Cornerstone OnDemand Inc
Form 10-Q
May 15, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2012

OR

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

For the transition period from to

Commission File Number 001-35098

Cornerstone OnDemand, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**13-4068197**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**

1601 Cloverfield Blvd.

Suite 620 South

Santa Monica, CA 90404

(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code:

(310) 752-0200

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 x 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 x No ¨

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

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding as of May 7, 2012
Common Stock	**49,774,141**

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CORNERSTONE ONDEMAND, INC.

QUARTERLY REPORT ON FORM 10-Q

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TRADEMARKS

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

CORNERSTONE ONDEMAND, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

(unaudited)

	March 31, 2012	December 31, 2011
Assets		
Cash and cash equivalents	$ 87,186	$ 85,409
Accounts receivable, net	25,096	34,110
Deferred commissions	3,895	3,537
Prepaid expenses and other current assets	4,015	3,789
Total current assets	120,192	126,845
Capitalized software development costs, net	4,760	4,106
Property and equipment, net	4,182	3,663
Other assets, net	1,541	748
Total Assets	$ 130,675	$ 135,362
Liabilities and Stockholders Equity		
Liabilities:		
Accounts payable	$ 5,357	$ 3,834
Accrued expenses	5,631	8,039
Deferred revenue, current portion	53,003	52,338
Capital lease obligations, current portion	1,701	1,617
Debt, current portion	456	265
Other liabilities	752	996
Total current liabilities	66,900	67,089
Other liabilities, non-current	1,145	806
Deferred revenue, net of current portion	2,834	3,542
Capital lease obligations, net of current portion	1,447	1,056
Long-term debt, net of current portion	957	409
Total liabilities	73,283	72,902
Commitments and contingencies (Note 7)		
Stockholders Equity:		
Common stock, $0.0001 par value; 1,000,000 shares authorized, 49,702 and 49,274 shares issued and outstanding at March 31, 2012 and December 31, 2011	5	5
Additional paid-in capital	230,110	226,916
Accumulated deficit	(172,757)	(164,651)
Accumulated other comprehensive income	34	190
Total stockholders equity	57,392	62,460

Total Liabilities and Stockholders Equity	$ 130,675	$ 135,362

See accompanying notes to unaudited condensed consolidated financial statements.

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CORNERSTONE ONDEMAND, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Revenue	$ 24,002	$ 15,747
Cost of revenue	6,844	4,579
Gross profit	17,158	11,168
Operating expenses:		
Sales and marketing	16,237	9,845
Research and development	3,093	2,322
General and administrative	5,954	3,553
Total operating expenses	25,284	15,720
Loss from operations	(8,126)	(4,552)
Other income (expense):		
Interest expense	(143)	(684)
Change in fair value of preferred stock warrant liabilities		(42,559)
Other, net	239	236
Other income (expense), net	96	(43,007)
Loss before provision for income taxes	(8,030)	(47,559)
Provision for income taxes	(82)	(34)
Net loss	$ (8,112)	$ (47,593)
Accretion of redeemable preferred stock		(5,208)
Net loss attributable to common stockholders	$ (8,112)	$ (52,801)
Net loss per share attributable to common stockholders, basic and diluted	$ (0.16)	$ (3.65)
Weighted average common shares outstanding, basic and diluted	49,384	14,453

See accompanying notes to unaudited condensed consolidated financial statements.

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CORNERSTONE ONDEMAND, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands)

(unaudited)

	Three Months Ended March 31,	
	2012	**2011**
Net loss	$ (8,112)	$ (47,593)
Foreign currency translation adjustment, net of tax	(157)	(82)
Total comprehensive loss	$ (8,269)	$ (47,675)

See accompanying notes to unaudited condensed consolidated financial statements.

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CORNERSTONE ONDEMAND, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Cash flows from operating activities:		
Net loss	$ (8,112)	$ (47,593)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	1,161	823
Non-cash interest expense	68	387
Change in fair value of preferred stock warrant liabilities		42,559
Unrealized foreign exchange gain	(201)	
Stock-based compensation expense	2,499	805
Non-cash charitable contribution of common stock		193
Changes in operating assets and liabilities:		
Accounts receivable	9,225	5,744
Deferred commissions	(279)	(305)
Prepaid expenses and other assets	(269)	(1,077)
Accounts payable	1,426	1,474
Accrued expenses	(2,301)	(10)
Deferred revenue	(362)	(1,415)
Other liabilities	174	(194)
Net cash provided by operating activities	3,029	1,391
Cash flows from investing activities:		
Purchases of property and equipment	(46)	(64)
Capitalized software costs	(1,264)	(663)
Net cash used in investing activities	(1,310)	(727)
Cash flows from financing activities:		
Proceeds from initial public offering, net of underwriting discounts and commissions		90,539
Payments of initial public offering costs		(1,256)
Proceeds from issuance of preferred stock upon warrant exercises		3,163
Repayment of debt	(210)	(9,072)
Principal payments under capital lease and financing obligations	(449)	(398)
Proceeds from stock option exercises	594	179
Proceeds from common stock warrant exercises		159
Net cash (used in) provided by financing activities	(65)	83,314
Effect of exchange rate changes on cash and cash equivalents	123	
Net increase in cash and cash equivalents	1,777	83,978
Cash and cash equivalents at beginning of period	85,409	7,067

Cash and cash equivalents at end of period	$ 87,186	$ 91,045
Supplemental cash flow information:		
Cash paid for interest	$ 75	$ 325
Cash paid for income taxes	$ 200	$ 43
Non-cash investing and financing activities:		
Conversion of convertible preferred stock to common stock	$	$ 132,775
Assets acquired under capital leases and other financing arrangements	$ 1,775	$ 193
Capitalized assets financed by accounts payable and accrued expenses	$ 47	$
Capitalized stock-based compensation	$ 87	$ 42
Deferred offering costs included in accounts payable and accrued expenses	$	$ 2,377

See accompanying notes to unaudited condensed consolidated financial statements.

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CORNERSTONE ONDEMAND, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Company Overview

Cornerstone OnDemand, Inc. (Cornerstone or the Company) was incorporated on May 24, 1999 in the state of Delaware and began its principal operations in November 1999.

The Company is a global provider of a comprehensive learning and talent management solution delivered as Software-as-a-Service (SaaS). The Company s solution is designed to enable organizations to meet the challenges they face in empowering and maximizing the productivity of their human capital. These challenges include developing employees throughout their careers, engaging all employees effectively, improving business execution, cultivating future leaders, and integrating with an organization s extended enterprise of clients, vendors and distributors by delivering training, certification programs and other content.

The Company is headquartered in Santa Monica, California and has offices in Paris, London, Munich, Mumbai, Madrid and Tel Aviv.

Initial Public Offering

In March 2011, the Company completed its initial public offering whereby it sold 7,500,000 shares of common stock at a price of $13.00 per share. The Company s shares are traded on the NASDAQ Global Market. The Company received proceeds from its initial public offering of $90.5 million, net of underwriting discounts and commissions but before offering expenses of $3.7 million.

As part of the offering, an additional 4,575,000 shares of common stock were sold by certain existing stockholders at a price of $13.00 per share. The Company did not receive any of the proceeds from the sale of such shares by the selling stockholders.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, the financial statements include all adjustments (consisting of normal recurring adjustments) considered necessary for the fair statement of the interim periods presented. Results for the three months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012, for any other interim period or for any other future year.

The condensed consolidated balance sheet at December 31, 2011 has been derived from the audited financial statements at that date, but does not include all of the disclosures required by GAAP. The accompanying condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company s Form 10-K filed with the Securities and Exchange Commission on March 6, 2012.

Recent Accounting Pronouncements

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurement.* The primary focus of this standard is the convergence of accounting requirements for fair value measurements and related financial statement disclosures under U.S. GAAP and International Financial Reporting Standards (IFRS). While this ASU does not significantly change existing guidance for measuring fair value, it does require additional disclosures about fair value measurements and changes the wording of certain requirements in the guidance to achieve consistency with IFRS. This guidance was effective for interim and annual periods beginning after December 15, 2011. The Company adopted this standard during the three months ended March 31, 2012. The adoption did not have any material impact on the financial statement disclosures.

In June 2011, the FASB issued ASU No. 2011-05, *Presentation of Comprehensive Income*. This update requires companies to present reclassification adjustments included in other comprehensive income on the face of the financial statements and allows companies to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. It also eliminates the option for companies to present the components of other comprehensive income as part of the statement of changes

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in stockholders equity. This guidance was effective for fiscal periods beginning after December 15, 2011. The adoption of this standard did not have a material effect on the Company s financial position, results of operations, or cash flows. The Company adopted this standard in the three months ended March 31, 2012 by including a new separate statement labeled Consolidated Statements of Comprehensive Income. As of March 31, 2012, accumulated other comprehensive income comprises foreign currency translation adjustments.

2. NET LOSS PER SHARE ATTRIBUTABLE TO COMMON STOCKHOLDERS

The following table presents our basic and diluted loss per share attributable to common stockholders (in thousands, except per share amounts):

	For the Three Months Ended March 31, 2012	For the Three Months Ended March 31, 2011
Net loss attributable to common stockholders	$ (8,112)	$ (52,801)
Weighted-average shares of common stock outstanding	49,384	14,453
Net loss per share attributable to common stockholders basic and diluted	$ (0.16)	$ (3.65)

At March 31, 2012 and 2011, anti-dilutive shares excluded from the calculation of diluted net loss per share attributable to common stockholders were (in thousands):

	March 31, 2012	March 31, 2011
Options to purchase common stock	6,052	5,699
Common stock subject to repurchase	25	60
Common stock warrants	130	735
Total shares excluded from net loss per share attributable to common stockholders	**6,207**	**6,494**

As of March 31, 2012, immediately exercisable options to purchase 75,000 shares of common stock had been granted, of which an option to purchase 60,000 shares of common stock was early exercised during September 2010. Of the 60,000 shares issued upon early exercise of such option during September 2010, 25,000 and 60,000 were unvested and subject to the Company s repurchase right at March 31, 2012 and March 31, 2011, respectively, and were therefore excluded from the calculation of weighted-average shares of common stock used in calculating net loss per share.

3. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value represents the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The fair value hierarchy is based on the following three levels of inputs, of which the first two are considered observable and the last one is considered unobservable:

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access at the measurement date.

Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 Unobservable inputs.

Observable inputs are based on market data obtained from independent sources. At December 31, 2010, the Company s warrants to purchase preferred stock were measured using unobservable inputs that required a high level of judgment to determine fair value, and thus were classified as Level 3 inputs. All of the warrants to purchase preferred stock were exercised in March 2011, and the Company recorded changes to the fair value of the warrants through the respective warrant exercise dates. Upon the completion of the Company s initial public offering in March 2011, all of the then-outstanding shares of preferred stock were automatically converted into shares of common stock on a one-for-one basis.

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Assets and liabilities measured at fair value on a recurring basis include the following as of March 31, 2012 and December 31, 2011 (in thousands):

	March 31, 2012				December 31, 2011			
	Fair Value	Level 1	Level 2	Level 3	Fair Value	Level 1	Level 2	Level 3
Cash equivalents	$ 71,521	$ 71,521	$	$	$ 71,521	$ 71,521	$	$

At March 31, 2012, cash equivalents of $71.5 million consisted of money market funds with original maturity dates of three months or less backed by U.S. Treasury bills.

The following table summarizes the changes in the fair value of preferred stock warrant liability for the three months ended March 31, 2011 (in thousands):

Fair value at December 31, 2010	$ 39,756
Changes in fair value of preferred stock warrant liabilities recorded in the statement of operations	42,559
Exercise of preferred stock warrants	(82,315)
Fair value at March 31, 2011	$

4. DEBT

Silicon Valley Bank

In August 2010, the Company entered into a $15.0 million credit facility with Silicon Valley Bank (SVB Credit Facility), with a maturity of August 2012. During September 2010, the amount available under the line of credit was reduced by $0.3 million due to the issuance of an irrevocable standby letter of credit in relation to a sales arrangement with a state agency. During May 2011, the amount available under the line of credit was further reduced by $0.3 million due to the issuance of an irrevocable standby letter of credit in relation to the Company s corporate credit card agreement.

During May 2011, the Company amended the SVB Credit Facility to allow for loan advances, in addition to the amount available under the existing line of credit, of up to an aggregate of $3.0 million for the purchase of software and equipment. Advances for the purchase of software and equipment may be drawn through May 2012, have an interest rate of prime rate plus 1.25%, and are amortized monthly over the remaining term, which is the lessor of either 12 or 36 months and May 2015, payable in equal monthly installments of principal plus accrued interest. In May 2011, the Company borrowed approximately $0.7 million under this facility for the purchase of software and equipment. At March 31, 2012, loan advances of $0.5 million were outstanding.

The SVB Credit Facility is subject to certain financial covenants, including a liquidity coverage ratio and achievement of defined performance criteria. At March 31, 2012, $15.7 million was available to support future borrowings under the SVB Credit Facility.

5. STOCK-BASED AWARDS

The following table summarizes the stock option activity for the three months ended March 31, 2011 (in thousands, except per share and term information):

	0000000000	0000000000	0000000000	0000000000
	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual	Aggregate Intrinsic Value

				Term		
Outstanding, December 31, 2011	5,475	$	6.04	8.3	$	66,817
Granted	673	$	18.84	9.8		
Exercised	(427)	$	1.39	6.2		
Forfeited	(39)	$	12.49			
Outstanding, March 31, 2012	**5,682**	**$**	**7.86**	**8.4**	**$**	**79,444**

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	0000000000 Shares	0000000000 Weighted-Average Exercise Price	0000000000 Weighted-Average Remaining Contractual Term	0000000000 Aggregate Intrinsic Value
Exercisable at December 31, 2011	2,233	$ 2.24	7.2	$ 35,742
Vested and expected to vest at December 31, 2011	5,262	$ 5.83	8.2	$ 65,328
Exercisable at March 31, 2012	2,210	$ 3.62	7.4	$ 40,270
Vested and expected to vest at March 31, 2012	5,592	$ 7.83	8.3	$ 78,356

Unrecognized compensation expense relating to stock options was $19.2 million at March 31, 2012, which is expected to be recognized over a weighted-average period of 2.8 years.

The aggregate grant date fair value of stock options granted for the three months ended March 31, 2012 was $6.5 million.

Restricted Stock Units

At March 31, 2012, 370,000 of nonvested shares restricted stock units were outstanding at March 31, 2012. Unrecognized compensation expense related to nonvested restricted stock units was $2.5 million at March 31, 2012, which is expected to be recognized into expense over the weighted-average period of 2.4 years.

Stock-Based Compensation

Stock-based compensation expense related to stock options and restricted stock units is included in the following line items in the accompanying Consolidated Statement of Operations for the three months ended March 31, 2012 and 2011 (in thousands):

	Three Months Ended March 31, 2012	2011
Cost of revenue	$ 491	$ 46
Sales and marketing expense	478	212
Research and development expense	144	114
General and administrative expense	1,386	433
Total	**$ 2,499**	**$ 805**

6. INCOME TAXES

The Company s income tax expense was $82,000 and the effective income tax rate was (1.0)% for the three months ended March 31, 2012, as compared to an income tax expense of $34,000 and an effective income tax rate of (0.1)% for the three months ended March 31, 2011. The increase in the income tax expense primarily relates to additional foreign income taxes. The Company s effective tax rate differs from the statutory rate primarily due to the change in the valuation allowance on the Company s deferred tax assets and foreign income taxes.

The Company recorded valuation allowances on the net deferred tax assets of the Company s U.S. operations and certain foreign jurisdictions and does not anticipate recording an income tax benefit related to these deferred tax assets. The Company will reassess the realization of deferred tax assets each reporting period and will be able to reduce the valuation allowance to the extent that the financial results of these operations improve and it becomes more likely than not that the deferred tax assets are realizable.

The Company is subject to U.S. federal income tax, state income tax and various foreign income taxes. The Company is subject to examination for years after 2008 and 2007 for its U.S. federal income tax returns and state income tax returns, respectively. The Company is subject to examination by various foreign jurisdictions for years after 2007. The Company believes it has adequately reserved for its uncertain tax positions; however, there is no assurance that taxing authorities will not propose adjustments that are more or less than our expected outcome. It is not expected that the amount of unrecognized tax benefits will be recognized in the next twelve months. In addition, the Company does not expect the change in uncertain tax positions to have a material impact on its financial position, results of operations or liquidity.

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7. COMMITMENTS AND CONTINGENCIES

Guarantees and Indemnifications

The Company has made guarantees and indemnities under which it may be required to make payments to a guaranteed or indemnified party in relation to certain transactions, including revenue transactions in the ordinary course of business. In connection with certain facility leases, the Company has agreed to indemnify its lessors for certain claims arising from the facility or the lease. The Company is obligated to indemnify its directors and officers to the maximum extent permitted under the laws of the State of Delaware. However, the Company has a directors and officers insurance policy that may reduce its exposure in certain circumstances and may enable it to recover a portion of future amounts that may be payable, if any. The duration of the guarantees and indemnities varies and, in many cases, is indefinite but subject to statutes of limitations. To date, the Company has made no payments related to these guarantees and indemnities. The Company estimates the fair value of its indemnification obligations as insignificant based on this history and the Company s insurance coverage and therefore has not recorded any liability for these guarantees and indemnities in the accompanying consolidated balance sheets.

License and Capital Lease Commitments

On January 13, 2012, the Company entered into an agreement to purchase intellectual property rights related to a software application for $0.8 million which was financed through a third-party debt agreement. Payments of approximately $0.2 million are due in 2012, 2013, 2014 and 2015.

During the three months ended March 31, 2012, the Company financed the purchase of equipment through capital lease agreements that increased its capital lease commitments by approximately $1.0 million through 2015.

Litigation

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. If the Company determines that it is probable that a loss has been incurred and the amount is reasonably estimable, the Company will record a liability. The Company has determined that it does not have a potential liability related to any legal proceedings or claims that would individually or in the aggregate materially adversely affect its financial conditions or operating results.

8. SUBSEQUENT EVENTS

During April and May 2012, the Board of Directors granted stock options to purchase 769,364 shares of common stock at a weighted-average exercise price of $21.07 per share. The stock options vest over four years. On May 1, 2012, the Board of Directors granted restricted stock units for 88,812 shares of common stock which vest over two years.

During April 2012, the Company entered into operating leases in France and New Zealand, with operating lease commitments of approximately $0.4 million due through 2013 and also entered into an e-learning content reseller agreement with a third-party content provider. The Company is obligated to pay license fees under the e-learning content reseller agreement of $0.8 million in 2012, 2013 and 2014 under this agreement. During May 2012, the Company entered into a capital lease agreement that increased its capital lease commitments by approximately 0.2 million.

On April 5, 2012, the Company completed the acquisition of Sonar Limited, a New Zealand based cloud talent management solutions provider serving small business globally, for approximately $12.5 million in cash and 46,694 restricted shares of common stock of the Company, with a fair value of $1.0 million. As of the date of issuance of the interim financial statements for the quarter ended March 31, 2012, the initial accounting for the acquisition, including the allocation of the purchase price to the net tangible and intangible assets, is incomplete. The Company expects to complete the accounting for the acquisition during the quarter ending June 30, 2012.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements are any statements that look to future events and consist of, among other things, statements regarding our business strategies; anticipated future operating results and operating expenses; our ability to attract new clients to enter into subscriptions for our solution; our ability to service those clients effectively and induce them to renew and *upgrade their deployments of our solution; our ability to expand our sales organization to address effectively the new industries, geographies and types of organizations we intend to target; our ability to accurately forecast revenue and appropriately plan our expenses; market acceptance of enhanced solutions; alternate ways of addressing learning and talent management needs or new technologies generally by us and our competitors; continued acceptance of SaaS as an effective method for delivering learning and talent management solutions and other business management applications; the attraction and retention of qualified employees and key personnel; our ability to protect and defend our intellectual property; costs associated with defending intellectual property infringement and other claims; events in the markets for our solution and*

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alternatives to our solution, as well as in the United States and global markets generally; future regulatory, judicial and legislative changes in our industry; and changes in the competitive environment in our industry and the markets in which we operate. In addition, forward-looking statements also consist of statements involving trend analyses and statements including such words as may, believe, could, anticipate, would, might, plan, expect, and similar expressions or the negative of such terms or other comparable terminology. These forward-looking statements speak only as of the date of this Form 10-Q and are subject to business and economic risks. As such, our actual results could differ materially from those set forth in the forward-looking statements as a result of the factors set forth below in Part II, Item 1A, Risk Factors, and in our other reports filed with the Securities and Exchange Commission. We assume no obligation to update the forward-looking statements to reflect events that occur or circumstances that exist after the date on which they were made.

The following discussion should be read in conjunction with our unaudited condensed consolidated financial statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q.

Overview

We are a leading global provider of a comprehensive learning and talent management solution delivered as software-as-a-service, or SaaS. We enable organizations to meet the challenges they face in empowering their people and maximizing the productivity of their human capital. These challenges include developing employees throughout their careers, engaging all employees effectively, improving business execution, cultivating future leaders and enabling an organization s extended enterprise of clients, vendors and distributors by delivering training, certification programs and other content. We currently have 891 clients who use our solution to empower approximately 8.2 million users across 180 countries and 32 languages.

Our product offering consists of four integrated clouds for recruiting, learning, performance, and extended enterprise. Clients can purchase these clouds individually and easily add and integrate additional clouds at any time. We offer a number of cross-cloud tools for analytics and reporting, employee profile management, employee on-boarding and e-learning content aggregation. We also provide consulting services for configuration and training for our solution as well as third-party e-learning content for use with our solution.

We founded our business in 1999 to improve access to education through the distribution of online educational content to individuals, small businesses and large corporations. Our distribution model was built using Internet technologies that are now known as software-as-a-service. When the Internet bubble burst in 2000, we focused on corporations that needed tools to manage compliance and on-boarding of employees as well as to link learning to employee performance, leadership development and knowledge management. As a result of our work with clients to address their particular challenges, we had as early as 2001 developed the foundation for a comprehensive learning and talent management cloud-based solution that included functionality for learning management and performance management. In 2006, we added our extended enterprise functionality which helps clients extend learning and talent management to their customers, vendors and distributors. During the first quarter of 2012, we added our recruiting cloud. The recruiting cloud supports the modern ways that businesses source, recruit, hire and onboard new employees.

Global 500 companies were among our first clients. In our early years, we focused primarily on building our account management and support capabilities to be able to service these large clients more effectively. Sales were initially constrained by the resistance of some large corporations to purchase SaaS solutions. By the mid-2000s, however, our market opportunity increased significantly with both the adoption of SaaS solutions generally by large enterprises and the market s recognition of learning and talent management as a distinct industry.

In response to these positive trends, we raised our first round of institutional venture capital in May 2007. We used this capital to serve clients across multiple industries, geographies and enterprise types by increasing the number of our direct sales personnel, both domestically and internationally, and by expanding our indirect channels through distribution relationships. Between December 2007 and March 31, 2012, our number of users increased from 859,000 to approximately 8.2 million. In 2009, after a highly competitive process involving a number of potential providers, ADP chose to enter into a distributor agreement with us that allows ADP to sell our solution globally.

On April 5, 2012, we completed the acquisition of Sonar Limited, a New Zealand cloud-based talent management solutions provider serving small business globally. Sonar Limited s talent management solutions will be rebranded as Cornerstone Small Business and will be sold principally to clients with less than 500 employees, while our integrated clouds will continue to be sold to companies with 500 or more employees. Cornerstone Small Business will not be integrated into the Cornerstone solution.

We generate most of our revenue from sales of our solution pursuant to multi-year client agreements. Our sales typically involve competitive processes, with sales cycles that generally vary in duration from two to nine months depending on the size of the potential client. We price our solution based on the number of clouds the client can access and the permitted number of users with access to each cloud. Our client agreements typically have terms of three years. We also generate revenue from consulting services for configuration, training, and consulting, as well as from the resale or hosting of third-party e-learning content.

We generate sales of our solution primarily through our direct sales teams and, to a lesser extent, indirectly through our distributors. We intend to accelerate our investment in our direct sales and distribution activities to continue to address our market opportunity.

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We target our sales and marketing efforts at large and mid-sized clients, and our solution can be used in all industry vertical segments. We also continue to market and sell to existing clients, who may renew their subscriptions, add clouds, broaden the deployment of our solution across their organizations and increase the usage of our solution over time. For 2010 and 2011, no single client or distributor accounted for more than 10% of our revenue. Our number of clients has grown from 105 at December 31, 2007 to 481 at December 31, 2010 and to 805 at December 31, 2011. Our number of clients has grown to 891 at March 31, 2012 from 805 at December 31, 2011 and 562 at March 31, 2011.

We recognize revenue from subscriptions ratably over the term of the client agreement and revenue from consulting services as these services are performed. We generally invoice our clients a portion of the annual subscription fees upfront for multi-year subscriptions and upfront for consulting services. For amounts not invoiced in advance for multi-year subscriptions and consulting services, we invoice under various terms over the subscription and service periods. We record amounts invoiced for portions of annual subscription periods that have not occurred or services that have not been performed as deferred revenue on our balance sheet. With the growth in the number of clients, our revenue has grown to $24.0 million for the three months ended March 31, 2012 from $15.7 million for the three months ended March 31, 2011.

We have historically experienced seasonality in terms of when we enter into client agreements. We sign a significantly higher percentage of agreements with new clients, as well as renewal agreements with existing clients, in the fourth quarter of each year and usually sign a significant portion of these agreements during the last month, and with respect to each quarter, often the last two weeks, of the quarter. We believe this seasonality is driven by several factors, most notably the tendency of procurement departments at our enterprise clients to purchase technology at the end of a quarter or calendar year, possibly in order to use up their available quarterly or annual funding allocations, or to be able to deploy new talent management capabilities prior to the beginning of a new financial or performance period. As the terms of most of our client agreements are measured in full year increments, agreements initially entered into the fourth quarter or last month of any quarter will generally come up for renewal at that same time in subsequent years. This seasonality is reflected to a much lesser extent, and sometimes is not immediately apparent, in our revenue, due to the fact that we recognize subscription revenue over the term of the client agreement, which is generally three years. In addition, this seasonality is reflected in changes in our deferred revenue balance, which generally is impacted by the timing in which we enter into agreements with new clients, the timing of when we invoice new clients, the timing in which we invoice existing clients for annual subscription periods, and the timing in which we recognize revenue. Due to the seasonality of when we enter into client agreements, generally in the fourth quarter of each year, and the timing in which we invoice our clients for annual subscription periods, our deferred revenue decreased slightly to $55.8 million at March 31, 2012 from $55.9 million at December 31, 2011. We expect this seasonality to continue in the future, which may cause fluctuations in certain of our operating results and financial metrics, and thus limit our ability to predict future results.

We believe the market for learning and talent management remains large and underpenetrated, providing us with significant growth opportunities. We expect businesses and other organizations to continue to increase their spending on learning and talent management solutions in order to maximize productivity of their employees, manage changing workforce demographics and ensure compliance with global regulatory requirements. Historically, many of these software solutions have been human resource applications running on hardware located on organizations premises. However, we believe that just as organizations have increasingly chosen SaaS solutions for business applications such as sales force management, they are also increasingly adopting SaaS learning and talent management solutions.

We have focused on growing our business to pursue what we believe is a significant market opportunity, and we plan to continue to invest in building for growth. As a result, we expect our cost of revenue and operating expenses to increase in future periods. Sales and marketing expenses are expected to increase, as we continue to expand our direct sales teams, increase our marketing activities, and grow our international operations. Research and development expenses are expected to increase as we improve the existing functionality for our solution. We also believe that we must invest in maintaining a high degree of client service and support that is critical for our continued success. We plan to continue our policy of implementing best practices across our organization, expanding our technical operations and investing in our network infrastructure and services capabilities in order to support continued future growth. We also expect to incur additional general and administrative expenses as a result of both our growth and our continued transition to operating as a public company. In addition, to the extent that we make additional strategic acquisitions in the future, like our recent acquisition of Sonar Limited, our investments in operations may increase.

Our quarterly operating results have fluctuated in the past and may continue to fluctuate in the future based on a number of factors, many of which are beyond our control. In addition to those in the *Risk Factors* section of this Form 10-Q, such factors include:

- our ability to attract new clients;
- the timing and rate at which we enter into agreements for our solution with new clients;

the extent to which our existing clients renew their subscriptions for our solution and the timing of those renewals;

the extent to which our existing clients purchase additional clouds or add incremental users;

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- changes in the mix of our sales between new and existing clients;
- changes to the proportion of our client base that is comprised of enterprise or mid-sized organizations;
- seasonal factors affecting the demand for our solution;
- our ability to manage growth, including in terms of new clients, additional users and new geographies;
- the timing and success of competitive solutions offered by our competitors;
- changes in our pricing policies and those of our competitors; and
- general economic and market conditions.

One or more of these factors may cause our operating results to vary widely. As such, we believe that our quarterly results of operations may vary significantly in the future and that period-to-period comparisons of our operating results may not be meaningful and should not be relied upon as an indication of future performance.

Initial Public Offering

In March 2011, we completed our initial public offering whereby we sold 7,500,000 shares of common stock at a price of $13.00 per share. Our shares are traded on the NASDAQ Global Market. We received proceeds from our initial public offering of $90.5 million, net of underwriting discounts and commissions, but before offering expenses of $3.7 million.

As part of the offering, an additional 4,575,000 shares of common stock were sold by certain existing stockholders at a price of $13.00 per share, including 1,575,000 shares sold by such stockholders upon the exercise of the underwriters option to purchase additional shares. We did not receive any of the proceeds from the sale of such shares by the selling stockholders.

Metrics

We regularly review a number of metrics, including the following key metrics, to evaluate our business, measure our performance, identify trends affecting our business, formulate financial projections and make strategic decisions.

- *Bookings*. Under our revenue recognition policy, we generally recognize subscription revenue from our client agreements ratably over the terms of those agreements. For this reason, the major portion of our revenue for a period will be from client agreements signed in prior periods rather than new business activity during the current period. In order to assess our business performance with a metric that more fully reflects current period business activity, we track bookings, which is a non-GAAP financial measure defined as the sum of revenue and the change in the deferred revenue balance for the period. We include changes in the deferred revenue balance in bookings to reflect new business activity in the period evidenced by prepayments or billings under our billing policies arising from acquisition of new clients, sales of additional clouds to existing clients, the addition of incremental users by existing clients and client renewals. We exclude non-cash reductions of revenue related to the issuance of common stock warrants because these charges do not relate to sales activity in the period, and we do not consider the issuance of warrants to be indicative of our core operating performance. Bookings are affected by our billing terms, and any changes in those billing terms may shift bookings between periods. Due to the seasonality of our sales, bookings growth is inconsistent from quarter to quarter throughout a calendar year. For a reconciliation of bookings to revenue, please see *Results of Operations* *Revenue and Metrics*.

Number of clients. We believe that our ability to expand our client base is an indicator of our market penetration and the growth of our business as we continue to invest in our direct sales teams and distributors.

Number of users. Since our clients generally pay fees based on the number of users of our solution within their organizations, we believe the total number of users is an indicator of the growth of our business.

Key Components of Our Results of Operations

Sources of Revenue and Revenue Recognition

Our solution is designed to enable organizations to meet the challenges they face in maximizing the productivity of their human capital. We generate revenue from the following sources:

Subscriptions to Our Solution. Clients pay subscription fees for access to our comprehensive learning and talent management solution for a specified period of time, typically three years. Fees are based primarily on the number of clouds the client can access and the number of users having access to those clouds. We generally recognize revenue from subscriptions ratably over the term of the agreement.

Consulting Services. We offer our clients assistance in implementing our solution and optimizing its use. Consulting services include application configuration, system integration, business process re-engineering, change management and training services. Services are billed either on a time-and-material or a fixed-fee basis. These services are generally purchased as part of a subscription arrangement and are typically performed within the first several months of the

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arrangement. Clients may also purchase consulting services at any other time. Our consulting services are performed by us directly or by third-party service providers we hire. Clients may also choose to perform these services themselves or hire their own third-party service providers. We generally recognize revenue from consulting services using the proportional performance method over the period the services are performed.

E-learning Content. We resell third-party on-line training content, which we refer to as e-learning content, to our clients. We also host other e-learning content provided to us by our clients. We generally recognize revenue from the resale of e-learning content as it is delivered and recognize revenue from hosting as the hosting services are provided.

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Our client agreements generally include both a subscription to access our solution and related consulting services, and may also include e-learning content. Our agreements generally do not contain any cancellation or refund provisions other than in the event of our default.

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Cost of Revenue

Cost of revenue consists primarily of costs related to hosting our solution; personnel and related expenses, including stock-based compensation, for network infrastructure, IT support, consulting services and on-going client support; payments to external service providers; amortization of capitalized software costs and trademarks; licensing fees; and referral fees. In addition, we allocate a portion of overhead, such as rent, IT costs, depreciation and amortization and employee benefits costs, to cost of revenue based on headcount. The costs associated with providing consulting services are significantly higher as a percentage of revenue than the costs associated with providing access to our solution due to the labor costs to provide the consulting services.

Operating Expenses

Our operating expenses are as follows:

Sales and Marketing. Sales and marketing expenses consist primarily of personnel and related expenses for our sales and marketing staff, including salaries, benefits, bonuses, stock-based compensation and commissions; costs of marketing and promotional events, corporate communications, online marketing, product marketing and other brand-building activities; and allocated overhead.

We intend to continue to invest in sales and marketing and expect spending in these areas to increase as we continue to expand our business both domestically and internationally. We expect sales and marketing expenses to continue to be among the most significant components of our operating expenses.

Research and Development. Research and development expenses consist primarily of personnel and related expenses for our research and development staff, including salaries, benefits, bonuses and stock-based compensation; the cost of certain third-party service providers; and allocated overhead. Research and development costs, other than software development expenses qualifying for capitalization, are expensed as incurred.

We have focused our research and development efforts on continuously improving our solution. We believe that our research and development activities are efficient because we benefit from maintaining a single software code base for our solution. We expect research and development expenses to increase in absolute dollars in the future, as we scale our research and development department and expand our network infrastructure.

General and Administrative. General and administrative expenses consist primarily of personnel and related expenses for administrative, legal, finance and human resource staffs, including salaries, benefits, bonuses and stock-based compensation; professional fees; insurance premiums; other corporate expenses; and allocated overhead.

We expect our general and administrative expenses to increase as we continue to expand our operations, hire additional personnel and incur costs as a public company. We expect to incur increased expenses related to outside legal counsel assistance, accounting and auditing activities, compliance with the SEC requirements and enhancing our internal control environment through the adoption and administration of new corporate policies.

Other

Interest Expense. Interest expense consists primarily of interest expense from borrowings under our credit facility and our promissory notes; capital lease payments; amortization of debt issuance costs and debt discounts.

Change in Fair Value of Preferred Stock Warrant Liabilities. Preferred warrant liabilities are the result of warrants issued in connection with our long-term debt and preferred stock financings. Changes in the fair value of our preferred stock occur in connection with changes in the overall value of our company. Prior to the completion of our initial public offering, all of our warrants to purchase preferred stock were exercised, and as a result, we will no longer record any changes in the fair value of these liabilities in our statements of operations.

Other, Net. Other, net consists of income and expense associated with fluctuations in foreign currency exchange rates and other non-operating expenses. We expect interest income (expense) and other income (expense) to vary depending on the movement in foreign currency exchange rates and the related impact on our foreign exchange gain (loss).

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Provision for Income Taxes

The provision for income taxes is related to certain foreign income taxes. As we have incurred operating losses in all periods to date and recorded a full valuation allowance against our U.S. federal and state net deferred tax assets, we have not historically recorded a provision for federal and state income taxes.

Critical Accounting Policies and Estimates

Information with respect to our critical accounting policies which we believe have the most significant effect on our reported results and require subjective or complex judgments of management are contained in Management s Discussion and Analysis of Financial Condition and Results of Operations of our Form 10-K filed with the Securities and Exchange Commission on March 6, 2012.

As of March 31, 2012, there have been no material changes to our critical accounting policies since December 31, 2011.

Recent Accounting Pronouncements

For information regarding recent accounting pronouncements, refer to Note 1 of notes to condensed consolidated financial statements included in this Quarterly Report on Form 10-Q.

Results of Operations

The following table sets forth our results of operations for each of the periods indicated (in thousands). The period-to-period comparison of financial results is not necessarily indicative of future results.

	Three Months Ended March 31,	
	2012	2011
Revenue	$ 24,002	$ 15,747
Cost of revenue	6,844	4,579
Gross profit	17,158	11,168
Operating expenses:		
Sales and marketing	16,237	9,845
Research and development	3,093	2,322
General and administrative	5,954	3,553
Total operating expenses	25,284	15,720
Loss from operations	(8,126)	(4,552)
Other income (expense):		
Interest expense	(143)	(684)
Change in fair value of preferred stock warrant liabilities		(42,559)
Other, net	239	236
Other income (expense), net	96	(43,007)
Loss before provision for income taxes	(8,030)	(47,559)
Provision for income taxes	(82)	(34)
Net loss	$ (8,112)	$ (47,593)

The following table sets forth our revenue and key metrics that we use to evaluate our business, measure our performance, identify trends affecting our business, formulate financial projections and make strategic decisions:

Revenue and Metrics

	At or For Three Months Ended March 31,	
	2012	**2011**
Revenue (in thousands)	$ 24,002	$ 15,747
Bookings (in thousands)	$ 23,959	$ 14,331
Number of clients	891	562
Number of users (rounded to nearest thousand)	8,181	5,221

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Revenue increased $8.3 million, or 52%, for the three months ended March 31, 2012 as compared to the same period in 2011. Revenue growth in the three months ended March 31, 2012 was driven by $8.0 million in additional revenue from client agreements signed in prior periods that was not fully reflected in those periods, as a result of the seasonality of when we enter into new client agreements and our revenue recognition policy, which generally recognizes subscription revenue over the contract period. Revenue for the three months ended March 31, 2012 from client agreements signed prior to the first quarter of 2012 was $22.3 million, compared to revenue for the three months ended March 31, 2011 from client agreements signed prior to the first quarter of 2011 of $14.3 million. Revenue in the United States increased by $5.8 million, or 52%, for the three months ended March 31, 2012 as compared to the same period in 2011, while international revenue increased by $2.5 million, or 53%, during the same period. The increase in domestic and international sales was mainly attributable to the acquisition of 210 domestic and 119 international clients, respectively, during the period from March 31, 2011 through March 31, 2012. As a percentage of total revenue, international revenue accounted for 30% in the three months ended March 31, 2012 and March 31, 2011.

Bookings increased 67% for the three months ended March 31, 2012, as compared to the same period in 2011. The increase in bookings for the three months ended March 31, 2012 is attributable to a 52% increase in revenue for the three months ended March 31, 2012 as compared to the same period in 2011. The growth rates for revenue and bookings are not correlated with each other in a given period due to the seasonality of when we enter into client agreements, the varied timing of billings, the recognition in most cases of subscription revenue on a straight-line basis over the term of each client agreement, and the recognition of consulting revenue based on proportional performance over the period the services are performed. Our number of clients grew 11% at March 31, 2012 compared to December 31, 2011, 59% compared to March 31, 2011, and 85% compared to December 31, 2010. Our number of users increased 9% at March 31, 2012 compared to December 31, 2011, 57% compared to March 31, 2011 and 66% compared to December 31, 2010, due primarily to the acquisition of new clients, although we also increased the number of users within existing clients.

As discussed above under the heading *Metrics*, bookings is a non-GAAP financial measure defined as the sum of revenue and the change in the deferred revenue balance for the period. Our management uses bookings in analyzing its financial results and believes it is useful to investors, as a supplement to the corresponding GAAP measure, in evaluating our ongoing operational performance and trends and in comparing our financial measures with other companies in the same industry. However, it is important to note that other companies, including companies in our industry, may calculate bookings differently or not at all, which may reduce its usefulness as a comparative measure.

The following table presents a reconciliation of revenue to bookings for each of the periods presented (in thousands):

	Deferred Revenue Balance	Three Months Ended March 31, 2012
Revenue		$ 24,002
Deferred revenue at December 31, 2011	$ 55,880	
Deferred revenue at March 31, 2012	55,837	
Change in deferred revenue	(43)	(43)
Bookings		**$ 23,959**

	Deferred Revenue Balance	Three Months Ended March 31, 2011
Revenue		$ 15,747
Deferred revenue at December 31, 2010	$ 33,818	
Deferred revenue at March 31, 2011	32,403	
Change in deferred revenue	(1,415)	(1,415)
Bookings		**$ 14,332**

We believe our revenue growth is a result of our continued investment in and development of our direct sales and sales support teams. We believe this investment has enabled us to achieve greater sales coverage and better sales execution, as well as increased marketing activities, which we believe have increased brand awareness and created higher demand for our solution. We have also continued to enhance our comprehensive solution, which we believe has encouraged existing clients to add additional clouds and users.

Cost of Revenue and Gross Margin

	Three Months Ended March 31, (dollars in thousands)	
	2012	**2011**
Cost of revenue	$ 6,844	$ 4,579
Gross profit	$ 17,158	$ 11,168
Gross margin	72%	71%

Cost of revenue increased $2.3 million, or 49%, for the three months ended March 31, 2012 as compared to the same period in 2011. The increase was attributable to $1.2 million in increased employee-related costs due to higher headcount, $0.3 million in increased allocated overhead such as rent, IT costs, depreciation and amortization and employee benefits costs, $0.3 million in increased network infrastructure costs, $0.2 million in increased third-party e-learning costs, $0.2 million in increased amortization of capitalized software, and $0.1 million in increased referral fees.

Our gross margin was 72% for the three months ended March 31, 2012 compared to 71% in the same period in 2011. Our gross profit increased by $6.0 million, or 54%, for the three months ended March 31, 2012 as compared to the same period in 2011. The increase in gross margin and gross profit was attributable to increased revenue and our realization of economies of scale in our consulting services and network infrastructure, as we have emphasized continuous improvement in processes for delivering client implementation and support programs.

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Sales and Marketing

	Three Months Ended March 31, (dollars in thousands)	
	2012	2011
Sales and marketing	$ 16,237	$ 9,845
Percent of revenue	68%	63%

Sales and marketing expenses increased $6.4 million, or 65%, for the three months ended March 31, 2012 as compared to the same period in 2011. The increase was attributable to the expansion of our sales force to address increased opportunities in new and existing markets and increases in marketing programs. Total headcount in sales and marketing at March 31, 2012 increased 54% compared to March 31, 2011, contributing to an increase in employee-related costs of $4.5 million (consisting of increased employee compensation and benefits of $3.1 million, increased commissions of $1.1 million, and increased stock-based compensation of $0.3 million). In addition, we incurred increased allocated overhead costs, such as rent, IT costs, and depreciation and amortization of $0.9 million, increased travel costs associated with our direct sales teams of $0.5 million and increased costs associated with marketing programs of $0.1 million.

As a percentage of revenue, sales and marketing expenses increased to 68% for the three months ended March 31, 2012 compared to 63% for the same period in 2011. Sales and marketing expenses may fluctuate from period to period based on the timing of our investments and related expenditures in our sales and marketing programs, as they vary in scope and scale over periods.

Research and Development

	Three Months Ended March 31, (dollars in thousands)	
	2012	2011
Research and development	$ 3,093	$ 2,322
Percent of revenue	13%	15%

Research and development expenses increased by $0.8 million, or 33%, for the three months ended March 31, 2012 as compared to the same period in 2011. The increase was principally due to a 39% increase in research and development headcount at March 31, 2012 compared to March 31, 2011 to maintain and improve the functionality of our solution. We incurred increased employee-related costs of $0.2 million arising primarily from increased headcount, consisting of increased employee compensation. In addition, in the three months ended March 31, 2012, we incurred increased expenses of allocated overhead costs, such as rent, IT costs, and depreciation and amortization of $0.3 million relating to overall increased expenses to support our continued growth, and increased expenses related to third-party consultants of $0.2 million.

We capitalize a portion of our software development costs related to the development and enhancements of our solution, which is then amortized to cost of revenue. The timing of our capitalizable development and enhancement projects may affect the amount of development costs expensed in any given period. We capitalized $1.2 million and $0.7 million of software development costs and amortized $0.6 million and $0.4 million in the three months ended March 31, 2012 and March 31, 2011, respectively.

As we mature as a company, we expect our headcount in research and development to increase. However, we also expect the portion of employee-related costs as a percentage of total development resources that are capitalized as capitalized software costs to decrease.

General and Administrative

	Three Months Ended March 31, (dollars in thousands)	
	2012	2011

General and administrative	$ 5,954	$ 3,553
Percent of revenue	25%	23%

General and administrative expenses increased by $2.4 million, or 67% for the three months ended March 31, 2012 as compared to the same period in 2011. The increase was driven by increased employee-related costs and increased overhead costs associated with increased headcount and professional fees to support our growing business, operations as a public company and our expansion into new geographic regions. We incurred increased employee-related costs of $1.5 million, consisting of increased employee compensation and benefits of $0.5 million and increased stock-based compensation expense of $1.0 million, as a result of increased headcount and corresponding stock-based compensation awards between March 31, 2011 and March 31, 2012. In addition, in the three

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months ended March 31, 2012, we incurred increased professional fees of $1.0 million for accounting, audit, legal and tax services and increased allocated overhead costs, such as rent, IT costs, and depreciation and amortization, of $0.1 million. These increases were partially offset by decreased charitable donations of $0.2 million. General and administrative headcount increased by 31% at March 31, 2012 as compared to March 31, 2011, primarily in our accounting and finance department to support our growth and operations as a public company.

As a percentage of revenue, general and administrative expenses increased to 25% in the three months ended March 31, 2012 compared to 23% in the same period in 2011. This increase was due to revenue increasing at a lower rate than increases in our general and administrative expenses.

Other Income (Expense)

	Three Months Ended March 31, (dollars in thousands)	
	2012	**2011**
Interest expense	$ (143)	$ (684)
Change in fair value of preferred stock warrant liabilities		(42,559)
Other, net	239	236
Other income (expense), net	$ 96	$ (43,007)

Interest expense for the three months ended March 31, 2012 decreased by $0.5 million as compared to the same period in 2011 due to decreased borrowings and the write-off of the remaining unamortized debt discount of $0.3 million in the three months ended March 31, 2011 associated with debt that was repaid with proceeds from our initial public offering.

During the three months ended March 31, 2011, we recorded a non-cash charge of $42.6 million related to the change in fair value of our preferred stock warrant liabilities from December 31, 2010 to the respective exercise dates of the warrants in March 2011. We valued our preferred stock warrants at the end of each fiscal period using the Black-Scholes option pricing model. During March 2011, all of our warrants to purchase preferred stock were exercised, and all outstanding shares of preferred stock, including all shares of preferred stock issued upon the exercise of the preferred stock warrants, were converted into common stock on a one-for-one basis. As a result, subsequent to the three months ended March 31, 2011, we no longer record any changes in the fair value of such liabilities in our statement of operations.

Other, net is comprised of foreign exchange gains and losses. Foreign exchange gains for the three months ended March 31, 2012 and 2011 were related to fluctuations in the British Pound and Euro in relation to the U.S. Dollar.

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Provision for Income Taxes

	Three Months Ended March 31, (dollars in thousands)	
	2012	2011
Provision for income taxes	$ (82)	$ (34)

We have incurred operating losses in all periods to date and have recorded a full valuation allowance against our net deferred tax assets and, therefore, have not recorded a provision for income taxes for any of the periods presented, other than provisions for certain foreign income taxes. Realization of any of our deferred tax assets depends upon future earnings, the timing and amount of which are uncertain.

Liquidity and Capital Resources

To date, our operations and growth have been financed primarily through the sale of equity securities, including net cash proceeds from our initial public offering of common stock in March 2011, in which we raised approximately $90.5 million, net of underwriting discounts and commissions but before offering expenses of $3.7 million.

At March 31, 2012, our principal sources of liquidity were $87.2 million of cash and cash equivalents and $15.7 million available under our credit facility with Silicon Valley Bank (SVB Credit Facility), which matures in August 2012. Borrowings under the SVB Credit Facility are available based on a multiple of our contracted monthly recurring revenue, as defined in the agreement governing the facility, and are reduced by the issuance of irrevocable standby letters of credit. Interest is payable monthly, and the principal is due upon maturity. The interest rate is prime plus 1.5% if the outstanding indebtedness under the facility is less than or equal to $5.0 million, and prime plus 2.5% if the outstanding indebtedness is greater than $5.0 million. The SVB Credit Facility requires immediate repayment upon an event of default, as defined in the agreement, which includes events such as a payment default, a covenant default or the occurrence of a material adverse change, as defined in the agreement.

During May 2011, we amended the SVB Credit Facility to allow for up to $3.0 million in loan advances, in addition to the amount available under the existing line of credit specifically for the purchase of software and equipment. Advances for the purchase of software and equipment may be drawn through May 2012, have an interest rate of prime plus 1.25%, and are repayable monthly over a period of either 12 months or 36 months, depending on the items purchased. Any borrowings for the purchase of software and equipment under the SVB Credit Facility survive the original maturity of the SVB Credit Facility of August 2012 and any additional borrowings will be payable in accordance with the repayment schedule of the individual loan advances. In May 2011, we borrowed approximately $0.7 million for the purchase of software and equipment, payable monthly through May 2014. At March 31, 2012, we had $0.5 million outstanding under the SVB Credit Facility.

Our cash flows from operating activities have historically been significantly impacted by the contractual payment terms and patterns of client agreements, as well as our investments in sales and marketing and research and development to drive our business growth.

Based on our current level of operations and anticipated growth, we believe our future cash flows from operating activities, existing cash and cash equivalents, together with our ability to borrow under the existing SVB Credit Facility will provide adequate funds for our ongoing operations for at least the next twelve months. Our future capital requirements will depend on many factors, including our rate of revenue, billings growth and collections, the level of our sales and marketing efforts, the timing and extent of spending to support product development efforts and expansion into new territories, the timing of introductions of new services and enhancements to existing services, the timing of general and administrative expenses as we grow our administrative infrastructure, the continuing market acceptance of our solution, and to the extent to which we incur costs associated with integrating Sonar Limited, our recently acquired New Zealand subsidiary, which we acquired in April 2012. To the extent that existing cash and cash from operations are not sufficient to fund our future activities, we may need to raise additional funds or utilize our cash resources supplemented by borrowing under our SVB Credit Facility. The acquisition of Sonar Limited for $12.5 million was funded with our own cash resources. Although we are not currently a party to any agreement or letter of intent with respect to potential investments in, or acquisitions of, complementary businesses, services or technologies, we may enter into these types of arrangements in the future, which could also require us to seek additional equity financing or utilize our cash resources supplemented by borrowing under our SVB Credit Facility.

Depending on certain growth opportunities, we may choose to accelerate investments in sales and marketing, research and development, technology and services, which may require the use of proceeds from our initial public offering for such additional expansion and expenditures, although we have no present understandings, commitments or agreements to enter into any such acquisitions.

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The following table sets forth a summary of our cash flows for the periods indicated (in thousands):

	Three Months Ended March 31, 2012	2011
Net cash provided by operating activities	$ 3,029	$ 1,391
Net cash used in investing activities	(1,310)	(727)
Net cash (used in) provided by financing activities	(65)	83,314

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Net Cash Provided by Operating Activities

Our net loss and cash flows from operating activities are significantly influenced by our investments in headcount and infrastructure to support anticipated growth. In addition, our net loss in prior periods has been significantly greater than our use of cash for operating activities due to the inclusion of substantial non-cash charges. Our cash flows from operating activities are affected by the seasonality of our business, which results in variations in the timing of our invoicing of, and our receipt of payments from, our clients. We have generally experienced increased invoicing in the third and fourth quarters of each year due to higher acquisitions of new clients, the timing of annual billings for existing clients and increased client renewals during these quarters. As a result, we have also experienced increased levels of client payments during the fourth and first quarters of each year, related to client receipts from third and fourth quarter invoices. Conversely, we experience relatively lower levels of billings in the first and second quarter of each year, and thus client receipts in the second and third quarters are lower relative to the other quarters. We expect this seasonality and resulting trends in cash flows from operating activities to continue.

Cash provided by operating activities of $3.0 million in the three months ended March 31, 2012 was a result of significant increased revenues due to the growth in our business and reflected our continued significant investments in headcount, increased expenses incurred as a result of becoming a public company, including costs associated with public company reporting and corporate governance requirements, and other expenses incurred to grow our business. In the three months ended March 31, 2012, $3.4 million, or 42%, of our net loss of $8.1 million consisted of non-cash items, including $2.5 million of stock-based compensation, $1.2 million of depreciation and amortization, $0.1 million of non-cash interest expense, and approximately $0.2 million in foreign exchange gains.

Cash provided by operating activities in the three months ended March 31, 2012 also included a $9.2 million decrease in accounts receivable due to the receipt of payments from our clients in addition to lower levels of billings in the three months ended March 31, 2012 as compared to the three months ended December 31, 2011 due to the seasonality of our business as discussed above. Cash provided by operating activities also included an increase in accounts payable of $1.4 million attributable to increased expenses associated with our growth, a $0.3 million decrease in prepaid expenses and other assets, and a $0.2 million decrease in other liabilities. Cash provided by operating activities in the three months ended March 31, 2012 was partially offset by a $2.3 million decrease in accrued liabilities primarily due to the payment of our 2011 bonuses, a $0.4 million decrease in deferred revenue for the three months ended March 31, 2012 due to the recognition of revenue, and a $0.3 million increase in deferred commissions due to the increased sales during the period.

Cash provided by operating activities in the three months ended March 31, 2011 of $1.4 million was a result of significant increased sales due to the growth in our business, partially offset by our continued significant investments in headcount, increased expenses incurred as a public company, including costs associated with public company reporting and corporate governance requirements, and other expenses incurred to grow our business. In the three months ended March 31, 2011, $44.8 million, or 94%, of our net loss of $47.6 million consisted of non-cash items, including a $42.6 million increase in preferred stock warrant liabilities, $0.8 million of depreciation and amortization, $0.8 million of stock-based compensation, $0.4 million of non-cash interest expense, and $0.2 million in a non-cash charitable contribution expense incurred in connection with the issuance of 20,000 shares of our common stock to a non-profit organization in February 2011.

Cash provided by operating activities included a decrease of $5.7 million in accounts receivable due to the receipt of payments from our clients in addition to lower levels of billings in the three months ended March 31, 2011 as compared to the three months ended December 31, 2010 due to the seasonality of our business as discussed above. Cash provided by operating activities also included an increase in accounts payable of $1.5 million, excluding a decrease of $0.4 million in accounts payable related to purchases of property and equipment as of December 31, 2010 which were transferred to capital leases during the three months ended March 31, 2011. Cash provided by operating activities in the three months ended March 31, 2011 was partially offset by a $1.4 million decrease in deferred revenue for the three months ended March 31, 2011 due to the recognition of revenue, a $0.3 million increase in deferred commissions due to the increased sales during the period, and a $0.2 million decrease in other liabilities.

Net Cash Used in Investing Activities

Our primary investing activities have consisted of capital expenditures to develop our capitalized software as well as to purchase computer equipment and furniture and fixtures in support of expanding our infrastructure and workforce. As our business grows, we expect our capital expenditures and our investment activity to continue to increase. Since our initial public offering, we have also invested in marketable securities.

We used $1.3 million and $0.7 million of cash in investing activities in the three months ended March 31, 2012 and 2011, respectively, primarily due to investments in our capitalized software.

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Net Cash (Used in) Provided by Financing Activities

Cash used in financing activities of $0.1 million in the three months ended March 31, 2012 was primarily due to payments of $0.5 million on our capital lease and financing obligations and $0.2 million to repay debt, partially offset by $0.6 million in proceeds from stock option exercises.

Cash provided by financing activities in the three months ended March 31, 2011 of $83.3 million was primarily due to $90.5 million of proceeds from our initial public offering, net of underwriting discounts and commissions but before offering expenses. In addition, cash provided by financing activities was also due to $3.5 million in proceeds from the exercise of options and warrants to purchase common and preferred stock. These proceeds were partially offset by $9.1 million of payments related to debt outstanding at December 31, 2010, consisting of a $4.0 million payment to Ironwood Equity Fund LP and $5.1 million of payments on our SVB Credit Facility, $1.3 million of payments on costs related to our initial public offering, and $0.4 million of payments on our capital lease obligations.

Contractual Obligations

There have been no significant changes in contractual obligations from those disclosed in our Form 10-K filed with the Securities and Exchange Commission on March 6, 2012 except during the three months ended March 31, 2012, we entered into new capital lease arrangements requiring payments of principal and interest of $1.0 million through 2015.

Off-Balance Sheet Arrangements

As part of our ongoing business, we do not have any relationships with other entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, that 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 any financing, liquidity, market or credit risk that could arise if we had engaged in those types of relationships.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We have operations both within the United States and internationally, and we are exposed to market risks in the ordinary course of our business. These risks primarily include interest rate, foreign exchange and inflation risks, as well as risks relating to changes in the general economic conditions in the countries where we conduct business. To reduce certain of these risks, we monitor the financial condition of our large clients and limit credit exposure by collecting in advance and setting credit limits as we deem appropriate. In addition, our investment strategy has historically been to invest in financial instruments that are highly liquid and readily convertible into cash and that mature within three months from the date of purchase. To date, we have not used derivative instruments to mitigate the impact of our market risk exposures. We have also not used, nor do we intend to use, derivatives for trading or speculative purposes.

Interest Rate Risk

At March 31, 2012, we had $87.2 million in cash and cash equivalents, which primarily consisted of money market funds backed by United States Treasury Bills. The carrying amount of our cash equivalents reasonably approximates fair value due to the short maturities of these instruments.

The primary objectives of our investment activities are the preservation of capital, the fulfillment of liquidity needs and the fiduciary control of cash and investments. We do not enter into investments for trading or speculative purposes. Our investments are exposed to market risk due to a fluctuation in interest rates, which may affect our interest income and the fair market value of our investments. Due to the short-term nature of our investment portfolio, however, we do not believe an immediate 10% increase or decrease in interest rates would have a material effect on the fair market value of our portfolio. We therefore do not expect our operating results or cash flows to be materially affected by a sudden change in market interest rates.

We do not believe our cash equivalents have significant risk of default or illiquidity. While we believe our cash equivalents do not contain excessive risk, we cannot provide absolute assurance that in the future our investments will not be subject to adverse changes in market value. In addition, we maintain significant amounts of cash and cash equivalents at one or more financial institutions that are in excess of federally insured limits. We cannot be assured that we will not experience losses on these deposits.

Foreign Currency Risk

We have foreign currency risks related to our revenue and operating expenses denominated in currencies other than the U.S. Dollar. Our historical revenue has primarily been denominated in U.S. Dollars, and a significant portion of our current revenue continues to be denominated in U.S. Dollars. However, we expect an increasing portion of our future revenue to be denominated in currencies other than the U.S. Dollar, primarily the Euro and British Pound. To a lesser extent, we also have revenue denominated in Australian Dollars, New Zealand Dollars, Singapore Dollars, and Japanese Yen. The effect of an immediate 10% adverse change in foreign exchange rates on foreign-denominated accounts at March 31, 2012 would result in a foreign currency loss of approximately $1.2 million. Our operating expenses are generally denominated in the currencies of the countries in which our operations are located, primarily the United States and, to a much lesser extent, the United Kingdom, other European Union countries, Canada, India and Israel. Increases and decreases in our foreign-denominated revenue from movements in foreign exchange rates are partially offset by the corresponding decreases or increases in our foreign-denominated operating expenses.

As our international operations grow, our risks associated with fluctuation in currency rates will become greater, and we will continue to reassess our approach to managing this risk. In addition, currency fluctuations or a weakening U.S. Dollar can increase the costs of our international expansion. To date, we have not entered into any foreign currency hedging contracts although we may do so in the future.

Inflation Risk

We do not believe that inflation has had a material effect on our business, financial condition or results of operations. Nonetheless, if our costs were to become subject to significant inflationary pressures, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our business, financial condition and results of operations.

Counterparty Risk

Our financial statements are subject to counterparty credit risk, which we consider as part of the overall fair value measurement. We attempt to mitigate this risk through credit monitoring procedures.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The term 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), refers to controls and procedures that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that such information is accumulated and communicated to a company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2012, the end of the period covered by this Quarterly Report on Form 10-Q. Based upon such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of such date.

Changes in Internal Controls

There was no change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. 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 Quarterly Report on Form 10-Q, we are not a party to any litigation 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.

Item 1A. Risk Factors

The following risk factors and other information included in this Quarterly Report on Form 10-Q should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we presently deem less significant may also impair our business operations. Please see page 18 of this Quarterly Report on Form 10-Q for a discussion of the forward-looking statements that are qualified by these risk factors. If any of the events or circumstances described in the following risk factors actually occurs, our business, operating results and financial condition could be materially adversely affected.

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Risks Related to Our Business and Industry

We have a history of losses, and we cannot be certain that we will achieve or sustain profitability.

We have incurred losses since our inception. We experienced net losses of $8.1 million, $63.9 million, $48.4 million, and $8.4 million for the three months ended March 31, 2012, and years ended December 31, 2011, 2010 and 2009, respectively. At March 31, 2012, our accumulated deficit was $172.8 million and total stockholders equity was $57.4 million. We expect to continue to incur operating losses as a result of expenses associated with the continued development and expansion of our business. Our expenses include sales and marketing, research and development and other costs relating to the development, marketing and sale of our solution and consulting services that may not generate revenue until later periods, if at all. Any failure to increase revenue or manage our cost structure as we implement initiatives to grow our business could prevent us from achieving or sustaining profitability. In addition, our ability to achieve profitability is subject to a number of the risks and uncertainties discussed below, many of which are beyond our control. We cannot be certain that we will be able to achieve or sustain profitability on a quarterly or annual basis.

Unfavorable conditions in our industry or the global economy or reductions in information technology spending could limit our ability to grow our business and negatively affect our operating results.

Our operating results may vary based on the impact of changes in our industry or the global economy on us or our clients. The revenue growth and potential profitability of our business depends on demand for enterprise application software and services generally and for learning and talent management solutions in particular. We sell our solution primarily to large and mid-sized organizations whose businesses fluctuate based on general economic and business conditions. In addition, a portion of our revenue is attributable to the number of users of our solution at each of our clients, which in turn is influenced by the employment and hiring patterns of our clients and potential clients. To the extent that weak economic conditions cause our clients and potential clients to freeze or reduce their headcount, demand for our solution may be negatively affected. Historically, economic downturns have resulted in overall reductions in spending on information technology and learning and talent management solutions as well as pressure for extended billing terms, as occurred during the recent recession. If economic conditions deteriorate or do not materially improve, our clients and potential clients may elect to decrease their information technology and learning and talent management budgets by deferring or reconsidering product purchases, which would limit our ability to grow our business and negatively affect our operating results.

Our financial results may fluctuate due to our long, variable and, therefore, unpredictable sales cycle and our focus on large and mid-market organizations.

We plan our expenses based on certain assumptions about the length and variability of our sales cycle. If our sales cycle becomes longer or more variable, our results may be adversely affected. Our sales cycle generally varies in duration between two to nine months and, in some cases, even longer depending on the size of the potential client. Factors that may influence the length and variability of our sales cycle include:

- the need to educate potential clients about the uses and benefits of our solution;
- the relatively long duration of the commitment clients make in their agreements with us;
- the discretionary nature of potential clients purchasing and budget cycles and decisions;
- the competitive nature of potential clients evaluation and purchasing processes;
- evolving functionality demands of potential clients;
- fluctuations in the learning and talent management needs of potential clients;

- announcements or planned introductions of new products by us or our competitors; and
- lengthy purchasing approval processes of potential clients.

The fluctuations that result from the length and variability of our sales cycle may be magnified by our focus on sales to large and mid-sized organizations. If we are unable to close an expected significant transaction with one or more of these companies in a particular period, or if an expected transaction is delayed until a subsequent period, our operating results for that period, and for any future periods in which revenue from such transaction would otherwise have been recognized, may be adversely affected.

Our financial results may fluctuate due to other factors, including invoicing terms, some of which may be beyond our control.

There are a number of other factors that may cause our financial results to fluctuate from period to period, including:

- the extent to which new clients are attracted to our solution to satisfy their learning and talent management needs;
- the timing and rate at which we sign agreements with new clients;
- the extent to which we retain existing clients and satisfy their requirements;

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the extent to which existing clients renew their subscriptions to our solution and the timing of those renewals;

the extent to which existing clients purchase or discontinue the use of additional clouds and add or decrease the number of users;

the addition or loss of large clients, including through acquisitions or consolidations;

the number and size of new clients, as compared to the number and size of renewal clients in a particular period;

the mix of clients between small, mid-sized and large organizations;

changes in our pricing policies or those of our competitors;

changes in billing cycles and the size of advance payments relative to overall contract value in client agreements;

seasonal factors affecting demand for our solution or potential clients   purchasing decisions;

the financial condition and creditworthiness of our clients;

the amount and timing of operating expenses, including those related to the maintenance and expansion of our business, operations and infrastructure;

the timing and success of new product and service introductions by us;

the timing and success of current and new competitive products and services by our competitors;

other changes in the competitive dynamics of our industry, including consolidation among competitors, clients or strategic partners;

the timing of expenses related to the development of new products and technologies, including enhancements to our solution;

our ability to manage our existing business and future growth, including in terms of additional clients, incremental users and new geographic regions;

expenses related to our data centers and the expansion of such data centers;

the effects of, and expenses associated with, acquisitions of third-party technologies or businesses and any potential future charges for impairment of goodwill resulting from those acquisitions;

general economic, industry and market conditions; and

various factors related to disruptions in our SaaS hosting network infrastructure, defects in our solution, privacy and data security, and exchange rate fluctuations, each of which is described elsewhere in these risk factors.

In light of the foregoing factors, we believe that our financial results, including our revenue and deferred revenue levels, may vary significantly from period-to-period. As a result, period-to-period comparisons of our operating results may not be meaningful and should not be relied on as an indication of future performance.

The forecasts of market growth may prove to be inaccurate, and even if the markets in which we compete achieve the forecasted growth, we cannot assure you our business will grow at similar rates, or at all.

Growth forecasts are subject to significant uncertainty and are based on assumptions and estimates which may not prove to be accurate. Forecasts relating to the expected growth in the SaaS market or learning and talent management market may prove to be inaccurate. Even if these markets experience the forecasted growth, we may not grow our businesses at similar rates, or at all. Our growth is subject to many factors, including our success in implementing our business strategy, which is subject to many risks and uncertainties.

Our business depends substantially on clients renewing their agreements and purchasing additional clouds from us or adding additional users. Any decline in our client renewals or purchases of additional clouds or additional users would harm our future operating results.

In order for us to improve our operating results, it is important that our clients renew their agreements with us when the initial contract term expires and also purchase additional clouds or add additional users. Our clients have no obligation to renew their subscriptions after the initial subscription period, and we cannot assure you that clients will renew subscriptions at the same or higher level of service, if at all. In the past, some of our clients have elected not to renew their agreements with us. Moreover, certain of our clients have the right to cancel their agreements for convenience, subject to certain notice requirements and, in some cases, early termination fees. Our clients renewal rates may decline or fluctuate as a result of a number of factors, including their satisfaction or dissatisfaction with our solution, pricing, the prices of competing products or services, mergers and acquisitions affecting our client base, reduced hiring by our clients or red