

Support.com, Inc.  
Form 10-Q  
November 04, 2013

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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(Mark One)

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

For the Quarterly Period Ended September 30, 2013  
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 No. 000-30901

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SUPPORT.COM, INC.  
(Exact Name of Registrant as Specified in Its Charter)

Delaware 94-3282005  
(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification No.)

900 Chesapeake Drive  
Redwood City, CA 94063  
(Address of Principal Executive Offices)  
(Zip Code)

Registrant's Telephone Number, Including Area Code: (650) 556-9440

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

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

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

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

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

On October 31, 2013, 52,775,201 shares of the Registrant’s Common Stock, \$0.0001 par value, were outstanding.

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SUPPORT.COM, INC.  
 FORM 10-Q  
 QUARTERLY PERIOD ENDED SEPTEMBER 30, 2013  
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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## SUPPORT.COM, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

	September 30, 2013 (Unaudited)	December 31, 2012 (1 )
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 30,622	\$ 30,852
Short-term investments	37,828	25,498
Accounts receivable, net	13,644	9,689
Prepaid expenses and other current assets	2,236	1,359
Total current assets	84,330	67,398
Property and equipment, net	507	591
Goodwill	14,240	14,240
Purchased technology, net	—	62
Intangible assets, net	3,770	4,775
Other assets	1,038	1,193
Total assets	\$ 103,885	\$ 88,259
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 1,239	\$ 444
Accrued compensation	3,138	1,609
Other accrued liabilities	3,856	3,969
Short-term deferred revenue	4,358	6,618
Total current liabilities	12,591	12,640
Long-term deferred revenue	32	35
Other long-term liabilities	1,604	1,421
Total Liabilities	14,227	14,096
Commitments and contingencies (Note 4)		
Stockholders' equity:		
Common stock; par value \$0.0001, 150,000,000 shares authorized; 53,939,053 issued and 52,746,455 outstanding at September 30, 2013; 50,002,587 issued and 49,809,989 outstanding at December 31, 2012	5	5
Additional paid-in capital	255,444	242,954
Treasury stock	(5,036 )	(922 )
Accumulated other comprehensive loss	(1,893 )	(1,501 )
Accumulated deficit	(158,862 )	(166,373)
Total stockholders' equity	89,658	74,163

Total liabilities and stockholders' equity	\$ 103,885	\$ 88,259
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(1) Derived from the December 31, 2012 audited Consolidated Financial Statements included in our Annual Report on Form 10-K, as filed with the Securities and Exchange Commission ("SEC") on March 8, 2013.

See accompanying notes.

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SUPPORT.COM, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Revenue:				
Services	\$19,305	\$14,769	\$51,879	\$42,278
Software and other	4,054	3,407	11,807	10,799
Total revenue	23,359	18,176	63,686	53,077
Cost of revenue:				
Cost of services	11,046	8,815	29,194	28,696
Cost of software and other	294	312	872	1,142
Total cost of revenue	11,340	9,127	30,066	29,838
Gross profit	12,019	9,049	33,620	23,239
Operating expenses:				
Research and development	1,456	1,643	4,325	5,121
Sales and marketing	4,120	3,789	12,431	14,908
General and administrative	3,077	2,897	8,193	8,661
Amortization of intangible assets and other	335	397	1,005	1,155
Total operating expenses	8,988	8,726	25,954	29,845
Income (loss) from operations	3,031	323	7,666	(6,606)
Interest income and other, net	127	93	307	227
Income (loss) from continuing operations, before income taxes	3,158	416	7,973	(6,379)
Income tax provision	121	118	446	353
Income (loss) from continuing operations, after income taxes	3,037	298	7,527	(6,732)
Income (loss) from discontinued operations, after income taxes	(5)	(7)	(16)	10
Net income (loss)	\$3,032	\$291	\$7,511	\$(6,722)
Basic earnings (loss) per share:				
Continuing operations, after income taxes	\$0.06	\$0.01	\$0.15	\$(0.14)
Discontinued operations, after income taxes	(0.00)	(0.00)	(0.00)	0.00
Basic net earnings (loss) per share	\$0.06	\$0.01	\$0.15	\$(0.14)
Diluted earnings (loss) per share:				
Continuing operations, after income taxes	\$0.06	\$0.01	\$0.14	\$(0.14)
Discontinued operations, after income taxes	(0.00)	(0.00)	(0.00)	0.00
Diluted net earnings (loss) per share	\$0.06	\$0.01	\$0.14	\$(0.14)
Shares used in computing per share amounts:				
Basic	52,266	48,707	51,080	48,571

Diluted	54,661	50,326	53,508	48,571
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See accompanying notes.

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SUPPORT.COM, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

(Unaudited)

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Net income (loss)	\$3,032	\$291	\$7,511	\$(6,722)
Other comprehensive income (loss):				
Change in foreign currency translation adjustment	(149 )	132	(375 )	40
Change in net unrealized gain (loss) on investments	5	24	(18 )	315
Other comprehensive income (loss)	(144 )	156	(393 )	355
Comprehensive income (loss)	\$2,888	\$447	\$7,119	\$(6,367)

See accompanying notes.

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SUPPORT.COM, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2013	2012
Operating Activities:		
Net income (loss)	\$7,511	\$(6,722 )
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	262	404
Amortization of premiums and discounts on investments	442	446
Amortization of purchased technology	62	62
Amortization of intangible assets and other	1,005	1,155
Stock-based compensation	2,434	2,938
Warrant-related charges	383	—
Changes in assets and liabilities:		
Accounts receivable, net	(3,955 )	649
Prepaid expenses and other current assets	(891 )	(533 )
Other long-term assets	97	(187 )
Accounts payable	795	(507 )
Accrued compensation	1,511	646
Other accrued liabilities	(132 )	(123 )
Other long-term liabilities	181	320
Deferred revenue	(2,263 )	849
Net cash provided by (used in) operating activities	7,442	(603 )
Investing Activities:		
Purchases of investments	(43,836)	(33,317)
Maturities of investments	31,046	33,560
Sales of investments	—	2,400
Purchases of property and equipment	(178 )	(503 )
Acquisition of business, net of cash acquired	—	(1,327 )
Net cash provided by (used in) investing activities	(12,968)	813
Financing Activities:		
Proceeds from issuances of common stock	9,673	1,069
Repurchase of common stock	(4,114 )	—
Net cash provided by financing activities	5,559	1,069
Effect of exchange rate changes on cash and cash equivalents	(263 )	69
Net increase (decrease) in cash and cash equivalents	(230 )	1,348
Cash and cash equivalents at beginning of period	30,852	22,159
Cash and cash equivalents at end of period	\$30,622	\$23,507
Supplemental schedule of cash flow information:		
Income taxes paid	\$97	\$99

See accompanying notes.

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SUPPORT.COM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Support.com, Inc. (the “Company” or “Support.com”, “We” or “Our”) and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated. The condensed consolidated balance sheet as of September 30, 2013 and the condensed consolidated statements of operations and comprehensive income (loss) for the three and nine months ended September 30, 2013 and 2012 and the condensed consolidated statements of cash flows for the nine months ended September 30, 2013 and 2012 are unaudited. In the opinion of management, these unaudited interim condensed consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) that are necessary for a fair presentation of the results for, and as of, the periods shown. The results of operations for such periods are not necessarily indicative of the results expected for the full fiscal year or for any future period. The condensed consolidated balance sheet information as of December 31, 2012 is derived from audited consolidated financial statements as of that date. These financial statements have been prepared based upon Securities and Exchange Commission (“SEC”) rules that permit reduced disclosure for interim periods. For a more complete discussion of significant accounting policies and certain other information, these unaudited interim condensed consolidated financial statements should be read with the consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012, filed with the Securities and Exchange Commission on March 8, 2013.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The accounting estimates that require management’s most significant, difficult and subjective judgments include accounting for revenue recognition, the valuation and recognition of investments, the assessment of recoverability of intangible assets and their estimated useful lives, the valuations and recognition of stock based compensation and the recognition and measurement of current and deferred income tax assets and liabilities. Actual results could differ materially from these estimates.

Revenue Recognition

For all transactions, we recognize revenue only when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred;
- Collection is considered probable; and
- The fees are fixed or determinable.

We consider all arrangements with payment terms longer than 90 days not to be fixed or determinable. If the fee is considered not to be fixed or determinable, revenue is recognized as payment becomes due from the customer.

Services Revenue

Services revenue is comprised primarily of fees for technology support services. Service programs available for consumer markets include computer and mobile device set-up, security and support, virus and malware removal and wireless network set-up, security and support. Service programs available for small business markets include the consumer services plus managed services such as server and network monitoring and maintenance.

We offer services to consumers and small businesses, primarily through our channel partners (which include communications providers, retailers, technology companies and others) and to a lesser degree directly through our website at [www.support.com](http://www.support.com). We transact with customers via reseller programs, referral programs and direct transactions. In reseller programs, the channel partner generally executes the financial transactions with the consumer and pays a fee to us which we recognize as revenue when the service is delivered. In referral programs, we transact with the consumer directly and pay a referral fee to the referring party. Referral fees are generally expensed in the period in which revenues are recognized. In such instances, since we are the transacting party and bear substantially all risks associated with the transaction, we record the gross amount of revenue. In direct transactions, we sell directly to the customer at the retail price.

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The services described above are of four types for revenue recognition purposes:

**Subscriptions** - Customers purchase subscriptions or “service plans” under which certain services are provided over a fixed subscription period. Revenues for subscriptions are recognized ratably over the respective subscription periods.

**Incident-Based Services** - Customers purchase a discrete, one-time service. Revenue recognition occurs at the time of service delivery. Fees paid for services sold but not yet delivered are recorded as deferred revenue and recognized at the time of service delivery.

**Service Cards / Gift Cards** - Customers purchase a service card or a gift card, which entitles the cardholder to redeem a certain service at a time of their choosing. For these sales, revenue is deferred until the card has been redeemed and the service has been provided.

**Hourly-Based Services** - In connection with the provisions of certain services programs, fees are calculated based on contracted hourly rates with channel partners. For these programs, we recognize revenue as services are performed, based on billable hours of work delivered by our technology specialists. These services programs also include performance standards, which may result in incentives or penalties, which are recognized as earned or incurred.

In certain cases, we are paid for services that are sold but not yet delivered. We initially record such balances as deferred revenue, and recognize revenue when the service has been provided or, on the non-subscription portion of these balances, when the likelihood of the service being redeemed by the customer is remote (“services breakage”). Based on our historical redemption patterns for these relationships, we believe that the likelihood of a service being delivered more than 90 days after sale is remote. We therefore recognize non-subscription deferred revenue balances older than 90 days as services revenue. For the three and nine months ended September 30, 2013 and 2012, services breakage revenue accounted for approximately 1% of our total revenue.

Channel partners are generally invoiced monthly. Fees from consumers via referral programs and direct transactions are generally paid with a credit card at the time of sale. Revenue is recognized net of any applicable sales tax.

Services revenue also includes fees from implementation services of our Nexus Service Delivery Platform (“Nexus platform”), typically covering integration to other customer systems. We generally charge for these services on a time and material basis.

We generally provide a refund period on services, during which refunds may be granted to customers under certain circumstances, including inability to resolve certain support issues. For our channel sales, the refund period varies by partner, but is generally between 5 and 14 days. For referral programs and direct transactions, the refund period is generally 5 days. For all channels, we recognize revenue net of refunds and cancellations during the period. Refunds and cancellations have not been material.

## Software and Other Revenue

Software and other revenue is comprised primarily of fees for end-user software products provided through direct customer downloads and through the sale of this software via channel partners. Our software is sold to consumers as a perpetual license or as a fixed period subscription. We act as the primary obligor and generally control fulfillment, pricing, product requirements, and collection risk and therefore we record the gross amount of revenue. We provide a 30-day money back guarantee for the majority of our end-user software products.

For certain products, we sell perpetual licenses. We provide a limited amount of free technical support to customers. Since the cost of providing this free technical support is insignificant and free product enhancements are minimal and infrequent, we do not defer the recognition of revenue associated with sales of these products.

For certain of our products (principally SUPERAntiSpyware), we sell licenses for a fixed subscription period. We provide regular, significant updates over the subscription period and therefore recognize revenue for these products ratably over the subscription period.

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Other revenue consists primarily of revenue generated through partners advertising to our customer base in various forms, including toolbar advertising, email marketing, and free trial offers. We recognize other revenue in the period in which our partners notify us that the revenue has been earned.

Software and other revenue also includes fees from licensing of our Nexus platform. In such arrangements, customers receive a right to use our platform in their own technology support organizations. We license the Nexus platform using a software-as-a-service model under which customers cannot take possession of the technology and pay us on a per-user per-month basis during the term of the arrangement. Revenue from licensing of our Nexus platform was approximately 7% and 6% of software and other revenue in the three and nine months ended September 30, 2013, respectively.

## Cash, Cash Equivalents and Investments

All liquid instruments with an original maturity at the date of purchase of 90 days or less are classified as cash equivalents. Cash equivalents and short-term investments consist primarily of money market funds, certificates of deposit, commercial paper, corporate and municipal bonds. Our interest income on cash, cash equivalents and investments is recorded monthly and reported as interest income and other in our condensed consolidated statements of operations.

Our cash equivalents and short-term investments are classified as available-for-sale, and are reported at fair value with unrealized gains/losses included in accumulated other comprehensive income within stockholders' equity on the condensed consolidated balance sheets and in the condensed consolidated statements of comprehensive income (loss). We view our available-for-sale portfolio as available for use in our current operations, and therefore we present our marketable securities as short-term assets.

We monitor our investments for impairment on a quarterly basis and determine whether a decline in fair value is other-than-temporary by considering factors such as current economic and market conditions, the credit rating of the security's issuer, the length of time an investment's fair value has been below our carrying value, our intent to sell the security and our belief that we will not be required to sell the security before the recovery of our amortized cost. If an investment's decline in fair value is deemed to be other-than-temporary, we reduce its carrying value to its estimated fair value, as determined based on quoted market prices or liquidation values. Declines in value judged to be other-than temporary, if any, are recorded in operations as incurred. At September 30, 2013, we evaluated our unrealized gains/losses on available-for-sale securities and determined them to be temporary. We currently do not intend to sell securities with unrealized losses and we concluded that we will not be required to sell these securities before the recovery of our amortized cost basis.

The following is a summary of cash, cash equivalents and investments at September 30, 2013 and December 31, 2012 (in thousands):

As of September 30, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash	\$ 13,244	\$ —	\$ —	\$ 13,244
Money market funds	15,756	—	—	15,756
Certificates of deposits	3,329	—	(1 )	3,328
Commercial paper	12,996	—	(1 )	12,995
Corporate notes and bonds	23,143	4	(20 )	23,127
	\$ 68,468	\$ 4	\$ (22 )	\$ 68,450

Classified as:

Cash and cash equivalents	\$ 30,623	\$ —	\$ (1	) \$30,622
Short-term investments	37,845	4	(21	) 37,828
	\$ 68,468	\$ 4	\$ (22	) \$68,450

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As of December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash	\$ 11,116	\$ —	\$ —	\$11,116
Money market funds	17,235	—	—	17,235
Certificates of deposits	1,880	—	(1 )	1,879
Commercial paper	5,745	1	(1 )	5,745
Corporate notes and bonds	20,172	7	(6 )	20,173
U.S. government agency securities	202	—	—	202
	\$ 56,350	\$ 8	\$ (8 )	\$56,350

## Classified as:

Cash and cash equivalents	\$ 30,853	\$ —	\$ (1 )	\$30,852
Short-term investments	25,497	8	(7 )	25,498
	\$ 56,350	\$ 8	\$ (8 )	\$56,350

The following table summarizes the estimated fair value of our available-for-sale securities classified by the stated maturity date of the security (in thousands):

	September 30, 2013	December 31, 2012
Due within one year	\$ 30,007	\$ 23,885
Due within two years	7,821	1,613
	\$ 37,828	\$ 25,498

## Fair Value Measurements

ASC 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements. Fair value is defined under ASC 820 as 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 ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value, which are the following:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In accordance with ASC 820, the following table represents our fair value hierarchy for our financial assets (cash equivalents and investments) measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012 (in thousands):

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As of September 30, 2013	Level			Total
	Level 1	Level 2	3	
Money market funds	\$15,756	\$—	\$—	\$15,756
Certificates of deposits	3,328	—	—	3,328
Commercial paper	—	12,995	—	12,995
Corporate notes and bonds	—	23,127	—	23,127
Total	\$19,084	\$36,122	\$—	\$55,206

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As of December 31, 2012	Level			Total
	Level 1	Level 2	3	
Money market funds	\$17,235	\$—	\$	—\$17,235
Certificates of deposits	1,879	—		— 1,879
Commercial paper	—	5,745		— 5,745
Corporate notes and bonds	—	20,173		— 20,173
U.S. government agency securities	—	202		— 202
Total	\$19,114	\$26,120	\$	—\$45,234

For short-term investments, measured at fair value using Level 2 inputs, we review trading activity and pricing for these investments as of the measurement date. When sufficient quoted pricing for identical securities is not available, we use market pricing and other observable market inputs for similar securities obtained from various third party data providers. These inputs either represent quoted prices for similar assets in active markets or have been derived from observable market data. There have been no transfers between Level 1 and Level 2 measurements during the three and nine months ended September 30, 2013 and 2012, respectively.

## Concentrations of Credit Risk

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash equivalents, investments and trade accounts receivable. Our investment portfolio consists of investment grade securities. Except for obligations of the United States government and securities issued by agencies of the United States government, we diversify our investments by limiting our holdings with any individual issuer. We are exposed to credit risks in the event of default by the issuers to the extent of the amount recorded on the condensed consolidated balance sheets. The credit risk in our trade accounts receivable is substantially mitigated by our evaluation of the customers' financial conditions at the time we enter into business and reasonably short payment terms.

For the three months ended September 30, 2013, Comcast (55%) accounted for 10% or more of our total revenue. For the three months ended September 30, 2012, Comcast (37%), OfficeMax (12%), Office Depot (12%) and Staples (10%) accounted for 10% or more of our total revenue. For the nine months ended September 30, 2013, Comcast (48%) and OfficeMax (10%) accounted for 10% or more of our total revenue. For the nine months ended September 30, 2012, Comcast (33%), Office Depot (13%), OfficeMax (13%) and Staples (11%) accounted for 10% or more of our total revenue. There were no other customers that accounted for 10% or more of total revenue for the three and nine months ended September 30, 2013 and 2012.

As of September 30, 2013, Comcast (73%) accounted for 10% or more of our total accounts receivable. As of December 31, 2012, Comcast (52%) and OfficeMax (10%) accounted for 10% or more of our total accounts receivable. There were no other customers that accounted for 10% or more of our total accounts receivable as of September 30, 2013 and December 31, 2012.

## Trade Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount. We perform evaluations of our customers' financial condition and generally do not require collateral. We make judgments as to our ability to collect outstanding receivables and provide allowances when collection becomes doubtful. Provisions are made based upon a specific review of all significant outstanding invoices. For those invoices not specifically provided for, provisions are recorded at differing rates, based upon the age of the receivable. In determining these percentages, we analyze our historical collection experience and current payment trends. The determination of past-due accounts is based on contractual terms. At September 30, 2013 and December 31, 2012, we had an allowance for doubtful accounts of \$2,000.

## Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss relate entirely to accumulated foreign currency translation losses associated with our foreign subsidiaries and unrealized gains (losses) on investments. Accumulated currency translation losses were \$1.9 million and \$1.5 million as of September 30, 2013 and December 31, 2012, respectively, and accumulated unrealized losses on investments were \$18,000 and zero as of September 30, 2013 and December 31, 2012, respectively.

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The amounts noted in the condensed consolidated statements of comprehensive income (loss) are shown before taking into account the related income tax impact. The income tax effect allocated to each component of other comprehensive income for each of the periods presented is not significant.

## Stock-Based Compensation

We apply the provisions of ASC 718, Stock Compensation, which requires the measurement and recognition of compensation expense for all stock-based payment awards, including grants of stock, restricted stock awards and options to purchase stock, made to employees and directors based on estimated fair values.

The fair value of our stock-based awards was estimated using the following weighted average assumptions for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Stock Option Plan:				
Risk-free interest rate	1.2 %	0.5 %	0.7 %	0.6 %
Expected term	3.6 years	3.7 years	3.7 years	3.7 years
Volatility	57.1 %	57.0 %	56.7 %	57.5 %
Expected dividend	0 %	0 %	0 %	0 %
Weighted average fair value (per share)	\$2.42	\$1.35	\$1.84	\$1.18

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Employee Stock Purchase Plan:				
Risk-free interest rate	0.09 %	0.2 %	0.09 %	0.2 %
Expected term	0.5 years	0.5 years	0.5 years	0.5 years
Volatility	42.8 %	71.7 %	42.8 %	71.7 %
Expected dividend	0 %	0 %	0 %	0 %
Weighted average fair value (per share)	\$1.18	\$0.98	\$1.18	\$0.98

We recorded the following stock-based compensation expense for the three and nine months ended September 30, 2013 and 2012 (in thousands):

Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
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Stock-based compensation expense related to grants of:

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Stock options	\$246	\$821	\$1,375	\$2,786
Employee Stock Purchase Plan (“ESPP”)	24	20	72	53
Restricted Stock Unit (“RSU”)	600	70	987	99
	\$870	\$911	\$2,434	\$2,938

Stock-based compensation expense

recognized in:

Cost of services	\$84	\$85	\$241	\$272
Cost of software and other	3	3	8	25
Research and development	192	252	530	819
Sales and marketing	103	96	285	372
General and administrative	488	475	1,370	1,450
	\$870	\$911	\$2,434	\$2,938

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## Earnings (Loss) Per Share

Basic earnings (loss) per share is computed using our net income (loss) and the weighted average number of common shares outstanding during the reporting period. Diluted earnings (loss) per share is computed using our net income (loss) and the weighted average number of common shares outstanding, including the effect of the potential common shares issuable upon exercise of outstanding stock options, vesting of RSUs and ESPP by using the treasury stock method when dilutive. For the nine months ended September 30, 2012, 1.1 million outstanding options and restricted stock units were excluded from the computation of diluted net loss per share since their effect would have been anti-dilutive. We excluded outstanding weighted average stock options of 999,000 and 1.2 million for the three and nine months ended September 30, 2013, respectively, and 2.9 million for the three and nine months ended September 30, 2012, from the calculation of diluted earnings (loss) per common share because the exercise prices of these stock options were greater than or equal to the average market value of the common stock. These stock options could be included in the calculation in the future if the average market value of the common stock increases and is greater than the exercise price of these stock options.

On October 30, 2013, the Company appointed a new Chief Financial Officer and Chief Operating Officer. Pursuant to his employment offer letter and as approved by the Company's Compensation Committee, the Company issued 195,000 stock options and 284,375 RSUs. These stock options and RSUs were not included in the computation of the basic and diluted earnings per share for the three and nine months ended September 30, 2013 because they were not outstanding during either period.

The following table sets forth the computation of basic and diluted earnings (loss) per share (in thousands, except per share amounts):

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Net income (loss)	\$3,032	\$291	\$7,511	\$(6,722 )
Basic:				
Weighted-average shares of common stock outstanding	52,266	48,707	51,080	48,571
Shares used in computing basic earnings (loss) per share	52,266	48,707	51,080	48,571
Basic earnings (loss) per share	\$0.06	\$0.01	\$0.15	\$(0.14 )
Diluted:				
Weighted-average shares of common stock outstanding	52,266	48,707	51,080	48,571
Add: Common equivalent shares outstanding	2,395	1,619	2,428	—
Shares used in computing diluted earnings (loss) per share	54,661	50,326	53,508	48,571
Diluted earnings (loss) per share	\$0.06	\$0.01	\$0.14	\$(0.14 )

## Warranties and Indemnifications

We generally provide a refund period on sales, during which refunds may be granted to consumers under certain circumstances, including our inability to resolve certain support issues. For our channel sales, the refund period varies by channel partner, but is generally between 5 and 14 days. For our software products, we provide a 30-day money back guarantee. For referral programs and direct transactions, the refund period is generally 5 days. For all sales channels, we recognize revenue net of refunds and cancellations during the period. Refunds and cancellations have not been material to date.

We generally agree to indemnify our customers against legal claims that our software products infringe certain third party intellectual property rights. As of September 30, 2013, we have not been required to make any payment resulting from infringement claims asserted against our customers and have not recorded any related accruals.

Note 2. Warrants

On October 25, 2010, we entered into a Support Services Agreement (the "Customer Agreement") with Comcast Cable Communications Management, LLC ("Comcast") under which Support.com provides technology support services to customers of Comcast in exchange for fees. In connection with the Customer Agreement, Support.com and Comcast entered into a Warrant Agreement, under which Support.com agreed to issue to Comcast warrants to purchase up to 975,000 shares of Support.com common stock in the future in the event that Comcast meets specified sales milestones under the Customer Agreement. Each warrant, if issued, will have an exercise price per share of \$4.9498 and a term of three years from issuance. On September 27, 2011, the Company and Comcast amended the Warrant Agreement to extend the expiration date for the performance milestones while maintaining the previously agreed revenue thresholds. The warrants will be valued as they are earned, and the resulting value will be recorded as a charge against revenue in the period in which the performance milestone is met and the warrant is earned. During the third quarter of 2013, the performance milestones for the first tranche of warrants were met. Therefore, we issued to Comcast warrants to purchase 166,000 shares of our common stock and recorded warrant-related charges of \$383,000 against revenue for the three months and nine months ended September 30, 2013. The value of the first tranche of warrants was estimated using the following assumptions: risk-free interest rate of 0.64%, expected term of 3 years, volatility of 58.51% and expected dividend of 0%. As of September 30, 2013, the performance milestones for the second tranche (warrants to purchase 324,000 shares) and the third tranche (warrants to purchase 485,000 shares) have not been met.

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Note 3. Income Taxes

We recorded an income tax provision of \$121,000 and \$446,000 for the three and nine months ended September 30, 2013, respectively, and \$118,000 and \$353,000 for the three and nine months ended September 30, 2012, respectively.

The provision for income taxes includes estimates of current taxes due in domestic and foreign jurisdictions. This provision reflects tax expense associated with state income tax, foreign taxes, and tax expense related to the recording of a deferred tax liability that results from the amortization for income tax purposes of acquisition-related goodwill.

When goodwill is amortizable for tax purposes, a deferred tax liability is recorded as the tax deduction is realized, which will not be reversed unless and until the goodwill is disposed of or impaired. We will continue to record an income tax expense related to the amortization of goodwill as a discrete item each quarter unless and until such disposition or impairment occurs.

As of September 30, 2013, our deferred tax assets are fully offset by a valuation allowance except in those jurisdictions where it is determined that a valuation allowance is not required. ASC 740, Income Taxes, provides for the recognition of deferred tax assets if realization of such assets is more likely than not. Based upon the weight of available evidence, which includes historical operating performance, reported cumulative net losses since inception and difficulty in accurately forecasting our future results, we provided a full valuation allowance against our net U.S. deferred tax assets and a partial valuation allowance against our foreign deferred tax assets. We reassess the need for our valuation allowance on a quarterly basis. If it is later determined that a portion or all of the valuation allowance is not required there generally will be a benefit to the income tax provision in the period such determination is made.

Note 4. Commitments and Contingencies

Tax contingencies

We are required to make periodic filings in the jurisdictions where we are deemed to have a presence for tax purposes. We have undergone audits in the past and have paid assessments arising from these audits. Our India entity was issued notices of income tax assessment pertaining to the 2004-2009 fiscal years. The notices claimed that the transfer price used in our inter-company agreements with our India entity was too low, and that the price should be increased. We believe our current transfer pricing position is more likely than not to be sustained. We believe that this will be resolved through the normal judicial appeal process used in India, and have submitted our case to the court.

We may be subject to other income tax assessments in the future. We evaluate estimated expenses that could arise from those assessments in accordance with ASC 740. We consider such factors as the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate on the amount of expenses. We record the estimated liability amount of those assessments that meet the definition of an uncertain tax position under ASC 740.

Legal contingencies

On February 7, 2012, a lawsuit seeking class-action certification was filed against the Company in the United States District Court for the Northern District of California, No. 12-CV-00609, alleging that the design of one the Company's software products and the method of promotion to consumers constitute fraudulent inducement, breach of contract, breach of express and implied warranties, and unjust enrichment. On the same day the same plaintiffs' law firm filed another action in the United States District Court for the Southern District of New York, No. 12-CV-0963, involving similar allegations against a subsidiary of the Company and one of the Company's channel partners who distributes our software products, and that channel partner has requested indemnification under contract terms with the Company. The law firm representing the plaintiffs in both cases has filed unrelated class actions in the past against a number of major software providers with similar allegations about those providers' products. On May 30, 2013, the Company received final court approval relating to the terms of the settlement. Under the terms of the settlement, the Company

offered a one-time cash payment, covered by the Company's insurance provider, to qualified class-action members and the deadline to submit a claim form concluded on February 28, 2013. In addition, the Company offered a limited free subscription to one of its software products and the deadline for redemptions concluded on August 31, 2013.

Therefore, the Company reversed a previous accrual of \$57,000 associated with this action and recorded a benefit in the same amount within interest income and other, net in the condensed consolidated statements of operations for the three and nine months ended September 30, 2013. The Company denies any wrongdoing or liability and entered into the settlement to minimize the costs of defense.

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We are also subject to other routine legal proceedings, as well as demands, claims and threatened litigation, that arise in the normal course of our business, potentially including assertions that we may be infringing patents or other intellectual property rights of others. We currently do not believe that the ultimate amount of liability, if any, for such routine legal proceedings (alone or combined) will materially affect our financial position, results of operations or cash flows. The ultimate outcome of any litigation is uncertain, however, and unfavorable outcomes could have a material negative impact on our financial condition and operating results. Regardless of outcome, litigation can have an adverse impact on us because of defense costs, negative publicity, diversion of management resources and other factors.

## Guarantees

We have identified guarantees in accordance with ASC 450. This guidance stipulates that an entity must recognize an initial liability for the fair value, or market value, of the obligation it assumes under the guarantee at the time it issues such a guarantee, and must disclose that information in its interim and annual financial statements. We have entered into various service level agreements with our channel partners, in which we may guarantee the maintenance of certain service level thresholds. Under some circumstances, if we do not meet these thresholds, we may be liable for certain financial costs. We evaluate costs for such guarantees under the provisions of ASC 450. We consider such factors as the degree of probability that we would be required to satisfy the liability associated with the guarantee and the ability to make a reasonable estimate of the resulting cost. We incurred zero and immaterial costs as a result of such obligations during the three and nine months ended September 30, 2013, respectively. We have not accrued any liabilities related to such obligations in the condensed consolidated financial statements as of September 30, 2013 and December 31, 2012.

## Note 5. Business Combination

### RightHand IT Corporation

On January 13, 2012, we executed an Asset Purchase Agreement to acquire certain assets and assume certain liabilities of RightHand IT Corporation (“RHIT”), a managed service provider for small business located in Louisville, Colorado. No stock was acquired as part of the transaction. The acquisition deepened our small business expertise and enabled us to grow our business by providing services to small business customers.

We engaged an independent third-party appraisal firm to assist in determining the fair value of assets acquired and liabilities assumed from the transaction. Such a valuation requires management to make significant estimates, especially with respect to intangible assets. These estimates are based on historical experience and information obtained from the management of the acquired company. We placed value on RHIT’s existing customer relationships, as well as non-compete agreements signed by certain key employees. The purchase price for RHIT exceeded the fair value of RHIT’s net tangible and intangible assets acquired. As a result, we have recorded goodwill in connection with this transaction. The amortization of this goodwill is deductible for tax purposes.

We paid a total of \$1.4 million in cash including \$300,000 held in escrow against payment of a milestone-based earn-out. The earn-out consisted of two criteria-based milestones that were met by specific dates through 2012. The probability-weighted fair value of the \$300,000 payment was \$277,000. As a result, we recorded the \$23,000 difference as other current assets on our condensed consolidated balance sheets. The balance of this asset was zero at December 31, 2012 since all criteria-based milestones have been achieved.

The tangible and identifiable intangible assets acquired and liabilities assumed, and resulting goodwill are summarized below. The financial information presented includes purchase accounting adjustments to the tangible and intangible assets:

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	Amount (in thousands)	Amortization Period
Accounts receivable	\$ 151	
Prepaid expenses and other current assets	46	
Total current assets	197	
Property and equipment, net	108	
Other assets	28	
Acquired assets	333	
Other accrued liabilities	(106 )	
Short-term deferred revenue	(49 )	
Assumed liabilities	(155 )	
Net assets assumed	178	
Identifiable intangible assets:		
Non-compete	70	36 months
Customer base	460	60 months
Goodwill	619	
Total purchase consideration	1,327	
Other current asset	23	
Total cash consideration	\$ 1,350	

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The operating results of RHIT have been included in our accompanying condensed consolidated statements of operations from January 14, 2012, the day following acquisition. Pro-forma results of operations have not been presented because the acquisition was not material to our results of operations. In addition to the \$1.4 million cash consideration, we incurred acquisition-related expenditures of approximately \$33,000 through June 30, 2012, which were expensed in the periods in which they were incurred in accordance with ASC 805, Business Combinations. These expenses were recorded in general and administrative expense in our condensed consolidated statements of operations.

## Note 6. Intangible Assets

Amortization expense and other related to intangible assets for the three and nine months ended September 30, 2013 was \$335,000 and \$1.0 million, respectively. Amortization expense and other related to intangible assets for the three and nine months ended September 30, 2012 was \$397,000 and \$1.2 million, respectively.

The following table summarizes the components of intangible assets (in thousands):

	Non-compete	Partner Relationships	Customer Base	Technology Rights	Tradenames	Indefinite Life Intangibles	Total
As of September 30, 2013							
Gross carrying value	\$ 593	\$ 145	\$ 641	\$ 5,330	\$ 760	\$ 250	\$7,719
Accumulated amortization	(464 )	(145 )	(332 )	(2,448 )	(560 )	—	(3,949)
Net carrying value	\$ 129	\$ —	\$ 309	\$ 2,882	\$ 200	\$ 250	\$3,770
As of December 31, 2012							
Gross carrying value	\$ 593	\$ 145	\$ 641	\$ 5,330	\$ 760	\$ 250	\$7,719
Accumulated amortization	(426 )	(145 )	(239 )	(1,700 )	(434 )	—	(2,944)
Net carrying value	\$ 167	\$ —	\$ 402	\$ 3,630	\$ 326	\$ 250	\$4,775

In December 2006, we acquired the use of a toll-free telephone number for cash consideration of \$250,000. This asset has an indefinite useful life.

The estimated future amortization expense of intangible assets, with the exception of the indefinite-life intangible assets as of September 30, 2013 is as follows (in thousands):

<u>Fiscal Year</u>	<u>Amount</u>
2013(October-December)	\$ 316
2014	1,091
2015	1,069
2016	1,028
2017	16
Total	\$ 3,520
	3.2
Weighted average remaining useful life	years

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The following table summarizes the components of purchased technology (in thousands):

	As of September 30, 2013	As of December 31, 2012
Purchased technology	\$ 350	\$ 350
Accumulated amortization	(350 )	(288 )
Total purchased technology, net	\$ —	\$ 62

## Note 7. Other Accrued Liabilities

Other accrued liabilities consist of the following (in thousands):

	As of September 30, 2013	As of December 31, 2012
Accrued expenses	\$ 2,335	\$ 2,421
Customer deposits	1,042	997
Other accrued liabilities	479	551
Total other accrued liabilities	\$ 3,856	\$ 3,969

## Note 8. Stockholder's Equity

## Stock Options

The following table represents the stock option activity for the nine months ended September 30, 2013:

	Number of Shares	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding options at December 31, 2012	9,529,597	\$ 3.05	3.63	\$ 12,595
Granted	256,550	\$ 4.37		
Exercised	(3,771,188)	\$ 2.53		
Forfeited	(216,049 )	\$ 4.33		
Outstanding options at September 30, 2013	5,798,910	\$ 3.40	3.51	\$ 12,436
Options vested and expected to vest	5,742,681	\$ 3.40	3.48	\$ 12,347
Exercisable at September 30, 2013	4,541,237	\$ 3.23	2.95	\$ 10,420

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value that would have been received by the option holders had they all exercised their options on September 30, 2013. This amount changes based on the fair market value of our stock. The aggregate intrinsic value of options exercised under our stock option plans was \$3.5 million and \$8.1 million during the three and nine months ended September 30, 2013, respectively, and \$195,000 and \$401,000 during the three and nine months ended September 30, 2012, respectively. Total fair value of options vested was \$398,000 and \$1.6 million during the three and nine months ended September 30, 2013, respectively, and \$891,000 and \$2.9 million during the three and nine months ended September 30, 2012, respectively.

At September 30, 2013, there was \$1.7 million of unrecognized compensation cost related to existing stock options outstanding which is expected to be recognized over a weighted average period of 2.13 years.

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## Employee Stock Purchase Plan

In the second quarter of 2011, to advance the interests of the Company and its stockholders by providing an incentive to attract, retain and reward eligible employees and by motivating such persons to contribute to the growth and profitability of the Company, the Company's Board of Directors and stockholders approved an ESPP and reserved 1,000,000 shares of our common stock for issuance effective as of May 15, 2011. The ESPP continues in effect for ten (10) years from its effective date unless terminated earlier by the Company. The ESPP consists of six-month offering periods during which employees may enroll in the plan. The purchase price on each purchase date shall not be less than eighty five percent (85%) of the lesser of (a) the fair market value of a share of stock on the offering date of the offering period or (b) the fair market value of a share of stock on the purchase date. During the nine months ended September 30, 2013, 38,915 shares were granted under ESPP.

## Restricted Stock Units

The following table represents RSU activity for the nine months ended September 30, 2013:

	Number of Shares	Weighted Average Grant Date Fair Value
Outstanding RSUs at December 31, 2012	98,363	\$ 2.82
Granted	1,443,112	\$ 5.05
Vested	(108,363 )	\$ 2.98
Forfeited	(16,300 )	\$ 5.89
Outstanding RSUs at September 30, 2013	1,416,812	\$ 5.04

On August 5, 2013, pursuant to approval by the Company's Compensation Committee, the Company issued 725,000 RSUs to its corporate employees. These RSUs vest annually in three equal tranches over three years.

On May 23, 2013, the Board of Directors of the Company approved, based on recommendations of the Compensation Committee, a grant of 48,851 RSUs to non-employee directors based on a fair market value of \$4.70 per share which represents the closing price of the Company's common stock on the Nasdaq Global Select Market ("Nasdaq") on May 23, 2013. These RSUs vest upon the first anniversary of the grant date.

During the first quarter of 2013, the Company's Compensation Committee approved the grant of RSUs to certain key executives. The RSUs granted to these executives included (i) 249,750 time-based RSUs that vest over a required service period of three years, and (ii) 399,750 performance-based RSUs contingent upon a required service period of three years and as well as the Company's achievement of specified annual performance targets for fiscal year 2013. We measured the grant-date fair value of the performance-based RSUs based upon the closing price of the Company's common stock on the Nasdaq as of the grant date. We expense the fair value of the performance-based RSUs that are probable of being earned based on our forecasted annual performance for fiscal year 2013.

At September 30, 2013, there was \$5.5 million of unrecognized compensation cost related to RSUs which is expected to be recognized over a weighted average period of 2.26 years.

## Stock Repurchase Program



On April 27, 2005, our Board of Directors authorized the repurchase of up to 2,000,000 outstanding shares of our common stock. As of September 30, 2013 the maximum number of shares remaining that can be repurchased under this program was 1,807,402. The Company does not intend to repurchase shares without a further approval from its Board of Directors.

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Repurchase of Shares

On February 19, 2013, the Company entered into an agreement with Joshua Pickus, the Company's President and Chief Executive Officer, pursuant to which Mr. Pickus sold directly to the Company on that day an aggregate 1,000,000 shares of its common stock acquired by him in a same-day exercise of fully vested options which were due to expire at the end of their seven-year term on April 6, 2013. Under the agreement, the purchase price per share was established as an amount equal to the lesser of (a) the closing price of the Company's common stock in regular trading hours on the day of the sale as reported by Nasdaq less 5%, or (b) the thirty-day simple moving average price of the Company's common stock on the day of the sale. This formula produced a purchase price per share of \$4.114, less the aggregate strike price due on exercise of the options underlying the repurchased shares of \$2.32 per share, which then resulted in a net cash outlay by the Company to acquire the shares of approximately \$1.8 million (or \$1.794 per share). The agreement was approved by the independent members of the Company's Board of Directors. The share repurchase amounted to \$4.1 million and is classified under treasury stock within stockholders' equity of the condensed consolidated balance sheets.

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

The following discussion of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and the related notes included elsewhere in this Form 10-Q (the "Report") and the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2012. The following discussion includes forward-looking statements. Please see "Risk Factors" in Item 1A of Part II of this Report for important information to consider when evaluating these statements.

Overview

Support.com is a leading provider of cloud-based services and software designed to enhance a customer's experience with technology. We enable leading brands to offer technology service programs that create new revenue streams and deepen customer relationships. We also help technology support organizations reduce costs, improve problem resolution and enhance the customer experience. Our solutions include the cloud-based Nexus® Service Delivery Platform ("Nexus platform"), a scalable workforce of technology specialists, mobile and desktop applications for end-users and proven expertise in program design and execution. We market our products and services directly and indirectly through channel partners. Our customers and channel partners include leading communications providers, retailers, technology companies and others. Our sales and marketing efforts are primarily focused in North America.

Total revenue for the third quarter of 2013 increased 29% year-over-year. Revenue from services increased 31% year-over-year primarily due to continued growth in our channel programs, primarily the programs with Comcast. Revenue from software and other increased 19% year-over-year primarily due to fees from licensing of our Nexus platform.

Cost of services for the third quarter of 2013 increased 25% year-over-year as a result of the hiring of additional technology specialists to support revenue growth. Cost of software and other for the third quarter of 2013 decreased 6% year-over-year due to lower royalty rate payments to third-party developers. Total gross margin was consistent year-over-year at 51% in the third quarter of 2013 and 50% in the third quarter of 2012.

Operating expenses were relatively consistent year-over-year at \$9 million and \$8.7 million for the third quarters of 2013 and 2012, respectively.

During the third quarter of 2013, the Company entered into program description number 3 (“Program Agreement”) under the Amended and Restated Support Services Agreement, dated July 5, 2012, with Comcast. Under the Program Agreement, the Company provided home networking support services to Comcast customers on an hourly basis.

In addition, during the third quarter of 2013, the Company reviewed the performance of advertising programs for its end-user software products. Upon completion of this review, the Company discontinued its largest advertising placement for such products because it no longer yielded positive results.

We intend the following discussion of our financial condition and results of operations to provide information that will assist in understanding our condensed consolidated financial statements, the changes in certain key items in those condensed consolidated financial statements from year to year, and the primary factors that accounted for those changes, as well as how certain accounting principles, policies and estimates affect our condensed consolidated financial statements.

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## Critical Accounting Policies and Estimates

In preparing our financial statements, we make estimates, assumptions and judgments that can have a significant impact on our revenue, operating income or loss and net income or loss, as well as on the value of certain assets and liabilities on our condensed consolidated balance sheet. We believe that the estimates, assumptions and judgments involved in the accounting policies described in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012 have the greatest potential impact on our condensed consolidated financial statements, so we consider them to be our critical accounting policies and estimates. There have been no significant changes in these critical accounting policies and estimates during the three and nine months ending September 30, 2013.

## RESULTS OF OPERATIONS

The following table sets forth the results of operations for the three and nine months ended September 30, 2013 and 2012 expressed as a percentage of total revenue.

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Revenue:				
Services	83 %	81 %	81 %	80 %
Software and other	17	19	19	20
Total revenue	100	100	100	100
Costs of revenue:				
Cost of services	47	48	46	54
Cost of software and other	1	2	1	2
Total cost of revenue	49	50	46	56
Gross profit	51	50	53	44
Operating expenses:				
Research and development	6	9	7	10
Sales and marketing	18	21	20	28
General and administrative	13	16	13	16
Amortization of intangible assets and other	1	2	2	2
Total operating expenses	39	48	41	56
Income (loss) from operations	13	2	12	(12 )
Interest and other income, net	1	0	0	0
Income (loss) from continuing operations, before income taxes	13	2	12	(13 )
Income tax provision	1	1	1	1
Income (loss) from continuing operations, after income taxes	13	3	12	(13 )

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Income (loss) from discontinued operations, after income taxes	(0 )	(0 )	(0 )	0
Net income (loss)	13 %	2 %	12 %	(13 )%

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## REVENUE

In thousands, except percentages	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013	2012	\$ Change	% Change	2013	2012	\$ Change	% Change
Services	\$ 19,305	\$ 14,769	\$ 4,536	31 %	\$ 51,879	\$ 42,278	\$ 9,601	23 %
Software and other	4,054	3,407	647	19 %	11,807	10,799	1,008	9 %
Total revenue	\$ 23,359	\$ 18,176	\$ 5,183	29 %	\$ 63,686	\$ 53,077	\$ 10,609	20 %

Services. Services revenue consists primarily of fees for technology services generated from our channel partners. We provide these services remotely, generally using service delivery personnel who utilize our proprietary technology to deliver the services. Services revenue for the three months and nine months ended September 30, 2013 increased by \$4.5 million and \$9.6 million, respectively, compared to the same periods in 2012. The increase was due primarily to continued growth in our channel programs, primarily the programs with Comcast. For the three months ended September 30, 2013, services revenue generated from our channel partnerships was \$18.6 million compared to \$13.8 million for the same period in 2012, while direct services revenue was \$739,000 compared to \$924,000 for the same period in 2012. For the nine months ended September 30, 2013, services revenue generated from our channel partnerships was \$49.4 million compared to \$39.2 million for the same period in 2012, while direct services revenue was \$2.4 million compared to \$3.0 million for the same period in 2012.

Software and other. Software and other revenue is comprised primarily of fees for end-user software products provided through direct customer downloads, and, to a lesser extent, through the sale of this software via channel partners and licensing of our Nexus platform. Software and other revenue for the three months ended September 30, 2013 increased by 19% compared to same period in 2012 primarily due to fees from licensing of our Nexus platform. For the three months ended September 30, 2013, software and other revenue generated from our direct sales, including licenses of our Nexus platform, was \$2.5 million compared to \$1.9 million for the same period in 2012, while software and other revenue generated from our channel partnerships was \$1.6 million compared to \$1.5 million for the same period in 2012. Software and other revenue for the nine months ended September 30, 2013 increased by 9% compared to same period in 2012 primarily due to fees from licensing of our Nexus platform. For the nine months ended September 30, 2013, software revenue from direct sales was \$7.1 million compared to \$6.4 million for the same period in 2012, while software and other revenue generated from our channel partnerships was \$4.7 million compared to \$4.4 million from the same period in 2012.

## COSTS AND EXPENSES

## Costs of Revenue

In thousands, except percentages	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013	2012	\$ Change	% Change	2013	2012	\$ Change	% Change
Cost of services	\$ 11,046	\$ 8,815	\$ 2,231	25 %	\$ 29,194	\$ 28,696	\$ 498	2 %
Cost of software and other	294	312	(18 )	(6 )%	872	1,142	(270 )	(24 )%
Total cost of revenue	\$ 11,340	\$ 9,127	\$ 2,213	24 %	\$ 30,066	\$ 29,838	\$ 228	1 %

Cost of services. Cost of services consists primarily of compensation and related cost of personnel and contractors providing services, and technology and telecommunication expenses associated to the delivery of services. The increase of \$2.2 million and \$498,000 in cost of services for the three and nine months ended September 30, 2013, respectively, compared to the same periods in 2012 was mainly driven by increased compensation and employee

related costs associated with the increase in our technology specialist workforce to support revenue growth.

Cost of software and other. Cost of software and other fees consists primarily of third-party royalty fees for our end-user software products. Certain of these products were developed using third-party research and development resources, and the third-party receives royalty payments on sales of products it developed. The decrease of \$18,000 and \$270,000 for the three and nine months ended September 30, 2013, respectively, over the same periods in 2012 was primarily due to a reduction of third-party royalty fees as the Company reduced the reliance on third-party software products.

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## Operating Expenses

In thousands, except percentages	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013	2012	\$ Change	% Change	2013	2012	\$ Change	% Change
Research and development	\$ 1,456	\$ 1,643	\$ (187 )	(11 )%	\$ 4,325	\$ 5,121	\$ (796 )	(16 )%
Sales and marketing	\$ 4,120	\$ 3,789	\$ 331	9 %	\$ 12,431	\$ 14,908	\$ (2,477)	(17 )%
General and administrative	\$ 3,077	\$ 2,897	\$ 180	6 %	\$ 8,193	\$ 8,661	\$ (468 )	(5 )%

Research and development. Research and development expense consists primarily of compensation costs, third-party consulting expenses and related overhead costs for research and development personnel. Research and development costs are expensed as they are incurred. The decrease of \$187,000 and \$796,000 in research and development expense for the three and nine months ended September 30, 2013, respectively, compared to the same periods in 2012 resulted primarily from a decrease in salary and employee related expenses including stock-based compensation expense due to a decrease in headcount.

Sales and marketing. Sales and marketing expense consists primarily of compensation costs of business development, program management and marketing personnel, as well as expenses for lead generation and promotional activities, including public relations, advertising and marketing. Sales and marketing expense for 2012, but not 2013, also included sales commissions for contact center sales agents. The increase of \$331,000 in sales and marketing expense for the three months ended September 30, 2013 compared to the same period in 2012 resulted primarily from advertising costs for end-user software products of \$422,000 (prior to our decision to discontinue our largest advertising placement), offset by a decrease in compensation and employee-related costs of \$108,000 due to decrease in headcount. The decrease of \$2.5 million in sales and marketing expense for the nine month ended September 30, 2013 compared to the same period in 2012 resulted from a reduction in contact sales agent workforce completed at the end of second quarter of 2012.

General and administrative. General and administrative expense consists primarily of compensation costs and related overhead costs for administrative personnel, and professional fees for legal, accounting and other professional services. The increase of \$180,000 for the three months ended September 30, 2013 compared to the same period in 2012 was primarily due to an increase of \$155,000 in compensation and related cost as a result of headcount growth and an increase of \$265,000 in recruiting fees for certain corporate positions and hiring expenses to support the new Comcast program, offset by decrease of \$190,000 in overhead costs. The decrease of \$468,000 in general and administrative expense for the nine months ended September 30, 2013 compared to the same period in 2012 was primarily due to a decrease of \$142,000 in professional services, decrease \$214,000 in franchise tax expense and a decrease of \$284,000 in overhead cost including rent and depreciation, offset by increase of \$248,000 in recruiting fees for certain corporate positions and hiring expenses to support revenue growth.

## Amortization of Intangible Assets and Other

In thousands, except percentages	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013	2012	\$ Change	% Change	2013	2012	\$ Change	% Change
Amortization of intangible assets and other	\$ 335	\$ 397	\$ (62 )	(16 )%	\$ 1,005	\$ 1,155	\$ (150 )	(13 )%



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The decrease in amortization of intangible assets and other for the three and nine months ended September 30, 2013 compared to the same periods in 2012 was primarily due to the re-measurement of milestone based earn-outs in connection with the acquisitions of RightHand IT Corporation in January 2012 and SUPERAntiSpyware in June 2011.

INTEREST INCOME AND OTHER, NET

	Three Months Ended September 30,				Nine Months Ended September 30,			
			\$	%			\$	%
In thousands, except percentages	2013	2012	Change	Change	2013	2012	Change	Change
Interest income and other, net	\$ 127	\$ 93	\$ 34	36 %	\$ 307	\$ 227	\$ 80	35 %

The increase in interest income and other for the three and nine months ended September 30, 2013 compared to the same periods in 2012 was primarily due to higher interest income on our investments as a result of higher yields and higher balances in our portfolio.

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## INCOME TAX PROVISION

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2013	2012	\$ Change	% Change	2013	2012	\$ Change	% Change
In thousands, except percentages								
Income tax provision	\$ 121	\$ 118	\$ 3	3 %	\$ 446	\$ 353	\$ 93	26 %

The income tax provision is comprised of estimates of current taxes due in domestic and foreign jurisdictions. For the three and nine months ended September 30, 2013 and 2012, income tax provision primarily consisted of state income tax, foreign taxes, and tax expense related to the recording of a deferred tax liability that results from the amortization for income tax purposes of acquisition-related goodwill. The increase in the income tax provision from 2012 to 2013 was primarily due to tax expense related to state and foreign income taxes.

## LIQUIDITY AND CAPITAL RESOURCES

Total cash, cash equivalents and investments at September 30, 2013 was \$68.5 million, compared to \$56.3 million at December 31, 2012. Cash equivalents and investments are comprised of money market funds, certificate of deposits, corporate notes and bonds, and U.S. government agency securities. The increase was primarily due to \$7.4 million cash generated from operating activities, and proceeds from exercises of employee stock options net of repurchase of shares of \$5.6 million.

## Operating Activities

Net cash provided by (used in) operating activities was \$7.4 million and (\$603,000) million for the nine months ended September 30, 2013 and 2012, respectively. Net cash provided by (used in) operating activities primarily reflect the net income (loss) for the period, adjusted for non-cash items such as depreciation, amortization of premiums and discounts on investments, stock-based compensation expense and amortization of intangible assets and changes in operating assets and liabilities.

Net cash provided by operating activities of \$7.4 million for the nine months ended September 30, 2013 resulted primarily from net income for the period of \$7.5 million, adjusted for non-cash items totaling \$4.6 million and changes in operating assets and liabilities of (\$4.7) million. Adjustment for non-cash items primarily consisted of stock-based compensation expense of \$2.4 million, amortization of intangible assets and other of \$1.0 million, amortization of premiums and discounts on investments of \$442,000, a warrant-related charge of \$383,000, and depreciation of \$262,000. The changes in operating assets and liabilities primarily consisted of an increase in accounts receivable of \$3.9 million, prepaid expenses and other current assets of \$891,000, accrued compensation of \$1.5 million offset by a decrease in deferred revenue of \$2.3 million.

Net cash used in operating activities was \$603,000 for the nine months ended September 30, 2012 and resulted primarily from a net loss for the period of \$6.7 million, adjusted by non-cash items totaling \$5.0 million and changes in operating assets and liabilities of \$1.1 million. Adjustment for non-cash items primarily included stock-based compensation expense of \$2.9 million, amortization of premiums and discounts on investments of \$446,000, amortization of intangible assets and other of \$1.1 million and depreciation of \$404,000. The changes in operating assets and liabilities primarily consisted of decrease in accounts receivable of \$649,000 and accounts payable of \$507,000, offset by an increase in prepaid expenses and other current assets of \$533,000, accrued compensation of \$646,000 and deferred revenue of \$849,000.

## Investing Activities

Net cash provided by (used in) investing activities was (\$13.0) million and \$813,000 for the nine months ended September 30, 2013 and 2012, respectively. Net cash used in investing activities for the nine months ended September 30, 2013 was primarily due to purchases of investments of \$43.8 million offset by maturities of investments of \$31.0 million, and purchases of property and equipment of \$178,000. Net cash provided by investing activities for the nine months ended September 30, 2012 was primarily due to sale and maturities of investment of \$36.0 million offset by purchases of investments of \$33.3 million, acquisition of RightHand IT Corporation for \$1.3 million and purchases of property and equipment for \$503,000.

#### Financing Activities

Net cash provided by financing activities was \$5.6 million and \$1.1 million for the nine months ended September 30, 2013 and 2012, respectively. Net cash provided by financing activities for the nine months ended September 30, 2013 was from the proceeds of exercise of employee stock options of \$9.7 million (including exercise of stock options that resulted in shares that were repurchased) offset by the repurchase of shares of \$4.1 million. Net cash provided by financing activities for the nine months ended September 30, 2012 was from the proceeds of exercise of employee stock options.

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Working Capital and Capital Expenditure Requirements

At September 30, 2013, stockholders' equity was \$89.7 million and working capital was \$71.7 million. We believe that our existing cash balances will be sufficient to meet our working capital requirements and our planned capital expenditures for at least the next 12 months.

If we require additional capital resources to grow our business internally or to acquire complementary technologies and businesses at any time in the future, we may seek to sell additional equity or debt securities. The sale of additional equity could result in dilution to our existing stockholders.

We plan to continue to make investments in our business during 2013. We believe these investments are essential to creating sustainable growth in our business in the future. Additionally, we may choose to acquire other businesses or complimentary technologies to enhance our product capabilities and such acquisitions would likely require the use of cash.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate and Market Risk

There has been significant deterioration and continuing instability in the financial markets. This extraordinary disruption and readjustment in the financial markets exposes us to additional investment risk. The value and liquidity of the securities in which we invest could deteriorate rapidly and the issuers of such securities could be subject to credit rating downgrades. In light of the current market conditions and these additional risks, we actively monitor market conditions and developments specific to the securities and security classes in which we invest. While we believe we take prudent measures to mitigate investment related risks, such risks cannot be fully eliminated, as there are circumstances outside of our control.

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. To achieve this objective, we invest our excess cash in a variety of securities, including U.S. government agency securities, corporate notes and bonds, commercial paper and money market funds. These securities are classified as available-for-sale. Consequently, our available-for-sale securities are recorded on the consolidated balance sheets at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive loss within stockholder's equity. Our holdings of the securities of any one issuer, except government agencies, do not exceed 10% of our portfolio. We do not utilize derivative financial instruments to manage our interest rate risks.

As of September 30, 2013, we held \$37.8 million in short-term investments (excluding cash and cash equivalents), which consisted primarily of government debt securities, corporate notes and bonds, and commercial paper. The weighted average interest rate of our portfolio was approximately 0.24% at September 30, 2013. A decline in interest rates over time would reduce our interest income from our investments. A hypothetical 10% increase or decrease in interest rates, however, would not have a material impact adverse effect on our financial condition.

Impact of Foreign Currency Rate Changes

The functional currencies of our international operating subsidiaries are the local currencies. We translate the assets and liabilities of our foreign subsidiaries at the exchange rates in effect on the balance sheet date. We translate their income and expenses at the average rates of exchange in effect during the period. We include translation gains and losses in the stockholders' equity section of our consolidated balance sheets. We include net gains and losses resulting from foreign exchange transactions in interest income and other in our consolidated statements of operations. Since we translate foreign currencies (primarily Canadian dollars and Indian rupees) into U.S. dollars for a small portion of

our operations, currency fluctuations have had an immaterial impact on our consolidated statements of operations. We have both revenue and expenses that are denominated in foreign currencies. Neither a weaker or stronger U.S. dollar environment would have a material impact on our consolidated statement of operations. The historical impact of currency fluctuations on our consolidated statements of operations has generally been immaterial. As of September 30, 2013, we did not engage in foreign currency hedging activities.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain “disclosure controls and procedures,” as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Our disclosure controls and procedures have been designed to meet, and our management believes they meet, reasonable assurance standards. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Our Chief Executive Officer and our Chief Financial Officer, after evaluating the effectiveness of our “disclosure controls and procedures” as of the end of the period covered by this quarterly report, have concluded that our disclosure controls and procedures are effective based on their evaluation of these controls and procedures required by paragraph (b) of Exchange Act Rules 13a-15 or 15d-15.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2013, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Note 4 “Commitments and Contingencies” to the condensed consolidated financial statements in Part I, Item 1 of this Quarterly Report on Form 10-Q for a description of legal proceedings.

ITEM 1A. RISK FACTORS

This report contains forward-looking statements regarding our business and expected future performance as well as assumptions underlying or relating to such statements of expectation, all of which are “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. We are subject to many risks and uncertainties that may materially affect our business and future performance and cause those forward-looking statements to be inaccurate. Words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “forecasts,” “estimates,” “seeks,” “may result in,” “focused on,” “continue to,” and similar expressions often identify forward-looking statements. In this report, forward-looking statements include, without limitation, the following:

Our expectations and beliefs regarding future financial results;

Our expectations regarding channel partners, renewal of contracts with these partners and the anticipated timing and magnitude of revenue from programs with these partners;

Our ability to successfully license, implement and support our Nexus Service Delivery Platform independent of our services;

Our expectations regarding sales of our end-user software, and our ability to source, develop and distribute additional software products;

Our ability to successfully monetize customers who receive free versions of our end-user software products;

Our expectations regarding our ability to deliver technology services efficiently and through arrangements that are profitable, including both in SKU-based pricing models as well as time-based billing for services and other pricing models we may employ;

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Our ability to execute effectively in the small business market;

Our ability to offer subscriptions to our services in a profitable manner;

Our ability to hire, train, manage and retain technology specialists in a home-based model in quantities sufficient to meet forecast requirements, and our ability to continue to enhance the flexibility of our staffing model;

Our ability to match staffing levels with service volume in a cost-effective manner;

Our ability to manage contract labor as a component of our workforce;

Our ability to operate successfully in a time-based billing model;

Our ability to manage sales costs in programs where we are responsible for sales;

Our ability to successfully manage advertising costs associated with our end-user software products;

Our beliefs and expectations regarding the introduction of new services and products, including additional software products and service offerings for devices beyond the computer;

Our expectations regarding revenues, cash flows and expenses, including cost of revenue, sales and marketing, research and development efforts, and administrative expenses;

Our assessment of seasonality, mix of revenue, and other trends for our business and the business of our channel partners;

Our ability to deliver projected levels of profitability;

Our expectations regarding the costs and other effects of acquisition and disposition transactions;

Our expectations regarding unit volumes, pricing and other factors in the market for computers and other technology devices, and the effects of such factors on our business;

Our expectations regarding the results of pending, threatened or future litigation;

The assumptions underlying our Critical Accounting Policies and Estimates, including our assumptions regarding revenue recognition; assumptions used to estimate the fair value of share-based compensation; assumptions regarding the impairment of goodwill and intangible assets; and expected accounting for income taxes; and

The expected effects of the adoption of new accounting standards.

An investment in our stock involves risk, and we caution investors that forward-looking statements are only predictions based on our current expectations about future events and are not guarantees of future performance. We encourage you to read carefully all information provided in this report and in our other filings with the SEC before deciding to invest in our stock or to maintain or change your investment. Forward-looking statements are based on information as of the filing date of this report, and we undertake no obligation to publicly revise or update any forward-looking statement for any reason.

Because forward-looking statements involve risks and uncertainties, there are important factors that may cause actual results to differ materially from our stated expectations. These factors are described below. This list does not include



all risks that could affect our business, and if these or any other risks or uncertainties materialize, or if our underlying assumptions prove to be inaccurate, actual results could differ materially from past results and from our expected future results.

Until recently, our business has not been profitable and may not achieve profitability in future periods.

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From the third quarter of 2012 through the third quarter of 2013, we delivered our first five quarters of profitability since 2005. We intend to make significant investments in support of our business, and may sustain losses in the future notwithstanding our efforts to maintain profitability. If we fail to achieve revenue growth as a result of our additional investments or if such revenue growth does not result in our maintaining profitability, the market price of our common stock will likely decline. A sustained period of losses would result in usage of cash to fund our operating activities and a corresponding reduction in our cash balance.

Our business is based on a relatively new and evolving business model.

We are executing a plan to grow our business by providing premium technology services, licensing our Nexus platform and providing end-user software products. We may not be able to offer these services and software products successfully. Our technology specialists are generally home-based, which requires a high degree of coordination and quality control of employees working from diverse and remote locations. Until recently, we have experienced financial losses in our business and we may use cash and incur costs in the future to support our growth initiatives. Our investments, which typically are made in advance of revenue, may not yield increased revenue to offset these expenses. As a result of these factors, the future revenue and income potential of our business is uncertain. Any evaluation of our business and our prospects must be considered in light of these factors and the risks and uncertainties often encountered by companies in our early stage of development. Some of these risks and uncertainties relate to our ability to do the following:

- Maintain our current relationships and programs, and develop new relationships, with channel partners and licensees of our technology platform and services on acceptable terms or at all;
- Reach prospective customers for our end-user software in a cost-effective fashion;
- Reduce our dependence on a limited number of channel partners for a substantial majority of our revenue;
- Attract and retain qualified management and employees;
- Hire, train, manage and retain our home-based technology specialists and enhance the flexibility of our staffing model in a cost-effective fashion and in quantities sufficient to meet forecast requirements;
- Manage substantial headcount changes over short periods of time;
- Manage contract labor efficiently and effectively;
- Meet anticipated growth targets;
- Maintain gross and operating margins;
- Match staffing levels with demand for services and forecast requirements;
- Obtain bonuses and avoid penalties in contractual arrangements;
- Manage our business to provide services and sales on an efficient basis in order to maintain profitability;
- Offer subscriptions to our services in a profitable manner;
- Successfully introduce new, and adapt our existing, services and products for consumers and small businesses;
- Respond effectively to changes in the online advertising markets in which we participate;
- Respond effectively to competition;
- Operate effectively in the small business market;
  - Successfully license our Nexus platform;
- Respond to changes in macroeconomic conditions as they affect our and our channel partners' operations;
- Realize benefits of any acquisitions we make;
- Adapt to changes in the markets we serve, including the decline in sales of personal computers and the proliferation of tablets and other mobile devices;
- Adapt to changes in our industry, including consolidation;
- Respond to government regulations relating to our current and future business;
- Manage and respond to present, threatened, and future litigation; and
- Manage our expanding operations and implement and improve our operational, financial and management controls.

If we are unable to address these risks, our business, results of operations and prospects could suffer.

Our quarterly results have in the past, and may in the future, fluctuate significantly.

Our quarterly revenue and operating results have in the past and may in the future fluctuate from quarter to quarter. As a result, we believe that quarter-to-quarter and year-to-year comparisons of our revenue and operating results may not be accurate indicators of future performance.

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Several factors that have contributed or may in the future contribute to fluctuations in our operating results include:

Demand for our services and products;  
The performance of our channel partners;  
    Change in or discontinuance of our principal programs with channel partners;  
Our reliance on a small number of channel partners for a substantial majority of our revenue;  
Instability or decline in the global macroeconomic climate and its effect on our and our channel partners' operations;  
Our ability to retain qualified management and employees;  
The efficiency of our technology specialists;  
Our ability to effectively match staffing levels with service volumes on a cost-effective basis;  
Our ability to manage contract labor;  
Hire, train, manage and retain our home-based technology specialists and enhance the flexibility of our staffing model in a cost-effective fashion and in quantities sufficient to meet forecast requirements;  
Manage substantial headcount changes over short periods of time;  
Our ability to manage sales costs in programs where we are responsible for sales;  
Our ability to attract and retain customers and channel partners;  
Our ability to reach customers directly in a cost effective manner;  
Our ability to serve the small business market;  
Our ability to successfully license our Nexus platform;  
The availability and cost-effectiveness of advertising placements for our software products and our ability to respond to changes in the online advertising markets in which we participate;  
The price and mix of products and services we or our competitors offer;  
The rate of expansion of our offerings and our investments therein;  
Our ability to successfully monetize customers who receive free versions of our software;  
Usage rates on the subscriptions we offer;  
Changes in the markets for computers and other technology devices relating to unit volume, pricing and other factors, including changes driven by declines in sales of personal computers and the growing popularity of tablets and other mobile devices, and the effects of such changes on our business;  
Our ability to adapt to our customers' needs in a market space defined by frequent technological change;  
The amount and timing of operating costs and capital expenditures in our business;  
Diversion of management's attention from other business concerns and disruption of our ongoing business activities as a result of acquisitions or divestitures by us;  
    Costs related to the defense and settlement of litigation which can also have an additional adverse impact on us because of negative publicity, diversion of management resources and other factors;  
Potential losses on investments, or other losses from financial instruments we may hold that are exposed to market risk; and  
The exercise of judgment by our management in making accounting decisions in accordance with our accounting policies.

Our inability to meet future financial performance targets that we announce or that are published by research analysts could cause the market price of our common stock to decline.

From time to time, we provide guidance related to our future financial performance. In addition, financial analysts may publish their own expectations of our future financial performance. Because our quarterly revenue and our operating results fluctuate and are difficult to predict, future financial performance is difficult to predict. We have in the past failed to meet our guidance for a particular period or analyst expectations for our guidance for future periods and our stock price has declined. Generally, the market prices of technology companies have been extremely volatile. Stock prices of many technology companies have often fluctuated in a manner unrelated or disproportionate to the operating performance of such companies. In the past, following periods of market volatility, stockholders have often

initiated securities class action litigation relating to the stock trading and price volatility of the technology company in question. Any securities litigation we may become involved in could result in our incurring substantial defense costs and diverting resources and the attention of management from our business.

Because a small number of customers and channel partners have historically accounted for, and for the foreseeable future will account for, the substantial majority of our revenue, under-performance of specific programs or loss of certain customers, channel partners or programs could decrease our revenue substantially.

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For the third quarter of 2013, Comcast (55%) accounted for 10% or more of our total revenues. The loss of this or other significant partners, the worsening of the terms or terminations of our arrangements with any of these partners, the reduction or discontinuance of programs with any of these partners, or the failure of any of these partners to achieve their targets could adversely affect our business. Generally, the agreements with our partners do not require them to conduct any minimum amount of business with us, and therefore they have decided in the past and could decide at any time in the future to reduce or eliminate their programs or the use of our services in such programs. They may also enter into multi-sourcing arrangements with other vendors for services previously provided exclusively by us. Further, we may not successfully obtain new channel partners or customers. There is also the risk that, once established, our programs with these and other channel partners may take longer than we expect to produce revenue or may not produce revenue at all, and the revenue produced may not be profitable if the costs of performing under the program are greater than anticipated or the program terminates before up-front investments can be recouped. One or more of our key channel partners may also choose not to renew their relationship with us, discontinue their programs, offer them only on a limited basis or devote insufficient time and attention to promoting them to their customers. Some of our key channel partners may prefer not to work with us if we also partner with their competitors. If any of these key channel partners merge with one of their competitors, all of these risks could be exacerbated.

Each of these risks could reduce our sales and have a material adverse effect on our operating results. Further risks associated with the loss or decline in a significant channel partner are detailed in “Our failure to establish and expand successful partnerships to sell our services and products would harm our operating results” below.

Our failure to establish and expand successful partnerships to sell our services and products would harm our operating results.

Our current business model requires us to establish and maintain relationships with third parties who market and sell our services and products. Failure to establish or maintain third-party relationships in our business, particularly with firms that sell our services and products, could materially and adversely affect the success of our business. We sell to numerous customers through each of these channel partners, and therefore a delay in the launch or rollout of our services or the reduction or discontinuance of a program with even one of these channel partners could cause us to miss revenue or other financial targets. The process of establishing a relationship with a channel partner can be complex and time consuming, and we must pass multiple levels of review in order to be selected. If we are unable to establish a sufficient number of new channel partners on a timely basis our sales will suffer.

Our Nexus platform licensing offering is in its early stages and failure to market, sell and develop the offering effectively and competitively could result in a lack of growth.

A number of competitive offerings exist in the market, providing various feature sets that may overlap with our Nexus platform today or in the future. Some competitors in this market far exceed our spending on sales and marketing activities and benefit from greater existing brand awareness, channel relationships and existing customer relationships. We may not be able to reach the market effectively and adequately or convey our differentiation as needed to grow our customer base. To reach our target market effectively, we may be required to invest substantial resources in sales and marketing activities, which could have a material adverse effect on our financial results. In addition, if we fail to develop and maintain competitive features, deliver high-quality products and satisfy existing customers, our Nexus platform license offering could fail to grow. Growth in Nexus platform license revenue also depends on scaling our multi-tenant technology platform flexibly and cost-effectively to meet changing customer demand. Disruptions in infrastructure operations as described below could impair our ability to deliver SaaS solutions to customers, thereby affecting our reputation with existing and prospective customers and possibly resulting in monetary penalties or financial losses.

Our end-user software revenues are dependent on online traffic patterns and the availability and cost of online advertising in certain key placements.

Most of our software revenue stream is obtained through advertising placements in certain key online media placements. From time to time a trend or a change in a key advertising placement will impact us, decreasing traffic or significantly increasing the cost or effectiveness of online advertising and therefore compromising our ability to purchase a desired volume and placement of advertisements at profitable rates. If such a change were to occur, as it has recently and on several occasions in the past, we may be unable to attract desired amounts of traffic, our costs for advertising may further increase beyond our forecasts and our software revenues may decrease. As a result, our operating results would be negatively impacted.

If we fail to attract, train and manage our technology specialists in a manner that meets forecast requirements and provides an adequate level of support for our customers, our reputation and financial performance could be harmed.

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Our business depends in part on our ability to attract, manage and retain our technology specialists and other support personnel. If we are unable to attract, train and manage in a cost-effective manner adequate numbers of competent technology specialists and other support personnel to be available as service volumes vary, particularly as we seek to expand the breadth and flexibility of our staffing model, our service levels could decline, which could harm our reputation, result in financial losses under contract terms, cause us to lose customers and channel partners, and otherwise adversely affect our financial performance. In the case of programs with time-based billing for services, the impact of failing to attract, train and manage such personnel could directly and adversely affect our revenue and profitability. Although our service delivery and communications infrastructure enables us to monitor and manage technology specialists remotely, because they are typically home-based and geographically dispersed we could experience difficulties meeting services levels and effectively managing the costs, performance and compliance of these technology specialists and other support personnel. Any problems we encounter in effectively attracting, managing and retaining our technology specialists and other support personnel could seriously jeopardize our service delivery operations and our financial results.

Changes in the market for computers and other consumer electronics could adversely affect our business.

Reductions in unit volumes of sales for computers and other devices we support, or in the prices of such equipment, could adversely affect our business. We offer both services that are attached to the sales of new computers and other devices, and services designed to fix existing computers and other devices. Declines in the unit volumes sold of these devices or declines in the pricing of such devices could adversely affect demand for our services or our revenue mix, either of which would harm our operating results. Further, we do not support all types of computers and devices, meaning that we must select and focus on certain operating systems and technology standards for computers, tablets, smart phones, and other devices. We may not be successful in supporting popular equipment and platforms, consumers and small businesses may trend toward use of equipment we do not support, and the process of migration away from platforms we support may decrease the market for our services and products. Any of these risks could harm our operating results.

Our failure to effectively manage third-party service providers would harm our operating results.

We enter into relationships with third parties to provide certain elements of our service offerings. We may be less able to manage the quality of services provided by third-party service providers as directly as we would our own employees. In addition, providing these services may be more costly. We also face the risk that disruptions or delays in the communications and information technology infrastructure of these third parties could cause lengthy interruptions in the availability of our services. Any of these risks could harm our operating results.

Disruptions in our information technology and service delivery infrastructure and operations, including interruptions or delays in service from third-party web hosting providers, could impair the delivery of our services and harm our business.

We depend on the continuing operation of our information technology and communication systems and those of our third-party service providers. Any damage to or failure of those systems could result in interruptions in our service, which could reduce our revenues and damage our reputation. The technology we use to serve customers and the Nexus platform we license are hosted at a third-party facility located in the United States, and we use a separate, independent third-party facility in the United States for emergency back-up and failover services in support of the hosted site. These two facilities are operated by unrelated publicly held companies specializing in operating such facilities, and we do not control the operation of these facilities. These facilities may experience unplanned outages and other technical difficulties in the future, and are vulnerable to damage or interruption from fires, floods, earthquakes, telecommunications and connectivity failures, power failures, and similar events. These facilities are also subject to risks from vandalism, break-ins, intrusion, and other malicious attacks. Despite substantial precautions taken, such as disaster recovery planning and back-up procedures, a natural disaster, act of terrorism or other



unanticipated problem could cause a loss of information and data and lengthy interruptions in the availability of our services and technology platform offerings, as our backup systems may not be able to meet our needs for an extended period of time. We rely on hosted systems maintained by third-party providers to deliver technology services and our Nexus platform to customers, including taking customer orders, handling telecommunications for customer calls, tracking sales and service delivery and making platform functionality available to customers. Any interruption or failure of our internal or external systems could prevent us or our service providers from accepting orders and delivering services, or cause company and consumer data to be unintentionally disclosed. Our continuing efforts to upgrade and enhance the security and reliability of our information technology and communications infrastructure could be very costly, and we may have to expend significant resources to remedy problems such as a security breach or service interruption. Interruptions in our services resulting from labor disputes, telephone or Internet failures, power or service outages, natural disasters or other events, or a security breach could reduce our revenue, increase our costs, cause customers and channel partners and licensees to fail to renew or to terminate their use of our offerings, and harm our reputation and our ability to attract new customers. We maintain insurance programs with highly rated carriers using policies that are designed for businesses in the technology sector and that expressly address, among other things, cyber attacks and potential harm resulting from incidents such as data privacy breaches; but depending on the type of damages, the amount, and the cause, all or part of any financial losses experienced may be excluded by the policies resulting in material financial losses for us.

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We must compete successfully in the markets in which we operate or our business will suffer.

We compete in markets that are highly competitive, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. We compete with a number of companies in the markets for technology services, end-user software products and customer experience management software. In addition, our channel partners may develop similar offerings internally.

The markets for our services and software products are still rapidly evolving, and we may not be able to compete successfully against current and potential competitors. Our ability to expand our business will depend on our ability to maintain our technological advantage, introduce timely enhanced products to meet growing support needs, deliver on-going value to our customers, scale our business cost-effectively, and develop complimentary relationships with other companies providing services or products to our partners. Competition in our markets could reduce our market share or require us to reduce the price of products and services, which could harm our business, financial condition and operating results.

The competitors in our markets for services and software can have some or all of the following comparative advantages: longer operating histories, greater economies of scale, greater financial resources, greater engineering and technical resources, greater sales and marketing resources, stronger strategic alliances and distribution channels, lower labor costs, larger user bases, products with different functions and feature sets and greater brand recognition than we have. We expect new competitors to continue to enter the markets in which we operate.

Our future service and product offerings may not achieve market acceptance.

If we fail to develop new and enhanced versions of our services and products in a timely manner or to provide services and products that achieve rapid and broad market acceptance, we may not maintain or expand our market share. We may fail to identify new service and product opportunities for our current market or new markets such as small business and technical customer experience management software. In addition, our existing services and products may become obsolete if we fail to introduce new services and products that meet new customer demands or support new standards. While we are developing new services and products, there can be no assurance that they will be timely released or ever be completed, and if they are, that they will gain market acceptance or generate material revenue for us. We have limited control over factors that affect market acceptance of our services and products, including the willingness of channel partners to offer our services and products and customer preferences for competitor services, products and delivery models.

We may make acquisitions that deplete our resources and do not prove successful.

We have made acquisitions in the past and may make additional acquisitions in the future. We may not be able to identify suitable acquisition candidates at prices we consider appropriate. If we do identify an appropriate acquisition candidate, we may not be able to successfully negotiate the terms of the acquisition. Our management may not be able to effectively implement our acquisition program and internal growth strategy simultaneously. The integration of acquisitions involves a number of risks and presents financial, managerial and operational challenges. We may have difficulty, and may incur unanticipated expenses related to, integrating management and personnel from these acquired entities with our management and personnel. Our failure to identify, consummate or integrate suitable acquisitions could adversely affect our business and results of operations. We cannot readily predict the timing, size or success of our future acquisitions. Even successful acquisitions could have the effect of reducing our cash balances. Acquisitions could involve a number of other potential risks to our business, including the following, any of which could harm our business results:

Unanticipated costs and liabilities and unforeseen accounting charges or fluctuations;  
Delays and difficulties in delivery of services and products;

Failure to effectively integrate or separate management information systems, personnel, research and development, marketing, sales and support operations;  
Loss of key employees;  
Economic dilution to gross and operating profit;  
Diversion of management's attention from other business concerns and disruption of our ongoing business;  
Difficulty in maintaining controls and procedures;  
Uncertainty on the part of our existing customers about our ability to operate after a transaction;

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Loss of customers;

Loss of partnerships;

Inability to execute our growth plans;

Declines in revenue and increases in losses;

Failure to realize the potential financial or strategic benefits of the acquisition or divestiture; and

Failure to successfully further develop the combined or remaining technology, resulting in the impairment of amounts recorded as goodwill or other intangible assets.

Our systems collect, access, use, and store personal customer information and enable customer transactions, which poses security risks, requires us to invest significant resources to prevent or correct problems caused by security breaches, and may harm our business.

A fundamental requirement for online communications, transactions and support is the secure collection, storage and transmission of confidential information. Our systems collect and store confidential and personal information of our individual customers as well as our channel partners and their customers' users, including credit card information, and our employees and contractors may access and use that information in the course of providing services. In addition, we collect and retain personal information of our employees in the ordinary course of our business. We and our third-party contractors use commercially available technologies to secure this information. Despite these measures, parties may attempt to breach the security of our data or that of our customers. In addition, errors in the storage or transmission of data could breach the security of that information. We may be liable to our customers for any breach in security and any breach could subject us to governmental or administrative proceedings or monetary penalties, damage our relationships with channel partners and harm our business and reputation. Also, computers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We may be required to expend significant capital and other resources to comply with mandatory privacy and security standards required by law, industry standard, or contract, and to further protect against security breaches or to correct problems caused by any security breach.

We are exposed to risks associated with credit card and payment fraud and with credit card processing.

Certain of our customers use credit cards to pay for our services and products. We may suffer losses as a result of orders placed with fraudulent credit cards or other payment data. Our failure to detect or control payment fraud could have an adverse effect on our results of operations. We are also subject to payment card association operating standards and requirements, as in effect from time to time. Compliance with those standards requires us to invest in network and systems infrastructure and processes. Failure to comply with these rules or requirements may subject us to fines, potential contractual liabilities, and other costs, resulting in harm to our business and results of operations.

Privacy concerns and laws or other domestic or foreign regulations may require us to incur significant costs and may reduce the effectiveness of our solutions, and our failure to comply with those laws or regulations may harm our business and cause us to lose customers.

Our software contains features that allow our technology specialists and other personnel to access, control, monitor and collect information from computers running our software. Federal, state and foreign government bodies and agencies, however, have adopted or are considering adopting laws and regulations restricting or otherwise regulating the collection, use and disclosure of personal information obtained from consumers and individuals. Those regulations could require costly compliance measures, could reduce the efficiency of our operations, or could require us to modify or cease to provide our systems or services. Liability for violation of, costs of compliance with, and other burdens imposed by such laws and regulations may limit the use and adoption of our services and reduce overall demand for them. Even the perception of privacy concerns, whether or not valid, may harm our reputation and inhibit adoption of our solutions by current and future customers. In addition, we may face claims about invasion of privacy or inappropriate disclosure, use, storage, or loss of information obtained from our customers. Any imposition of liability

could harm our reputation, cause us to lose customers and cause our operating results to suffer.

We rely on third-party technologies in providing certain of our services and software. Our inability to use, retain or integrate third-party technologies and relationships could delay service or software development and could harm our business.

We license technologies from third parties, which are integrated into our services, technology platform and end user software. Our use of commercial technologies licensed on a non-exclusive basis from third parties poses certain risks. Some of the third-party technologies we license may be provided under “open source” licenses, which may have terms that require us to make generally available our modifications or derivative works based on such open source code. Our inability to obtain or integrate third-party technologies with our own technology could delay service development until equivalent compatible technology can be identified, licensed and integrated. These third-party technologies may not continue to be available to us on commercially reasonable terms or at all. If our relationship with third parties were to deteriorate, or if such third parties were unable to develop innovative and saleable products, we could be forced to identify a new developer and our future revenue could suffer. We may fail to successfully integrate any licensed technology into our services or software, or maintain it through our own development work, which would harm our business and operating results. Third-party licenses also expose us to increased risks that include:

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Risks of product malfunction after new technology is integrated;  
Risks that we may be unable to obtain or continue to obtain support, maintenance and updates from the technology supplier;  
The diversion of resources from the development of our own proprietary technology; and  
Our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs.

We rely on intellectual property laws to protect our proprietary rights, and if these rights are not sufficiently protected or we are not able to obtain sufficient protection for our technology, it could harm our ability to compete and to generate revenue.

We rely on a combination of laws, such as those applicable to patents, copyrights, trademarks and trade secrets, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our proprietary rights. Our ability to compete and grow our business could suffer if these rights are not adequately protected. Our proprietary rights may not be adequately protected because:

Laws and contractual restrictions may not adequately prevent infringement of our proprietary rights and misappropriation of our technologies or deter others from developing similar technologies; and  
Policing infringement of our patents, trademarks and copyrights, misappropriation of our trade secrets, and unauthorized use of our products is difficult, expensive and time-consuming, and we may be unable to determine the existence or extent of this infringement or unauthorized use.

Intellectual property litigation is expensive and time-consuming and could divert management's attention from our business. The outcome of any litigation is uncertain and could significantly impact our financial results. Also, the laws of other countries in which we market our products may offer little or no protection of our proprietary technologies. Reverse engineering, unauthorized copying or other misappropriation of our proprietary technologies could enable third parties to benefit from our technologies without paying us for them, which would harm our competitive position and market share.

Our success and ability to compete depend to a significant degree on the protection of our solutions and other proprietary technology. It is possible that:

We may not be issued patents we may seek to protect our technology;  
Competitors may independently develop similar technologies or design around any of our patents;  
Patents issued to us may not be broad enough to protect our proprietary rights; and  
Our issued patents could be successfully challenged.

We may face intellectual property infringement claims that could be costly to defend and result in our loss of significant rights.

Our business relies on the use and licensing of technology. Other parties may assert intellectual property infringement claims against us or our customers, and our products may infringe the intellectual property rights of third parties. For example, our products may infringe patents issued to third parties. In addition, as is increasingly common in the technology sector, we may be confronted with the aggressive enforcement of patents by companies whose primary business activity is to acquire patents for the purpose of offensively asserting them against other companies. From time to time, we have received allegations of intellectual property infringement, and we may receive more claims in the future. We may also be required to pursue litigation to protect our intellectual property rights or defend against allegations of infringement. Intellectual property litigation is expensive and time-consuming and could divert management's attention from our business. The outcome of any litigation is uncertain and could significantly impact our financial results. If there is a successful claim of infringement, we may be required to develop non-infringing

technology or enter into royalty or license agreements, which may not be available on acceptable terms, if at all. Our failure to develop non-infringing technologies or license proprietary rights on a timely basis would harm our business.

We may face consumer class actions and similar claims that could be costly to defend or settle and result in negative publicity and diversion of management resources.

Our business involves direct sale and licensing of services and software to consumers and small businesses, and we typically include customary indemnification provisions in favor of our distribution partners in our partner agreements for the distribution of our services and software. As a result we can be subject to consumer litigation and legal proceedings related to our services and software, including putative class action claims and similar legal actions. Such litigation can be expensive and time-consuming regardless of the merits of any action, and could divert management's attention from our business. The cost of defense can be large as can any settlement or judgment in an action. The outcome of any litigation is uncertain and could significantly impact our financial results. Regardless of outcome, litigation can have an adverse impact on us because of defense costs, negative publicity, diversion of management resources and other factors.

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We have recorded long-lived assets, and our results of operations would be adversely affected if their value becomes impaired.

Goodwill and identifiable intangible assets were recorded in part due to our acquisition of substantially all of the assets and liabilities of YourTechOnline.com (“YTO”) in May 2008, our acquisition of substantially all of the assets of Xeriton Corporation in December 2009, our acquisition of certain assets and assumed liabilities of SUPERAntiSpyware (“SAS”) in June 2011 and our acquisition of certain assets and assumed liabilities of RightHand IT Corporation (“RHIT”) in January 2012. We also have certain intangible assets with indefinite lives. We assess the impairment of goodwill and indefinite lived intangible assets annually or more often if events or changes in circumstances indicate that the carrying value may not be recoverable. We assess the impairment of acquired product rights and other finite lived intangible assets whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. Our results of operations would be adversely affected if impairment of our goodwill or intangible assets occurred.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 6. EXHIBITS

Exhibits.

10.1 Employment Offer Letter between Roop Lakkaraju and Company dated October 22, 2013 (incorporated by reference to Exhibit 10.1 of Company’s current report on Form 8-K filed on October 30, 2013)

10.2 Program Description Number 3 to the Amended and Restated Support Services Agreement between Comcast and Company signed September 26, 2013 and effective as of June 24, 2013 (1)

31.1 Chief Executive Officer Section 302 Certification

31.2 Chief Financial Officer Section 302 Certification

32.1 Statement of the Chief Executive Officer under 18 U.S.C. § 1350 (2)

32.2 Statement of the Chief Financial Officer under 18 U.S.C. § 1350 (2)

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(1) Confidential treatment has been requested for portions of this exhibit.

The certifications filed as Exhibits 32.1 and 32.2 are not deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the Company under the Securities Exchange Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof irrespective of any general incorporation by reference language contained in any such filing, except to the extent that the registrant specifically incorporates it by reference.



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SIGNATURES

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

November 4, 2013 SUPPORT.COM, INC.

By: /s/ IDO SAKAL  
Ido Sakal  
Interim Chief Financial Officer and  
Principal Accounting Officer

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EXHIBIT INDEX TO SUPPORT.COM, INC.  
QUARTERLY REPORT ON FORM 10-Q  
FOR THE QUARTER ENDED SEPTEMBER 30, 2013

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