805. The purchase price allocation to goodwill and acquired intangibles above is preliminary and will be subject to adjustment upon completion of the final valuation. These adjustments could be material.

Note 3 Pro Forma Adjustments

(1) To record adjustments for assets not acquired, liabilities not assumed and expenses associated with non-acquired operations of TCI as part of the acquisition.

(2) Cash paid by the Company at closing for the acquisition of \$36.2 million, financed through a \$35.0 million draw on its revolving credit facility and \$1.2 million from the Company's cash.

(3) To record the acquisition of goodwill and acquired intangible assets based on estimated fair value. The purchase price allocation is subject to completion of the Company's analysis of the fair value of the assets and liabilities of TC as of the effective date of the TC acquisition. For the preliminary allocation of the purchase price to acquired intangibles, the Company used the average historical ratio of acquired intangibles to projected revenue for the last four portfolio purchases. Accordingly, the purchase price allocation is preliminary and will be adjusted upon completion of the final valuation. These adjustments could be material.

(4) To reflect the financing of the purchase price, which includes a contingent payment, with the Company's revolving credit facility. As of June 30, 2012, any borrowing outstanding under the revolving credit facility with UB was due and payable on October 31, 2012. In September 2012, the Company entered into an amendment to extend the due date to October 31, 2013.

(5) To record obligation to TCI as part of future payments due to a promotional fund.

(6) To record estimated amortization of the acquired intangible asset, using an estimated useful life of 8 years.

(7) To record interest expense on the additional financing necessary to complete the transaction at a current variable rate of 3.5% as if the draw had taken place on January 1, 2011. Under the terms of the Company's line of credit, the variable rate is fixed for the first six months after each draw. Upon the expiration of the fixed term, a 1/8th percent change in the variable rate would change interest expense by approximately \$44,000 for the period presented.

(8) To record income tax expense at an estimated combined Federal and State rate of 38%.

Note 4 Expired Products Revenue

During 2011, TCI completed its analysis with respect to the recognition of revenue related to TransitChek cards (TC cards) that have expired, or are expected in the future to expire and not be redeemed, concluding that the unused pretax funds remaining on these cards would not be escheatable to the State of New York. TCI subsequently received confirmation from the issuing bank of the TC cards that the issuing bank agreed with its conclusion. As a result, TCI concluded that the uncertainty in recording revenue no longer exists. The estimate of the percentage of expired and unredeemed TC cards, in relation to TC card sales, is based on current information and trends. The TCI commuter revenue for 2011 includes revenue from expired and unredeemed vouchers and TC cards totaling \$10.9 million, of which \$2.7 million relates to vouchers and TC cards issued during 2011 and \$8.2 million relates to TC cards issued prior to 2011. The \$8.2 million of expired product revenue has no associated expenses. The Company does not expect that there will be any revenue relating to TC cards issued prior to 2011 in the future.

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6,000,000 Shares

Common Stock

Prospectus

October 3, 2012

William Blair

Stifel Nicolaus Weisel

JMP Securities

Needham & Company

Until October 28, 2012 (25 days after the commencement of the offering), all dealers that buy, sell or trade the common stock, may be required to deliver a prospectus, regardless of whether they are participating in this offering. This is in addition to the dealers' obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.