

CASTLIGHT HEALTH, INC.
Form 10-Q
August 05, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2015

or

TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission File Number: 001-36330
CASTLIGHT HEALTH, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

26-1989091
(I.R.S. Employer
Identification Number)

Two Rincon Center
121 Spear Street, Suite 300
San Francisco, CA 94105
(Address of principal executive offices)

(415) 829-1400
(Registrant's telephone number, including area code)

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

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

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

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

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

As of July 31, 2015, there were 54,681,184 shares of the Registrant's Class A common stock outstanding and 39,635,427 shares of the Registrant's Class B common stock outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CASTLIGHT HEALTH, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	As of June 30, 2015 (unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$31,533	\$17,425
Marketable securities	132,905	175,057
Accounts receivable, net	11,048	11,097
Deferred commissions	3,956	3,675
Prepaid expenses and other current assets	5,960	3,476
Total current assets	185,402	210,730
Property and equipment, net	4,515	3,630
Marketable securities, noncurrent	—	6,220
Restricted cash, noncurrent	1,000	—
Deferred commissions, noncurrent	2,374	2,563
Other assets	3,692	131
Total assets	\$196,983	\$223,274
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$4,180	\$3,217
Accrued expenses and other current liabilities	4,702	5,791
Accrued compensation	8,730	10,455
Deferred revenue	24,125	20,708
Total current liabilities	41,737	40,171
Deferred revenue, noncurrent	7,638	6,652
Other liabilities, noncurrent	1,208	261
Total liabilities	50,583	47,084
Commitments and contingencies		
Stockholders' equity:		
Class A common stock	5	6
Class B common stock	4	3
Additional paid-in capital	404,412	393,397
Accumulated other comprehensive income (loss)	10	(40)
Accumulated deficit	(258,031)	(217,176)
Total stockholders' equity	146,400	176,190
Total liabilities and stockholders' equity	\$196,983	\$223,274

See Notes to Condensed Consolidated Financial Statements.

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CASTLIGHT HEALTH, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Revenue:				
Subscription	\$17,278	\$9,576	\$32,184	\$17,039
Professional services	1,232	957	2,277	1,870
Total revenue	18,510	10,533	34,461	18,909
Cost of revenue:				
Cost of subscription (1)	2,932	2,915	5,451	5,627
Cost of professional services (1)	5,322	4,502	9,975	8,373
Total cost of revenue	8,254	7,417	15,426	14,000
Gross profit	10,256	3,116	19,035	4,909
Operating expenses:				
Sales and marketing (1)	17,641	14,947	34,104	31,507
Research and development (1)	7,391	5,476	13,985	11,003
General and administrative (1)	6,517	4,519	11,980	8,529
Total operating expenses	31,549	24,942	60,069	51,039
Operating loss	(21,293	) (21,826	) (41,034	) (46,130
Other income, net	81	50	179	73
Net loss	\$(21,212	) \$(21,776	) \$(40,855	) \$(46,057
Net loss per Class A and B share, basic and diluted	\$(0.23	) \$(0.24	) \$(0.44	) \$(0.86
Weighted-average shares used to compute basic and diluted net loss per Class A and B share	93,804	89,520	92,801	53,284

(1) Includes stock-based compensation expense as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Cost of revenue:				
Cost of subscription	\$67	\$35	\$100	\$39
Cost of professional services	450	280	875	420
Sales and marketing	2,074	1,152	3,825	2,326
Research and development	730	493	1,363	914
General and administrative	896	980	1,923	1,794

See Notes to Condensed Consolidated Financial Statements.

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CASTLIGHT HEALTH, INC
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
 (In thousands)
 (unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Net loss	\$(21,212	) \$(21,776	) \$(40,855	) \$(46,057
Other comprehensive income (loss):				
Net change in unrealized gain (loss) on available-for-sale marketable securities	8	(41	) 50	(40
Reclassification adjustments for net realized gains on available-for-sale marketable securities	—	—	—	—
Other comprehensive income (loss)	8	(41	) 50	(40
Comprehensive loss	\$(21,204) \$(21,817) \$(40,805) \$(46,097

See Notes to Condensed Consolidated Financial Statements.

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CASTLIGHT HEALTH, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In thousands)
 (unaudited)

	Six Months Ended June 30,	
	2015	2014
Operating activities:		
Net loss	\$(40,855	) \$(46,057
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	910	604
Stock-based compensation	8,086	5,493
Amortization of deferred commissions	1,659	2,244
Accretion and amortization of marketable securities	827	497
Expense related to warrant	—	2,499
Changes in operating assets and liabilities:		
Accounts receivable	49	(5,327
Deferred commissions	(1,751	) (1,369
Prepaid expenses and other assets	(1,818	) (1,677
Accounts payable	1,258	384
Accrued expenses and other liabilities	(3,169	) (1,203
Deferred revenue	4,403	8,277
Net cash used in operating activities	(30,401	) (35,635
Investing activities:		
Restricted cash	(1,000	) 101
Investment in related party	(3,125) —
Purchase of property and equipment	(1,693	) (967
Purchase of marketable securities	(18,958	) (162,175
Sales of marketable securities	5,000	13,000
Maturities of marketable securities	61,553	8,000
Net cash provided by (used in) investing activities	41,777	(142,041
Financing activities:		
Proceeds from the exercise of stock options	2,826	1,628
Payments of deferred offering costs	(94	) (3,781
Proceeds from initial public offering	—	189,943
Net cash provided by financing activities	2,732	187,790
Net increase in cash and cash equivalents	14,108	10,114
Cash and cash equivalents at beginning of period	17,425	25,154
Cash and cash equivalents at end of period	\$31,533	\$35,268

See Notes to Condensed Consolidated Financial Statements.

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1. Organization and Description of Business

Description of Business

Castlight Health, Inc. ("Castlight") is a pioneer in a new category of cloud-based software that enables enterprises to understand and manage health care spending as a strategic business investment, and help employees and their families make more informed medical decisions based on factors such as cost, quality and patient experience. Our Enterprise Healthcare Management solutions allow our customers to conquer the complexity of the existing health care system by providing personalized, actionable information to their employees, implementing technology-enabled benefit designs and integrating disparate systems and applications. Our comprehensive technology offering aggregates complex, large-scale data and applies sophisticated analytics to make health care data transparent and useful. We were incorporated in the State of Delaware in January 2008. Our principal executive offices are located in San Francisco, California.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements were prepared in accordance with U.S. generally accepted accounting principles (GAAP), for interim financial information and with the instructions to Form 10-Q and Article 10 of Securities and Exchange Commission (SEC), Regulation S-X. In the opinion of management, the information herein reflects all adjustments, consisting only of normal recurring adjustments except as otherwise noted, considered necessary for a fair statement of results of operations, financial position and cash flows. The condensed consolidated financial statements include the results of Castlight and its wholly owned U.S. subsidiary. The results for the interim periods presented are not necessarily indicative of the results expected for any future period. The condensed consolidated balance sheet as of December 31, 2014 included herein was derived from the audited financial statements as of that date. The following information should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2014. There have been no changes to our significant accounting policies described in our Annual Report on Form 10-K that have had a material impact on our condensed consolidated financial statements and related notes.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires us to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements, as well as the reported amounts of revenue and expenses during the reporting period. These estimates include, but are not limited to, the determination of the relative selling prices for our services, certain assumptions used in the valuation of our equity awards, and the capitalization and estimated useful life of internal-use software development costs. Actual results could differ from those estimates, and such differences could be material to our consolidated financial position and results of operations.

Recently Issued and Adopted Accounting Pronouncements

In April 2015, the Financial Accounting Standards Board (FASB) issued new accounting guidance Customer's Accounting for Fees Paid in a Cloud Computing Arrangement. This guidance is intended to help entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement, primarily to determine whether the arrangement includes a sale or license of software. The guidance will be effective for us beginning January 1, 2016. Early adoption is permitted. We have elected not to early adopt. The adoption of this guidance is not expected to have a material impact on our condensed consolidated financial statements.

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09 regarding ASC Topic 606, Revenue from Contracts with Customers. The standard provides principles for recognizing revenue for the transfer of promised goods or services to customers with the consideration to which the entity expects to be entitled in

exchange for those goods or services. The guidance will be effective for us beginning January 1, 2018. Early adoption is not permitted. We are

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

evaluating the accounting, transition and disclosure requirements of the standard and cannot currently estimate the financial statement impact of adoption.

Note 3. Marketable Securities

At June 30, 2015 and December 31, 2014, respectively, marketable securities consisted of the following (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
June 30, 2015				
U.S. agency obligations	\$ 145,414	\$ 16	\$(5	) \$ 145,425
Money market mutual funds	8,015	—	—	8,015
	153,429	16	(5	) 153,440
Included in cash and cash equivalents	20,535	—	—	20,535
Included in marketable securities	\$ 132,894	\$ 16	\$(5	) \$ 132,905
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
December 31, 2014				
U.S. agency obligations	\$ 177,297	\$ 4	\$(44	) \$ 177,257
U.S. treasury securities	5,580	1	—	5,581
Money market mutual funds	1,919	—	—	1,919
	184,796	5	(44	) 184,757
Included in cash and cash equivalents	3,480	—	—	3,480
Included in marketable securities	\$ 175,093	\$ 5	\$(41	) \$ 175,057
Included in marketable securities, noncurrent	\$ 6,223	\$ —	\$(3	) \$ 6,220

Note 4. Fair Value Measurements

We measure our financial assets and liabilities at fair value at each reporting period using a fair value hierarchy that requires that we maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's classification within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Three levels of inputs may be used to measure fair value:

Level 1—Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2—Include other inputs that are directly or indirectly observable in the marketplace.

Level 3—Unobservable inputs that are supported by little or no market activity.

The fair value of marketable securities included in the Level 2 category is based on observable inputs, such as quoted prices for similar assets at the measurement date; quoted prices in markets that are not active; or other inputs that are observable, either directly or indirectly. These values were obtained from a third-party pricing service and were evaluated using pricing models that vary by asset class and may incorporate available trade, bid and other market information and price quotes from well-established third party pricing vendors and broker-dealers. There have been no changes in valuation techniques in the periods presented. We have no financial assets or liabilities measured using Level 3 inputs. There were no significant transfers between Levels 1 and 2 assets as of June 30, 2015 and December 31, 2014. The following tables present information about our assets that are measured at fair value on a recurring basis using the above input categories (in thousands):

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

	Level 1	Level 2	Total
June 30, 2015			
Cash equivalents:			
Money market mutual funds	8,015	—	8,015
U.S. agency obligations	—	12,520	12,520
Marketable securities:			
U.S. agency obligations	—	132,905	132,905
	\$8,015	\$145,425	\$153,440
	Level 1	Level 2	Total
December 31, 2014			
Cash equivalents:			
Money market mutual funds	\$1,919	\$—	\$1,919
U.S. agency obligations	—	1,561	1,561
Marketable securities:			
U.S. agency obligations	—	175,696	175,696
U.S. treasury securities	—	5,581	5,581
	\$1,919	\$182,838	\$184,757

Gross unrealized gains and losses for cash equivalents and marketable securities as of June 30, 2015 and December 31, 2014 were not material. We do not believe the unrealized losses represent other-than-temporary impairments based on our evaluation of available evidence as of June 30, 2015.

There were no realized gains or losses during the three months ended June 30, 2015. All of our marketable securities at June 30, 2015 mature within one year. As of December 31, 2014 those securities with maturities greater than one year are reflected in the noncurrent portion of our condensed consolidated balance sheets. Marketable securities on the balance sheets consist of securities with original or remaining maturities at the time of purchase of greater than three months, and the remainder of the securities is reflected in cash and cash equivalents.

Note 5. Property and Equipment

Property and equipment consisted of the following (in thousands):

	As of	
	June 30, 2015	December 31, 2014
Leasehold improvements	\$1,058	\$1,058
Computer equipment	3,641	3,247
Software	874	874
Capitalization of internal-use software	1,155	291
Furniture and equipment	301	301
Construction in process	537	—
Total	7,566	5,771
Accumulated depreciation	(3,051)	(2,141)
Property and equipment, net	\$4,515	\$3,630

Depreciation and amortization expense for the three months ended June 30, 2015 and 2014, was \$0.5 million and \$0.3 million, respectively, and \$0.9 million and \$0.6 million for the six months ended June 30, 2015 and 2014, respectively. Depreciation is recorded on a straight-line basis.

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

Note 6. Related Party Transactions and Variable Interest Entity

In the second quarter of 2015, we announced a strategic alliance with Lyra Health ("Lyra"), to develop and bring to market an integrated behavioral health solution. In connection with this strategic alliance, the Company made a \$3.1 million preferred stock investment in Lyra. Lyra is considered a related party to us because two of Lyra's co-founders serve on our board of directors, and Castlight's Chief Executive Officer, serves on Lyra's board. An independent committee of Castlight's board of directors, comprising of directors with no involvement in any external behavioral health business initiatives, approved the strategic alliance with and investment in Lyra.

Lyra Health was founded in 2015 to work with employers, health plans, and providers to improve behavioral health outcomes and plans to offer a complementary behavioral health service that combines technology with active care management to improve patient outcomes. As part of the strategic alliance Lyra's product will be integrated with Castlight Elevate for those customers who purchase the integrated solution. Castlight Elevate is an extension of the Castlight enterprise healthcare management platform which enables employees to research behavioral health services, make educated treatment choices, and commence care.

We have evaluated these transactions, including their related party aspects, and have determined that Lyra is a variable interest entity ("VIE") for Castlight. In determining that we are not the VIE's primary beneficiary, we considered qualitative and quantitative factors, including, but not limited to: which activities most significantly impact the VIE's economic performance and which party controls such activities; the characteristics of our involvement; and the obligation or likelihood for us to provide incremental financial support. Based on our evaluation, we determined that Castlight and our related parties collectively have power and benefits of the operations of VIE but that we are not the party most closely associated to the VIE. Accordingly, we are not required to consolidate the operations of the VIE. Our maximum exposure to loss as a result of our involvement with this unconsolidated VIE is limited to our investment of \$3.1 million and we are not obligated to provide incremental financial support to Lyra.

The investment in Lyra is accounted for under the cost method and is included under other assets in our condensed consolidated financial statements. We have not estimated the fair value of our investment because there have been no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investment. We will assess our investment for impairment on a quarterly basis or based on facts or circumstances that may require us to reassess the fair value of our investment.

Note 7. Deferred Revenue

Deferred revenue consisted of the following (in thousands):

	As of	
	June 30, 2015	December 31, 2014
Subscription	\$ 17,373	\$ 14,826
Professional services—implementation	3,622	2,974
Professional services—communications	3,130	2,908
Total current	24,125	20,708
Subscription	2,090	1,950
Professional services—implementation	4,816	4,327
Professional services—communications	732	375
Total noncurrent	7,638	6,652
Total	\$ 31,763	\$ 27,360

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

Note 8. Commitments and Contingencies

Legal Matters

On April 2, April 16, April 29, and May 4, 2015, purported securities class action lawsuits were filed in the Superior Court of the State of California, County of San Mateo, against us, certain of our current and former directors, executive officers, significant stockholders and underwriters associated with our IPO. The lawsuits, which were consolidated on July 22, 2015, were brought by purported stockholders of our company seeking to represent a class consisting of all those who purchased our stock pursuant and/or traceable to the Registration Statement and Prospectus issued in connection with our IPO. The lawsuits assert claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 and seek unspecified damages and other relief. We believe that the claims are without merit and intend to defend the lawsuits vigorously.

From time to time, we may become subject to other legal proceedings, claims or litigation arising in the ordinary course of business. In addition, we may receive letters alleging infringement of patents or other intellectual property rights. We do not believe that any liability from any reasonably foreseeable disposition of these legal actions and claims, individually or in the aggregate, would have a material effect on our business, operating results, cash flows or financial condition. The lawsuits described above are still in their early stages and the final outcome, including our liability, if any, with respect to the claims in the lawsuits, are uncertain. If an unfavorable outcome were to occur in the litigation, the impact could be material to our business, financial condition, cash flow or results of operations, depending on the specific circumstances of the outcome. We cannot make a reasonable estimate of the potential loss or range of loss, if any, arising from these matters. We accrue for loss contingencies when it is both probable that we will incur the loss and when we can reasonably estimate the amount of the loss or range of loss. If we determine that a loss is reasonably possible and can reasonably estimate the range of the loss, then we disclose the range of the loss.

Leases and Contractual Obligations

We lease office space under noncancelable operating leases in San Francisco, California. On May 21, 2015, we entered into a new office space lease in San Francisco, California, in order to expand our office facilities. The lease extends to June 30, 2021, with a five year renewal option. The total rent obligation under the lease is \$12.8 million. There were no other material changes in our contractual obligations from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014. Please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources" in our Annual Report on Form 10-K for a description of our contractual obligations.

Note 9. Stockholders' Equity

Common Stock

As of June 30, 2015, we had 54,678,735 shares of Class A common stock and 39,574,120 shares of Class B common stock outstanding.

Stock Options Activity

A summary of stock option activity for the six months ended June 30, 2015 is as follows (in thousands, except share and per share amounts):

	Options Outstanding	Weighted- Average Exercise Price	Aggregate Intrinsic Value
Balance at December 31, 2014	16,392,539	\$4.40	\$128,541
Stock option grants	491,900	\$8.95	

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Stock options exercised	(3,107,786)	\$1.02	
Stock options canceled	(1,766,650)	\$6.80	
Balance at June 30, 2015	12,010,003		\$5.11	\$53,906

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

The total grant-date fair value of stock options granted during the six months ended June 30, 2015 and 2014 was \$2.3 million and \$28.4 million, respectively.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-valuation model with the following assumptions and fair value per share:

	Six Months Ended June 30,	
	2015	2014
Volatility	53%	60%
Expected life (in years)	6.17	5.0-6.2
Risk-free interest rate	1.38%-1.91%	1.53%-1.99%
Dividend yield	—%	—%

As of June 30, 2015, we had \$27.7 million in unrecognized compensation cost related to non-vested stock options, which is expected to be recognized over a weighted-average period of approximately 2.8 years.

Restricted Stock Units

A summary of restricted stock unit activity for the six months ended June 30, 2015 is as follows :

	Number of Shares Outstanding	Weighted- Average Grant Date Fair Value
Balance at December 31, 2014	1,398,893	\$11.06
Restricted Stock Units granted	3,318,000	\$8.73
Restricted Stock Units vested	—	\$—
Restricted Stock Units forfeited	(316,900	) \$10.26
Balance at June 30, 2015	4,399,993	\$9.36

As of June 30, 2015, there was a total of \$38.3 million in unrecognized compensation cost related to restricted stock units, which is expected to be recognized over a weighted-average period of approximately 3.6 years.

In June 2015, we awarded performance stock units (PSUs) to certain employees. The number of shares that will eventually vest depends on achievement of performance targets for 2015, as determined by the compensation committee of our board of directors, and may range from 0 percent to 150 percent of the targeted award amount. The PSUs will vest over the period of two years in quarterly installments subject to recipients' continued service through the vesting date of November 15, 2017 in order to earn the shares. The compensation expense associated with the PSUs is expensed using the accelerated method.

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CASTLIGHT HEALTH, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(unaudited)

Note 10. Income Taxes

The effective tax rate for the three and six months ended June 30, 2015 and 2014 was zero percent, primarily as a result of the estimated tax loss for the year and the change in valuation allowance.

There were no material changes to unrecognized tax benefits in the three and six months ended June 30, 2015, and we do not anticipate that unrecognized tax benefits will significantly increase or decrease in the next 12 months. At June 30, 2015, all unrecognized tax benefits are subject to a full valuation allowance and, if recognized, will not affect the effective tax rate.

Note 11. Net Loss per Share

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share is computed by giving effect to all potential shares of common stock, including Preferred Stock and outstanding stock options and warrants, to the extent dilutive. Basic and diluted net loss per share was the same for each period presented as the inclusion of all potential shares of common stock outstanding would have been anti-dilutive.

Net loss is allocated based on the contractual participation rights of the Class A and Class B common stock as if the earnings for the year have been distributed. As the liquidation and dividend rights are identical, the net loss is allocated on a proportionate basis.

The following table presents the calculation of basic and diluted net loss per share for our common stock (in thousands, except per share data):

	Three Months Ended June 30,				Six Months Ended June 30,			
	2015		2014		2015		2014	
	Class A	Class B	Class A	Class B	Class A	Class B	Class A	Class B
Net loss	\$(13,086)	\$(8,126)	\$(18,671)	\$(3,105)	\$(25,658)	\$(15,197)	\$(43,850)	\$(2,207)
Weighted-average shares used to compute basic and diluted net loss per share	57,870	35,934	76,755	12,765	58,282	34,519	50,731	2,553
Basic and diluted net loss per share	\$(0.23)	\$(0.23)	\$(0.24)	\$(0.24)	\$(0.44)	\$(0.44)	\$(0.86)	\$(0.86)

The following securities were excluded from the calculation of diluted net loss per share for common stock because their effect would have been anti-dilutive for the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Stock options and restricted common stock	16,410	17,908	16,410	17,908
Warrants	115	115	115	115
Total	16,525	18,023	16,525	18,023

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ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are subject to the “safe harbor” created by those sections. Forward-looking statements are based on our management’s beliefs and assumptions and on information currently available to our management. In some cases, you can identify forward-looking statements by terms such as “may,” “will,” “should,” “could,” “goal,” “would,” “expect,” “plan,” “anticipate,” “estimate,” “project,” “predict,” “potential” and similar expressions intended to identify forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors, which may cause our actual results, performance, time frames or achievements to be materially different from any future results, performance, time frames or achievements expressed or implied by the forward-looking statements. We discuss many of these risks, uncertainties and other factors in this Quarterly Report on Form 10-Q in greater detail under the section titled “Risk Factors” set forth in Part II, Item 1A in this Quarterly Report on Form 10-Q. Given these risks, uncertainties and other factors, you should not place undue reliance on these forward-looking statements. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this filing. You should read this Quarterly Report on Form 10-Q completely and with the understanding that our actual future results may be materially different from what we expect. We hereby qualify our forward-looking statements by these cautionary statements. Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

All references to “Castlight,” “Castlight Health,” “we,” “us,” “our” or the “Company” mean Castlight Health, Inc. and its subsidiaries, except where it is made clear that the term means only the parent company.

Castlight Health, Castlight, Castlight Medical, Castlight Essentials, Castlight Pharmacy, Castlight Rewards, Castlight Reference-Based Pricing, Castlight Protect, Castlight Insights, Castlight Controls, Castlight Connect, Castlight Care and Castlight Dental are trademarks and/or registered trademarks of Castlight Health, Inc. in the United States and other countries. Other company and product names may be trademarks of the respective companies with which they are associated.

Overview

Castlight is a pioneer in a new category of cloud-based software that enables enterprises to understand and manage health care spending as a strategic business investment, and help employees and their families make more informed medical decisions based on factors such as cost, quality and patient experience. Our Enterprise Healthcare Management solutions allow our customers to conquer the complexity of the existing health care system by providing personalized, actionable information to their employees, implementing technology-enabled benefit designs and integrating disparate systems and applications. Our comprehensive technology offering aggregates complex, large-scale data and applies sophisticated analytics to make health care data transparent and useful. We deploy consumer-oriented applications that deliver strong employee engagement and enable employers to integrate disparate benefit programs into one platform available to employees and their families.

Since our inception in 2008, we have been committed to improving the efficiency of the U.S. health care industry. From 2008 to 2010, we focused our efforts on research and development to build our consumer health care database, our analytic capabilities and the initial version of our cloud-based application, Castlight Essentials (previously, Castlight Medical). After its release in 2010, we have continued to enhance that application, as well as release new applications, including Castlight Pharmacy, Castlight Rewards, Castlight Elevate, Castlight Protect and Castlight

Dental. These applications are delivered to our customers, and their employees and families, via our cloud-based offering and leverage consumer-oriented design principles that drive engagement and ease of use.

We market and sell our Enterprise Healthcare Management solutions to self-insured companies in a broad range of industries and to governmental entities. As of June 30, 2015, we had 181 signed customers, of which more than 150 customers have implemented our offering, which we refer to as launched customers. In comparison, we had 168 signed customers, including 115 launched customers, as of December 31, 2014. We sell our offering solely in the United States, and we market to our customers and potential customers primarily through our direct sales force.

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We generate revenue from sales of subscriptions, including support, and professional services primarily related to the implementation of our offering, including extensive communications support to drive adoption by our customer's employees and their families. Historically, we have derived a substantial majority of our subscription revenue from Castlight Essentials. Our subscription fees are based on the number of employees and adult dependents that employers identify as eligible to use our offering, which typically includes all of our customers' U.S. employees and adult dependents that receive health benefits. Our agreements with customers generally have terms of three years.

Our costs to implement our offering mainly include personnel-related costs for deployment of our applications that are expensed as incurred. However, the related revenue is deferred until our applications are ready for use by the customer. Revenue is then recognized ratably over the related contract term. As a result, for a typical customer, we generate negative gross margin during the implementation phase and positive gross margin thereafter. Accordingly, during periods of rapid growth, when the proportion of customers that we are implementing is high, we incur significant gross losses related to professional services. We expect overall gross margin to improve over time as the number of our launched customers grows in relation to the number of customers in the implementation phase. We intend to continue to invest aggressively in the success of our customers, expand our commercial operations and further develop our offering. As a result of these and other factors, we expect to continue to incur operating losses for the foreseeable future and may need to raise additional capital through equity and debt financings in order to fund our operations.

Key Factors Affecting Our Performance

Sale of Additional Applications. Our revenue growth rate and long-term profitability are affected by our ability to sell additional applications to our customer base. To date, a substantial majority of our revenue has come from sales of subscriptions of Castlight Essentials. We believe that there is a significant opportunity to sell subscriptions to other applications as our customers become more familiar with our offering and seek to address additional needs.

Annual Net Dollar Retention Rate and Average Annual Revenue. We believe that our ability to retain our customers and expand their subscription revenue growth over time will be an indicator of the stability of our revenue base and the long-term value of our customer relationships. We observed an annual net dollar retention rate of 103% for our signed customer base, for the year ended December 31, 2014. Additionally, our average annual revenue per launched customer grew approximately 17% for the year ended December 31, 2014 compared to the year ended December 31, 2013. We calculate annual net dollar retention rate for a given period as the aggregate annualized subscription contract value as of the last day of that year from those customers that were also customers as of the last day of the prior year, divided by the aggregate annualized subscription contract value from all customers as of the last day of the prior year. We calculate annualized subscription contract value for each customer as the expected monthly recurring revenue of our customers multiplied by 12. Recurring revenue excludes one-time fees. We calculate average annual revenue per launched customer for a given period, as the annualized revenue as of the last day of the year, divided by average customers launched during the same period.

Implementation Timelines. Our ability to convert backlog into revenue and improve our gross margin depends on how quickly we complete customer implementations. Our implementation timelines vary from customer to customer based on the source and condition of the data we receive from third parties, the configurations that we agree to provide and the size of the customer. Our implementation timelines for Castlight Essentials are typically three to nine months after entering into an agreement with a customer. Our implementation timelines for our other applications currently range from approximately three months to longer than twelve months.

Professional Services Model. We believe our professional services capabilities support the adoption of our subscription offerings. As a result, our sales efforts have been focused primarily on our subscription offering, rather than the profitability of our professional services business. Our professional services are generally priced on a fixed-fee basis and the costs incurred to complete these services, which consist mainly of personnel-related costs, have been greater than the amount charged to the customer. We also do not have standalone value for our implementation services for accounting purposes. Accordingly, we recognize implementation services revenue in the same manner as

the associated subscription revenue. Prior to launching an individual customer, we incur significant costs associated with implementation activities, which we record as cost of revenue. Since we do not recognize significant revenues from an individual customer until we launch, we generate a negative gross margin at the customer level during the implementation period.

Seasonality. A significantly higher proportion of our customers enter into new subscription agreements with us or renew previous agreements in the third and fourth quarters of the year compared to the first and second quarters. This

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seasonality is related to the employee benefits cycle, as customers typically want to make our applications available at the beginning of a new benefits year, which generally occurs in the first quarter. This seasonality is not immediately apparent in our revenue because we do not begin recognizing revenue from new customer agreements until we have implemented our offering, based on the implementation timelines discussed above. Therefore, revenue recognized in any quarter is primarily from customer agreements entered into in prior quarters. In addition, the mix of customers paying monthly, quarterly, or annually varies from quarter to quarter and impacts our deferred revenue balance. As a result of variability in our billing and implementation timelines, the deferred revenue balance does not represent the total value of our customer contracts, nor do changes in deferred revenue serve as a reliable indicator of our future subscription revenue.

Components of Results of Operations

Revenue

We generate revenue from subscription fees from customers for access to the applications they select, including basic customer service support. We also earn revenue from professional services primarily related to the implementation of our offering, including extensive communications support to drive adoption by our customers' employees and their dependents.

We recognize subscription fees on a straight-line basis ratably over the contract term beginning when our applications are implemented and ready for launch, which is based on the implementation timelines discussed above. Our customer agreements generally have a term of three years. We generally invoice our customers in advance on a monthly, quarterly or annual basis. Amounts that have been invoiced are initially recorded as deferred revenue. Amounts that have not been invoiced are not reflected in our consolidated financial statements. We generally invoice our implementation services upon contract signing on a fixed-fee basis, which is generally when we commence work. As a result of variability in our billing terms, the deferred revenue balance does not represent the total value of our customer contracts, nor do changes in deferred revenue serve as a reliable indicator of our future subscription revenue in a given period. The weighted average billing term for customers that we billed in the second quarter of 2015 was 5.3 months. The cumulative weighted average billing term for all customers signed as of June 30, 2015 was 5.2 months.

Costs and Operating Expenses

Cost of Revenue. Cost of revenue consists of the cost of subscription revenue and cost of professional services revenue.

Cost of subscription revenue primarily consists of data fees, employee-related expenses (including salaries, benefits and stock-based compensation) related to hosting costs of our cloud-based service, cost of subcontractors, expenses for service delivery (which includes call center support), allocated overhead, the costs of data center capacity, amortization of internal-use software and depreciation of owned computer equipment and software.

Cost of professional services revenue consists primarily of employee-related expenses associated with these services, the cost of subcontractors and travel costs, and allocated overhead. The time and costs of our customer implementations vary based on the source and condition of the data we receive from third parties, the configurations that we agree to provide and the size of the customer.

Our cost of revenue is expensed as we incur the costs. However, the related revenue is deferred until our applications are ready for use by the customer and then recognized as revenue ratably over the related contract term. Therefore, we expense the cost incurred to provide our applications and services prior to the recognition of the corresponding revenue.

Gross profit consists of total revenue, less cost of revenue. Gross margin is the percentage of gross profit to revenue.

Sales and Marketing. Sales and marketing expenses consist primarily of employee-related expenses (including salaries, sales commissions and bonuses, benefits and stock-based compensation), travel-related expenses and marketing programs. Commissions earned by our sales force that can be associated specifically with the noncancelable portion of a subscription contract are deferred and amortized over the noncancelable period.

Accordingly, commission expense can be materially impacted by changes in the termination provisions of customer contracts that we execute in a given period compared with previous periods.

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Research and Development. Research and development expenses consist primarily of employee-related expenses (including salaries, bonuses, benefits and stock-based compensation) and costs associated with subcontractors.

General and Administrative. General and administrative expenses consist primarily of employee-related expenses (including salaries and bonuses, benefits and stock-based compensation) for finance and accounting, legal, human

resources and management information systems personnel, legal costs, professional fees and other corporate expenses.

Results of Operations

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

	Three Months Ended June 30,		Six Months Ended June 30,		
	2015	2014	2015	2014	
	(percentages of revenue)				
Revenue:					
Subscription	93	% 91	% 93	% 90	%
Professional services	7	% 9	% 7	% 10	%
Total revenue	100	% 100	% 100	% 100	%
Cost of revenue:					
Cost of subscription	16	% 27	% 16	% 30	%
Cost of professional services	29	% 43	% 29	% 44	%
Total cost of revenue	45	% 70	% 45	% 74	%
Gross margin percentage	55	% 30	% 55	% 26	%
Operating expenses:					
Sales and marketing	95	% 142	% 99	% 167	%
Research and development	40	% 52	% 40	% 58	%
General and administrative	35	% 43	% 35	% 45	%
Total operating expenses	170	% 237	% 174	% 270	%
Operating loss	(115	)% (207	)% (119	)% (244)%
Other income, net	—	% —	% —	% —	%
Net loss	(115	)% (207	)% (119	)% (244)%
Revenue					

	Three Months Ended June 30,			Six Months Ended June 30,				
	2015	2014	% Change	\$ Change	2015	2014	% Change	\$ Change
	(dollars in thousands)							
Revenue:								
Subscription	\$17,278	\$9,576	80%	\$7,702	\$32,184	\$17,039	89%	\$15,145
Professional services	1,232	957	29%	275	2,277	1,870	22%	407
Total revenue	\$18,510	\$10,533	76%	\$7,977	\$34,461	\$18,909	82%	\$15,552

The overall increase in both subscription and professional services revenue for the three and six months ended June 30, 2015, was primarily attributable to revenue from customers launched in the trailing twelve months ended June 30, 2015. Our launched customer base grew from 90 as of June 30, 2014 to more than 150 launched customers as of June 30, 2015.

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Costs and Operating Expenses

	Three Months Ended June 30,				Six Months Ended June 30,			
	2015	2014	% Change	\$ Change	2015	2014	% Change	\$ Change
	(dollars in thousands)							
Cost of revenue:								
Subscription	2,932	2,915	1	% \$17	5,451	5,627	(3)	)% \$(176)
Professional services	5,322	4,502	18	% 820	9,975	8,373	19	% 1,602
Total cost of revenue	\$8,254	\$7,417	11	% \$837	\$15,426	\$14,000	10	% \$1,426
Gross margin (loss)								
percentage								
Subscription	83.0	% 69.6	%		83.1	% 67.0	%	
Professional services	(332)	)% (370)	)%		(338)	)% (348))%	
Total gross margin	55.4	% 29.6	%		55.2	% 26.0	%	
percentage								
Gross profit	\$10,256	\$3,116	229	% \$7,140	\$19,035	\$4,909	288	% \$14,126

Cost of subscription revenue remained flat for both the three and six months ended June 30, 2015, as the increase in costs associated with the customer support function (driven by increased launches) were offset by cost efficiencies gained from data center transition in the second quarter of 2014 to two relatively lower cost data centers in Colorado and Arizona.

Cost of professional services revenue increased for both the three and six months ended June 30, 2015, primarily due to employee-related expenses as we continue to hire talent to support our customer implementations and invest in our strategic growth objectives. We are continuing to invest in data infrastructure to enable more efficient implementations of Castlight Pharmacy and to further expand our ability to work with additional data sources associated with our newest products. We expect these investments to continue through third quarter of 2015.

Overall gross margin blends the effects of the gross margins derived from subscription revenues and the gross losses generated from professional services. Gross margin for the three and six months ended June 30, 2015 improved compared to three and six months ended June 30, 2014, primarily as the cost of subscription revenue as a percentage of total revenue continues to decrease over time, as a number of the associated costs, such as costs associated with data acquisition, include fixed elements. Improvements in overall gross margin for the three and six months ended June 30, 2015 are attributable to continued growth in the number of launched customers in relation to customers in the implementation phase.

Sales and Marketing

	Three Months Ended June 30,				Six Months Ended June 30,			
	2015	2014	% Change	\$ Change	2015	2014	% Change	\$ Change
	(dollars in thousands)							
Sales and marketing	\$17,641	\$14,947	18	% \$2,694	\$34,104	\$31,507	8	% \$2,597

The increase in sales and marketing for both the three and six months ended June 30, 2015 was primarily driven by increases in employee-related expenses as we continue to expand our sales force to address new opportunities and grow our customer base. The increases attributable to employee-related expenses were \$2.7 million and \$5.1 million for the three and six months ended June 30, 2015, respectively. The increase in the six months ended June 30, 2015 was offset by a \$2.5 million charge related to warrants that was recorded in the first half of 2014, only.

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Research and Development

	Three Months Ended June 30,				Six Months Ended June 30,			
	2015	2014	% Change	\$ Change	2015	2014	% Change	\$ Change
	(dollars in thousands)							
Research and development	\$7,391	\$5,476	35	% \$1,915	\$13,985	\$11,003	27	% \$2,982

The increase in research and development for both the three and six months ended June 30, 2015 was primarily attributable to increase in employee-related expenses as we continued to hire engineering talent in San Francisco and internationally to drive innovation and new products, such as Castlight Elevate. For the three and six months ended June 30, 2015, employee-related expenses increased \$1.1 million and \$1.6 million, respectively. Additionally, we allocated fewer engineering resources to customer launch activity representing efficiencies gained in implementations. This reduced allocation resulted in an increase of \$0.6 million and \$0.9 million for the three and six months ended June 30, 2015 respectively.

General and Administrative

	Three Months Ended June 30,				Six Months Ended June 30,			
	2015	2014	% Change	\$ Change	2015	2014	% Change	\$ Change
	(dollars in thousands)							
General and administrative	\$6,517	\$4,519	44	% \$1,998	\$11,980	\$8,529	40	% \$3,451

The increase in general and administrative expense for both the three and six months ended June 30, 2015 primarily attributable to increases in employee-related expenses associated with growth in headcount as we invested in our internal talent acquisition team to support the growth of our business. These employee-related expenses contributed to \$1.1 million and \$2.0 million increase for the three and six months ended June 30, 2015, respectively. Also contributing to the increase were facility and equipment infrastructure spending to support planned hiring, which contributed to \$0.8 million and \$1.2 million increase for the three and six months ended June 30, 2015, respectively.

Liquidity and Capital Resources

	Six Months Ended June 30,	
	2015	2014
	(in thousands)	
Net cash used in operating activities	\$(30,401	) \$(35,635
Net cash provided by (used in) investing activities	41,777	(142,041
Net cash provided by financing activities	2,732	187,790
Net increase in cash and cash equivalents	\$14,108	\$10,114

As of June 30, 2015, our principal sources of liquidity were cash, cash equivalents and marketable securities totaling \$164.4 million, which were held for working capital purposes. Our cash, cash equivalents and marketable securities are comprised primarily of U.S. agency obligations and money market funds.

Since our inception, we have financed our operations primarily through sales of equity securities and, to a lesser extent, payments from our customers. We believe that our existing cash, cash equivalents and marketable securities will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Our future

capital requirements will

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depend on many factors including our growth rate, subscription renewal activity, the timing and extent of spending to support development efforts, our expansion of sales and marketing activities, the introduction of new and enhanced services offerings and the continuing market acceptance of our cloud-based applications. We may in the future enter into arrangements to acquire or invest in complementary businesses, services and technologies and intellectual property rights. We may be required to seek additional equity or debt financing. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us, or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be adversely affected.

Operating Activities

For the six months ended June 30, 2015, cash used in operating activities was \$30.4 million. Cash used in operations improved primarily due to a decrease in net loss from \$46.1 million, in the first half of 2014 to \$40.9 million, in the first half of 2015. The net loss in the second quarter of 2015 was adjusted for \$11.5 million in non-cash expenses that primarily included stock-based compensation of \$8.1 million, and amortization of deferred commissions of \$1.7 million. Working capital uses of cash included a decrease in accrued expenses of \$3.2 million, primarily as a result of payout of annual bonuses and an increase in prepaid expenses and other assets of \$1.8 million. These were offset by an increase in deferred revenue of \$4.4 million as a result of contracts signed in the period with associated upfront fees and annual billings for launched customers.

Investing Activities

Cash provided by (used in) investing activities for the six months ended June 30, 2015, and 2014 was \$41.8 million, and \$(142.0) million, respectively. The increase in cash provided, was primarily the result of the timing of purchases, sales and maturities of marketable securities, net of \$47.6 million, and \$(141.2) million, respectively. This increase was offset by investment of \$3.1 million in Lyra Health, a behavioral health technology company, and purchases of property, plant and equipment, which includes leasehold improvements for our new facilities.

Financing Activities

For the six months ended June 30, 2015, financing activities provided \$2.7 million, primarily from cash proceeds resulting from issuance of stock under our equity incentive plans. The decrease in cash from financing activities compared to six months ended June 30, 2014, is primarily related to the proceeds from our initial public offering in the prior year.

Contractual Obligations and Commitments

Our principal commitments primarily consist of obligations under leases for office space and co-location facilities for data center capacity. On May 21, 2015, we entered into a new office space lease, under which we will lease approximately 36,000 square feet at 150 Spear Street, San Francisco, California, in order to expand our office facilities. The term of the lease extends to June 30, 2021, with a five year renewal option. The total rent obligation under the lease is \$12.8 million. Our existing lease agreements provide us with the option to renew and generally provide for rental payments on a graduated basis.

There were no other material changes in our contractual obligations from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014. Please see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources" in our Annual Report on Form 10-K for a description of our contractual obligations.

Off-Balance Sheet Arrangements

During the periods presented, we did not have, nor do we currently have, any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. We are therefore not exposed to the financing, liquidity, market or credit risk that could arise if we had engaged in those types of relationships.

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Critical Accounting Policies and Estimates

During the six months ended June 30, 2015, there were no significant changes to our critical accounting policies and estimates as described in our Annual Report on Form 10-K for the year ended December 31, 2014.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Sensitivity

We had cash, cash equivalents and marketable securities totaling \$164.4 million at June 30, 2015 and \$198.7 million as of December 31, 2014. This amount was invested primarily in U.S. agency obligations, U.S. treasury securities and money market funds. The cash, cash equivalents and short-term marketable securities are held for working capital purposes. Our investments are made for capital preservation purposes. We do not enter into investments for trading or speculative purposes. All our investments are denominated in U.S. dollars.

Our cash equivalents and our portfolio of marketable securities are subject to market risk due to changes in interest rates. Fixed rate securities may have their market value adversely affected due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However, because we classify our marketable securities as “available for sale”, no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or declines in fair value are determined to be other-than-temporary. Our fixed-income portfolio is subject to interest rate risk.

An immediate increase of 100-basis points in interest rates would have resulted in a \$0.4 million market value reduction in our investment portfolio as of June 30, 2015. All of our investments earn less than 100-basis points and as a result, an immediate decrease of 100-basis points in interest rates would have increased the market value by \$0.1 million as of June 30, 2015. This estimate is based on a sensitivity model that measures market value changes when changes in interest rates occur. Fluctuations in the value of our investment securities caused by a change in interest rates (gains or losses on the carrying value) are recorded in other comprehensive income, and are realized only if we sell the underlying securities.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the supervision and participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), as of the end of the period covered by this report.

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on our management’s evaluation, our principal executive officer and principal financial officer concluded that, as of June 30, 2015, our disclosure controls and procedures were designed at a reasonable assurance level and were effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in

Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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Part II. OTHER INFORMATION

Item 1. Legal Proceedings

On April 2, April 16, April 29, and May 4, 2015, purported securities class action lawsuits were filed in the Superior Court of the State of California, County of San Mateo, against us, certain of our current and former directors, executive officers, significant stockholders and underwriters associated with our IPO. The lawsuits, which were consolidated on July 22, 2015, were brought by purported stockholders of our company seeking to represent a class consisting of all those who purchased our stock pursuant and/or traceable to the Registration Statement and Prospectus issued in connection with our IPO. The lawsuits assert claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933 and seek unspecified damages and other relief. We believe that the claims are without merit and intend to defend the lawsuits vigorously.

From time to time, we may become subject to other legal proceedings, claims or litigation arising in the ordinary course of business. In addition, we may receive letters alleging infringement of patents or other intellectual property rights. We do not believe that any liability from any reasonably foreseeable disposition of these legal actions and claims, individually or in the aggregate, would have a material effect on our business, operating results, cash flows or financial condition. The lawsuits described above are still in their early stages and the final outcome, including our liability, if any, with respect to the claims in the lawsuits, are uncertain. If an unfavorable outcome were to occur in the litigation, the impact could be material to our business, financial condition, cash flow or results of operations, depending on the specific circumstances of the outcome. We cannot make a reasonable estimate of the potential loss or range of loss, if any, arising from these matters. We accrue for loss contingencies when it is both probable that we will incur the loss and when we can reasonably estimate the amount of the loss or range of loss. If we determine that a loss is reasonably possible and can reasonably estimate the range of the loss, then we disclose the range of the loss.

Item 1A. Risk Factors

The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that adversely affect our business. If any of the following risks actually occur, our business, financial condition, results of operations and future prospects could be materially and adversely affected. In that event, the market price of our Class B common stock could decline, and you could lose part or all of your investment.

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Risks Related to Our Business

We have a history of significant losses, which we expect to continue, and we may never achieve or sustain profitability in the future.

We have incurred significant net losses in each year since our incorporation in 2008 and expect to continue to incur net losses for the foreseeable future. We experienced net losses of \$85.9 million, \$62.2 million and \$35.0 million, during the years ended December 31, 2014, 2013 and 2012, respectively and \$40.9 million for the six months ended, June 30, 2015. As of June 30, 2015, we had an accumulated deficit of \$258.0 million. The losses and accumulated deficit were primarily due to the substantial investments we made to grow our business, enhance our technology and offering through research and development and acquire and support customers. We anticipate that cost of revenue and operating expenses will increase substantially in the foreseeable future as we seek to continue to grow our business, enhance our offering and acquire customers. These efforts may prove more expensive than we currently anticipate, and we may not succeed in increasing our revenue sufficiently to offset these higher expenses. Many of our efforts to generate revenue from our business are new and unproven, and any failure to increase our revenue or generate revenue from new applications and services could prevent us from attaining profitability. Furthermore, to the extent we are successful in increasing our customer base, we could also incur increased losses because costs associated with entering into customer agreements are generally incurred up front, while customers are generally billed over the term of the agreement. Our prior losses, combined with our expected future losses, have had and will continue to have an adverse effect on our stockholders' equity and working capital. We expect to continue to incur operating losses for the foreseeable future and may never become profitable on a quarterly or annual basis, or if we do, we may not be able to sustain profitability in subsequent periods. As a result of these factors, we may need to raise additional capital through debt or equity financings in order to fund our operations, and such capital may not be available on reasonable terms, if at all.

Our limited operating history makes it difficult to evaluate our current business and future prospects.

We were founded in 2008, began building the first version of Castlight Essentials (previously, Castlight Medical) in 2009, did not complete our first customer sale and implementation until 2010 and did not make substantial investments in sales and marketing until 2012. Our limited operating history limits our ability to forecast our future operating results and such forecasts are subject to a number of uncertainties, including our ability to plan for and model future growth.

We have encountered and will continue to encounter risks and uncertainties frequently experienced by new and growing companies in rapidly changing industries, such as determining appropriate investments of our limited resources, market adoption of our existing and future offerings, competition from other companies, acquiring and retaining customers, managing customer deployments, hiring, integrating, training and retaining skilled personnel, developing new applications and services, determining prices for our applications, unforeseen expenses and challenges in forecasting accuracy. If our assumptions regarding these and other similar risks and uncertainties, which we use to plan our business, are incorrect or change as we gain more experience operating our business or due to changes in our industry, or if we do not address these risks and uncertainties successfully, our operating and financial results could differ materially from our expectations and our business could suffer.

In addition, we may need to change our current operations infrastructure in order for us to achieve profitability and scale our operations efficiently, which makes our future prospects even more difficult to evaluate. For example, in order to grow sales of our Enterprise Healthcare Management solutions to smaller customers in a financially sustainable manner, we may need to further automate implementations, tailor our offering and modify our go-to-market approaches to reduce our service delivery and customer acquisition costs. If we fail to implement these changes on a timely basis or are unable to implement them effectively due to our limited experience with the new infrastructure or factors beyond our control, our business may suffer.

The market for our offering is immature and volatile, and if it does not develop, if it develops more slowly than we expect, or if our offering does not drive employee engagement, the growth of our business will be harmed.

The enterprise health care management software market is new and unproven, and it is uncertain whether it will achieve and sustain high levels of demand and market adoption. Our success depends to a substantial extent on the willingness of employers to increase their use of our Enterprise Healthcare Management solutions, the ability of our applications to increase employee engagement, as well as on our ability to demonstrate the value of our offering to customers and their employees and to develop new applications that provide value to customers and users. If employers do not perceive the benefits of our offering or our offering does not drive employee engagement, then our market might not develop at all, or it might develop more slowly than we expect, either of which could significantly adversely affect our operating results. In addition, we have limited insight

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into trends that might develop and affect our business. We might make errors in predicting and reacting to relevant business, legal and regulatory trends, which could harm our business. If any of these events occur, it could materially adversely affect our business, financial condition or results of operations.

If our security measures are breached and unauthorized access to a customer's data are obtained, our offering may be perceived as insecure, we may incur significant liabilities, our reputation may be harmed and we could lose sales and customers.

Our offering involves the storage and transmission of customers' proprietary information, as well as protected health information, or PHI, of our customers' employees and their dependents, which is regulated under the Health Insurance Portability and Accountability Act of 1996 and its implementing regulations, collectively HIPAA. Because of the extreme sensitivity of this information, the security features of our offering are very important. If our security measures, some of which are managed by third parties, are breached or fail, unauthorized persons may be able to obtain access to sensitive customer or employee data, including HIPAA-regulated protected health information. A security breach or failure could result from a variety of circumstances and events, including third-party action, employee negligence or error, malfeasance, computer viruses, attacks by computer hackers, failures during the process of upgrading or replacing software, databases or components thereof, power outages, hardware failures, telecommunication failures, user errors, and catastrophic events.

If our security measures were to be breached or fail, our reputation could be severely damaged, adversely affecting customer or investor confidence, customers may curtail their use of or stop using our offering and our business may suffer. In addition, we could face litigation, damages for contract breach, penalties and regulatory actions for violation of HIPAA and other applicable laws or regulations and significant costs for remediation and for measures to prevent future occurrences. In addition, any potential security breach could result in increased costs associated with liability for stolen assets or information, repairing system damage that may have been caused by such breaches, incentives offered to customers or other business partners in an effort to maintain the business relationships after a breach and implementing measures to prevent future occurrences, including organizational changes, deploying additional personnel and protection technologies, training employees and engaging third-party experts and consultants. While we maintain insurance covering certain security and privacy damages and claim expenses we may not carry insurance or maintain coverage sufficient to compensate for all liability and in any event, insurance coverage would not address the reputational damage that could result from a security incident.

We outsource important aspects of the storage and transmission of customer information, and thus rely on third parties to manage functions that have material cyber-security risks. These outsourced functions include services such as software design and product development, software engineering, database consulting, call center operations, co-location data centers, data-center security, IT, network security and Web application firewall services. We attempt to address these risks by requiring outsourcing subcontractors who handle customer information to sign business associate agreements contractually requiring those subcontractors to adequately safeguard personal health data and in some cases by requiring such outsourcing subcontractors to undergo third-party security examinations. However, we cannot assure you that these contractual measures and other safeguards will adequately protect us from the risks associated with the storage and transmission of customers proprietary and protected health information.

We may experience cyber-security and other breach incidents that may remain undetected for an extended period. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until launched against us, we may be unable to anticipate these techniques or to implement adequate preventive measures. In addition, in the event that our customers authorize or enable third parties to access their data or the data of their employees on our systems, we cannot ensure the complete integrity or security of such data in our systems as we would not control access. If an actual or perceived breach of our security occurs, or if we are unable to effectively resolve such breaches in a timely manner, the market perception of the effectiveness of our security measures could be harmed and we could lose sales and customers.

Our quarterly results may fluctuate significantly, which could adversely impact the value of our Class B common stock.

Our quarterly results of operations, including our revenue, gross margin, net loss and cash flows, may vary significantly in the future, and period-to-period comparisons of our operating results may not be meaningful. Accordingly, our quarterly results should not be relied upon as an indication of future performance. Our quarterly financial results may fluctuate as a result of a variety of factors, many of which are outside of our control, including, without limitation, those listed elsewhere in this “Risk Factors” section and those listed below:

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- the addition or loss of large customers, including through acquisitions or consolidations of such customers; seasonal and other variations in the timing of the sales of our offering, as a significantly higher proportion of our customers enter into new subscription agreements with us or renew previous agreements in the third and fourth quarters of the year compared to the first and second quarters;
- the timing of recognition of revenue, including possible delays in the recognition of revenue due to lengthy and sometimes unpredictable implementation timelines;
- failure to meet our contractual commitments under service-level agreements with our customers;
- the amount and timing of operating expenses related to the maintenance and expansion of our business, operations and infrastructure;
- our access to pricing and claims data managed by health plans and other third parties, or changes to the fees we pay for that data;
- the timing and success of introductions of new applications, services and pricing by us or our competitors or any other
- change in the competitive dynamics of our industry, including consolidation among competitors, customers or strategic partners;
- our ability to attract new customers;
- customer renewal rates and the timing and terms of customer renewals;
- network outages or security breaches;
- the mix of applications and services sold during a period;
- general economic, industry and market conditions;
- the timing of expenses related to the development or acquisition of technologies or businesses and potential future charges for impairment of goodwill from acquired companies; and
- impact of new accounting pronouncements.

We are particularly subject to fluctuations in our quarterly results of operations since the costs associated with entering into customer agreements and implementing our offerings are generally incurred prior to launch, while we generally recognize revenue over the term of the agreement beginning at launch. In addition, some of our contracts with customers provide for one-time bonus payments if our offering achieves certain metrics, such as a certain rate of employee engagement, which may lead to additional fluctuations in our quarterly operating results. In certain contracts, employee engagement may refer to the number of first time registrations by employees of our customers and in other cases it may refer to return usage of our applications by employees. Any fluctuations in our quarterly results may not accurately reflect the underlying performance of our business and could cause a decline in the trading price of our Class B common stock.

If we fail to manage our rapid growth effectively, our expenses could increase more than expected, our revenue may not increase and we may be unable to implement our business strategy.

We have experienced rapid growth in recent periods, which puts strain on our business, operations and employees. For example, our revenue has increased from \$10.5 million for the three months ended June 30, 2014 to \$18.5 million for the three months ended June 30, 2015, and our customer base grew from 130 customers at June 30, 2014 to 181 customers at June 30, 2015. We also grew from 339 full-time employees to 430 full-time employees during that time. We anticipate that we will continue to rapidly expand our operations. To manage our current and anticipated future growth effectively, we must continue to maintain and enhance our IT infrastructure, financial and accounting systems and controls. We must also attract, train and retain a significant number of qualified sales and marketing personnel, customer support personnel, professional services personnel, software engineers, technical personnel and management personnel, and the availability of such personnel, in particular software engineers, may be constrained. These and similar challenges, and the related costs, may be exacerbated by the fact that our headquarters are located in the San Francisco Bay Area.

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A key aspect to managing our growth is our ability to scale our capabilities to implement our offering satisfactorily with respect to both large and demanding enterprise customers, who currently comprise the substantial majority of our customer base, as well as smaller customers. Large customers often require specific features or functions unique to their particular business processes, which at a time of rapid growth or during periods of high demand, may strain our implementation capacity and hinder our ability to successfully implement our offering to our customers in a timely manner. We may also need to make further investments in our technology and automate portions of our offering or services to decrease our costs, particularly as we grow sales of our Enterprise Healthcare Management solutions to smaller customers. If we are unable to address the needs of our customers or their employees, or our customers or their employees are unsatisfied with the quality of our offering or services, they may not renew their agreements, seek to cancel or terminate their relationship with us or renew on less favorable terms.

Failure to effectively manage our rapid growth could also lead us to over-invest or under-invest in development and operations, result in weaknesses in our infrastructure, systems or controls, give rise to operational mistakes, financial losses, loss of productivity or business opportunities and result in loss of employees and reduced productivity of remaining employees. Our growth is expected to require significant capital expenditures and might divert financial resources from other projects such as the development of new applications and services. In addition, data and content fees, which are one of our primary operational costs, are not fixed as they vary based on the source and condition of the data we receive from third parties, and if they remain variable or increase over time, we would not be able to realize the economies of scale that we expect as we grow renewals and implementation of new customers, which would negatively impact our gross margin. If our management is unable to effectively manage our growth, our expenses might increase more than expected, our revenue may not increase or might grow more slowly than expected and we might be unable to implement our business strategy. The quality of our offering might also suffer, which could negatively affect our reputation and harm our ability to retain and attract customers.

We incur significant upfront costs in our customer relationships, and if we are unable to maintain and grow these customer relationships over time, we are likely to fail to recover these costs and our operating results will suffer.

We devote significant resources and incur significant upfront costs to establish relationships with our customers and implement our offering and related services, particularly in the case of large enterprises that, often request or require specific features or functions unique to their particular business processes. Accordingly, our operating results will depend in substantial part on our ability to deliver a successful customer experience and persuade our customers to maintain and grow their relationship with us over time. For example, if we are not successful in implementing our offering or delivering a successful customer experience, a customer could terminate or fail to renew their agreement with us, we would lose or be unable to recoup the significant upfront costs that we had expended on such customer and our operating results would suffer. As we are growing rapidly, our customer acquisition costs could outpace our build-up of recurring revenue, and we may be unable to reduce our total operating costs through economies of scale such that we are unable to achieve profitability.

Our ability to deliver our full offering to customers depends in substantial part on our ability to access pricing and claims data managed by a limited number of health plans and other third parties.

In order to deliver the full functionality offered by our Enterprise Healthcare Management solutions, we need access, on behalf of our customers, to sources of pricing and claims data, much of which is managed by a limited number of health plans and other third parties. We have developed various long-term and short-term data-sharing relationships with certain health plans and other third parties, including most, but not all, of the largest health plans in the United States. We are limited in our ability to offer the full functionality of our offering to customers of health plans with whom we do not have a data-sharing arrangement.

The terms of the agreements under which we have access to data managed by health plans and other third parties vary, which can impact the offering we are able to deliver. Many of our agreements with health plans and third parties have terms that limit our access to and permitted uses of claims or pricing data to the data associated with our mutual customers. Also, some agreements may be terminated if the underlying customer contracts do not continue, or may otherwise be subject to termination or non-renewal.

The health plans and other third parties that we currently work with may, in the future, change their position and limit or eliminate our access to pricing and claims data, increase the costs charged to us for access to data, provide data to us in more limited or less useful formats, or restrict our permitted uses of data. Furthermore, some health plans have developed or are developing their own proprietary price and quality estimation tools and may perceive continued cooperation with us as a

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competitive disadvantage and choose to limit or discontinue our access to pricing and claims data. Failure to continue to maintain and expand our access to pricing and claims data may adversely impact our ability to continue to serve existing customers and expand our offering to new customers.

If our access to pricing and claims data is reduced or becomes more costly to us, our ability to compete in the marketplace or to grow our revenue could be impaired and our operating results would suffer.

If our existing customers do not continue or renew their agreements with us, renew at lower fee levels or decline to purchase additional applications and services from us, our business and operating results will suffer.

We expect to derive a significant portion of our revenue from renewal of existing customer agreements and sales of additional applications and services to existing customers. As a result, achieving a high renewal rate of our customer agreements and selling additional applications and services is critical to our future operating results.

However, we have a limited operating history, and to date have not yet reached the end of the original term for the vast majority of our existing customer agreements. Accordingly, we do not yet have enough experience with customer renewals to predict our customer renewal rate and may experience significantly more difficulty than we anticipate in renewing existing customer agreements. Factors that may affect the renewal rate for our offering and our ability to sell additional applications and services include:

• the price, performance and functionality of our offering;

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