Mattersight Corp
Form 10-K
March 12, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2014

or

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

Commission file number 0-27975

Mattersight Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**36-4304577**
(State or other Jurisdiction of Incorporation or Organization)	***(I.R.S. Employer Identification No.)***

200 S. Wacker Drive, Suite 820

Chicago, Illinois 60606

(Address of Registrant s Principal Executive Offices) (Zip Code)

Registrant s telephone number, including area code: (877) 235-6925

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.01 per share	**NASDAQ Global Market**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Annual Report on Form 10-K or any amendment to this Annual Report on Form 10-K. ¨

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

Large accelerated filer ¨	Accelerated filer ¨	Non-accelerated filer ¨	Smaller reporting company x
		(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 Act). Yes ¨ No x

The aggregate market value of Common Stock held by non-affiliates of the registrant, based upon the closing price per share of registrant s Common Stock on June 30, 2014, as reported by The NASDAQ Stock Market LLC, is approximately $57,496,043.

The number of shares of the registrant s Common Stock outstanding as of March 4, 2015 was 22,748,300.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Mattersight s Proxy Statement for its 2015 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days after the end of Mattersight s fiscal year, are incorporated herein by reference into Part III where indicated; provided, that if such Proxy Statement is not filed with the Securities and Exchange Commission within 120 days after the fiscal year end covered by this Annual Report on Form 10-K, an amendment to this Annual Report on Form 10-K shall be filed no later than the end of such 120-day period.

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PART I

Item 1. *Business.*

Overview

Mattersight Corporation (together with its subsidiaries and predecessors, Mattersight, we, us, or the Company) is a leader in enterprise analyti focused on customer and employee interactions and behaviors. Through its Behavioral Analytics-related services, including Predictive Behavioral Routing, Performance Management, and Predictive Analytics (collectively, Behavioral Analytics), Mattersight captures and analyzes customer and employee interactions, employee desktop data, and other contextual information to optimally route customers to the best available employee, improve operational performance, and predict future customer and employee outcomes. Mattersight s analytics are based on millions of proprietary algorithms and the application of unique behavioral models. The Company s SaaS delivery model combines analytics in the cloud with deep customer partnerships to drive significant business value. Mattersight s solutions are used by leading companies in the healthcare, insurance, financial services, telecommunications, cable, utilities, education, hospitality, and government industries.

Through the performance of Behavioral Analytics, the Company generates two types of revenue:

(1) Managed services revenue, which is recurring, annuity revenue from long-term (generally three- to five-year) contracts and pilots, which are shorter-term (generally three to twelve months), and includes subscription and amortized deployment revenue; and

(2) Consulting services revenue, which is generally project-based and sold on a time-and-materials or fixed-fee basis and includes follow-on consulting services revenue.

The Company s multi-channel technology captures the unstructured data of voice interactions (conversations), related customer and employee data, and employee desktop activity, and applies millions of proprietary algorithms against those interactions. Each interaction contains hundreds of attributes that get scored and ultimately detect patterns of behavior or business process that provide the transparency and predictability necessary to enhance revenue, improve the customer experience, improve efficiency, and predict and navigate outcomes. Adaptive across industries, programs, and industry-specific processes, the Company s Behavioral Analytics offerings enable its clients to drive measurable economic benefit through the improvement of contact center performance, customer satisfaction and retention, fraud reduction, and streamlined back office operations. Specifically, through its Behavioral Analytics offerings, Mattersight helps its clients:

- Identify optimal customer/employee behavioral pairing for call routing;
- Identify and understand customer personality;
- Automatically measure customer satisfaction and agent performance on every analyzed call;
- Improve rapport between agent and customer;
- Reduce call handle times while improving customer satisfaction;
- Identify opportunities to improve self-service applications;

- Improve cross-sell and up-sell success rates;
- Improve the efficiency and effectiveness of collection efforts;
- Measure and improve supervisor effectiveness and coaching;
- Improve agent effectiveness by analyzing key attributes of desktop usage;
- Predict likelihood of customer attrition;
- Predict customer satisfaction and Net Promoter Scores® without customer surveys;
- Predict likelihood of debt repayment;
- Predict likelihood of a sale or cross-sell; and
- Identify fraud callers and improve authentication processes.

The Company has designed a highly-scalable, flexible, and adaptive application platform to enable the Company to implement and operate its Behavioral Analytics offerings for its clients. These offerings are primarily delivered through a SaaS model, as a managed subscription service from which Mattersight derives Managed services revenue and Consulting services revenue. Managed services revenue consists of revenue from deployment and subscription services and Consulting services revenue consists of revenue from post-deployment follow-on services, including coaching, training, and custom data analysis.

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In addition to our Behavioral Analytics offerings, Mattersight also generates revenue from the following services:

(1) Marketing Managed Services, which consist of marketing application hosting services, from which the Company derives Managed services revenue; and

(2) CRM Services, which consist of operational consulting services that enhance business performance through improved process efficiencies and redesign of workflows, from which the Company derives Consulting services revenue.

Types of Revenue

Managed Services Revenue

Managed services revenue is primarily driven by the execution of new Behavioral Analytics contracts, under which we deploy and provide our proprietary Behavioral Analytics offerings on a subscription basis. Based on each client s business requirements, the client s selection of our Behavioral Analytics offerings are configured and integrated into the client s environment and then deployed in either a remote-hosted or an on-premise hosted environment. Thereafter, the Behavioral Analytics offerings are provided, on a subscription basis, for a period that is generally three to five years after the go-live date or, in the cases where the Company contracts with a client for a short-term pilot of a Behavioral Analytics offering prior to committing to a longer subscription period, if any, the subscription or pilot periods generally range from three to twelve months after the go-live date. The fees and costs related to the initial deployment are deferred and amortized over the subscription period.

We also generate Managed services revenue from Marketing Managed Services, specifically, from hosted customer and campaign data management. This source of Managed services revenue will continue to diminish over time as we focus on growth through Behavioral Analytics, including predictive behavioral routing.

Consulting Services Revenue

In addition to the Consulting services revenue generated by our Behavioral Analytics contracts, we derive a portion of this type of revenue from CRM Services for long-standing accounts. We expect Consulting services revenue from CRM Services to continue to diminish over time as demand for these services continues to decline and we focus on growth through Behavioral Analytics. We bill for Consulting services on a time-and-materials or fixed-fee basis.

Business Segments

The Company operates in a single business segment, focused primarily on Behavioral Analytics. Financial information concerning our business segment is included in Financial Statements and Supplementary Data Part II, Item 8 of this Annual Report on Form 10-K.

International Operations

The Company s services are delivered to clients in the U.S. and the United Kingdom. The Company s revenue is and has been recognized in the U.S. subsidiary. The Company s long-lived assets are and have been predominately located in the U.S. and consist of equipment, software, furniture and fixtures, and leasehold improvements (net of accumulated depreciation and amortization).

Methods of Distribution

Our Managed services revenue and Consulting services revenue are generated by direct contractual relationships with our clients.

Intellectual Property Rights

General

Our ability to protect our software, methodologies, and other intellectual property is important to our success and our competitive position. We view as proprietary the software (including source code), algorithms, analyses, and other ideas, concepts, and developments that we create in order to provide, improve, and enhance our service offerings, as well as the work product we create in the course of providing services for clients. We seek to protect our intellectual property rights in these developments and work product by relying on a combination of patent, copyright, trademark, and trade secret law, and confidentiality and non-disclosure agreements with our employees and third parties.

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Patents

As of December 31, 2014, we hold thirteen U.S. patents and one European patent and have applied for over twenty additional patents. These patents cover a broad range of our analytics capabilities, including methods for analyzing language to assess customer personality and analyzing data to improve employee performance. We regularly review new areas of development in order to assess patentability.

Trademarks

We have obtained U.S. federal trademark registration for the MATTERSIGHT word mark and the MATTERSIGHT eye logo, which incorporates our tagline See What Matters . We believe that the registration of the MATTERSIGHT word mark and logo mark in the U.S. is material to our operations.

Licenses

A majority of our clients require that we grant to them licenses in and to the intellectual property rights associated with the work product we create in the course of providing services. In some cases, our clients require assignment of ownership in the intellectual property rights to such work product, typically where such work product incorporates their confidential information or would provide them some competitive advantage in their industry. Absent an agreement to the contrary, each assignment of ownership in intellectual property rights would result in our inability to reuse the relevant work product with other clients. As a result, it is our practice to retain the rights in the underlying core intellectual property on which such work product is based, including methodologies, workplans, and software, as well as residual know-how. Further, it is our policy to obtain from our clients a license to permit us to sell service offerings using such work product to other clients. These arrangements may be nonexclusive or exclusive, and licensors to us may retain the right to sell products and services that compete with those of the Company.

Seasonality

Seasonal impact to our revenue and earnings is limited, as a significant portion of our revenue is earned through our Behavioral Analytics subscription services, which is a recurring annuity revenue stream that is not impacted by holidays and vacations.

Clients

During fiscal year 2014, our five and ten largest clients accounted for 75% and 91% of our total revenue, respectively. During fiscal year 2013, our five and ten largest clients accounted for 69% and 90% of our total revenue, respectively. In fiscal year 2012, our five and ten largest clients accounted for 66% and 89% of our total revenue, respectively. In fiscal year 2014, there were three clients that accounted for 10% or more of total revenue: United HealthCare Services, Inc.; Progressive Casualty Insurance Company; and Health Care Service Corporation; which accounted for 25%, 20%, and 11% of total revenue, respectively. In fiscal year 2013, there were four clients that accounted for 10% or more of total revenue: Vangent, Inc.; Progressive Casualty Insurance Company; Allstate Insurance Company; and United HealthCare Services, Inc., which accounted for 21%, 15%, 13%, and 11% of total revenue, respectively. In fiscal year 2012, there were three clients that accounted for 10% or more of total revenue: Vangent, Inc.; Allstate Insurance Company; and Progressive Casualty Insurance Company; which accounted for 19%, 16%, and 13% of total revenue, respectively. For fiscal years 2014, 2013, and 2012, seven, nine, and eight clients, respectively, each accounted for over $1 million of total revenue. See Note Two Summary of Significant Accounting Policies of the Notes to Consolidated Financial Statements included in Part II Item 8 of this Annual Report on Form 10-K.

Competition

Although we view the manner in which we provide Behavioral Analytics, and its benefits, to be unique, we nonetheless operate in a highly competitive and rapidly changing market and compete with a variety of organizations that offer services that may be viewed as similar to ours. These competitive organizations include data analytics solutions providers, voice recording and voice analytic services providers and software licensors, call routing solution providers, and strategic consulting firms. In our opinion, few competitors offer the full range and depth of services that we can provide, but they may compete with us on individual factors such as expertise, price, or capacity.

Many of our competitors have longer operating histories, more clients, longer relationships with their clients, greater brand or name recognition, and significantly greater financial, technical, marketing, and public relations resources than we do. As a result, our competitors may be in a better position to respond quickly to new or emerging technologies and changes in client requirements. They may also develop and promote their products and services more effectively than we do. New market entrants also pose a threat to our business. Existing or future competitors may develop or offer solutions that are comparable or superior to ours at a lower price.

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Environmental Issues

There are no known material compliance issues with any Federal, state, or local environmental regulations.

Employees

As of December 31, 2014, we employed 197 persons, none of whom is represented by a union. We consider our employee relations to be good.

Available Information and Other

Our principal internet address is www.Mattersight.com. Our Annual, Quarterly, and Current Reports on Forms 10-K, 10-Q, and 8-K, and any amendments thereto, as well as the Forms 3, 4, and 5 beneficial ownership reports filed with respect to our stock, are made available free of charge on our website as soon as reasonably practicable after the reports have been filed with, or furnished to, the Securities and Exchange Commission (SEC). However, the information found on our website is not part of this or any other report filed by us with the SEC. These reports may also be obtained at the SEC s public reference room at 100 F Street, N.E., Washington, D.C. 20549. Information regarding the operation of the SEC s public reference room may be obtained by calling the SEC at (800) SEC-0330. The SEC also maintains a website at www.sec.gov that contains reports, proxy statements, and other information regarding SEC registrants, including Mattersight.

Mattersight was incorporated in Delaware in May 1999. Our executive office is currently located at 200 S. Wacker Drive, Suite 820, Chicago, Illinois 60606 and our main telephone number is (877) 235-6925.

Item 1A. ***Risk Factors***

There are a number of risks and uncertainties that could adversely affect our business and our overall financial performance. In addition to the matters discussed elsewhere in this Annual Report on Form 10-K, we believe the more significant of such risks and uncertainties include the following:

We have not realized an operating profit in fifteen years and there is no guarantee that we will realize an operating profit in the foreseeable future.

As of December 31, 2014, we had an accumulated deficit of $226.4 million. We expect to continue to use cash and incur operating expenses to support our growth, including costs associated with recruiting, training, and managing our sales force, costs to develop and acquire new technology, and promotional costs associated with reaching new clients. These investments, which typically are made in advance of revenue, may not yield an offsetting increase in revenue. As a result of these factors, our future revenue and income potential is uncertain.

Our financial results are subject to significant fluctuations because of many factors, any of which could adversely affect our stock price.

It is possible that in some future periods our operating results may be below the expectations of public market analysts and investors. In this event, the price of our publicly-traded securities may fall. Our revenue and operating results may vary significantly due to a number of factors, many of which are not in our control. We may incur an impairment of goodwill if our financial results are adversely impacted by these factors and we continue to incur financial losses or our stock price declines. These factors include:

- Our ability to continue to grow our revenue and meet anticipated growth targets;
- Our ability to maintain our current relationships, and develop new relationships, with clients, service providers, and business partners;
- Unanticipated cancellations or deferrals of, or reductions in the scope of, major Behavioral Analytics contracts;

- The length of the sales cycle associated with our solutions;

- Our ability to successfully introduce new, and upgrade our existing, service offerings for clients; and

- Our ability to respond effectively to competition.

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

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We depend on a limited number of clients for a significant portion of our revenue, and the loss of a significant client or a substantial decline in the size or scope of deployments for a significant client, could have a material adverse effect on our business.

We derive, and expect to continue to derive for the foreseeable future, a significant portion of our total revenue from a limited number of clients. See Clients in Part I Item 1 and Year Ended December 31, 2014 Compared with the Year Ended December 31, 2013 included in Management s Discussion and Analysis of Financial Condition and Results of Operations in Part II Item 7 of this Annual Report on Form 10-K. To the extent that any significant client uses less of our services or terminates its relationship with us, as may occur as clients respond to conditions affecting their own businesses, our total revenue could decline substantially and that could significantly harm our business. In addition, because a high percentage of our revenue is dependent on a relatively small number of clients, delayed payments by a few of our larger clients could result in a reduction of our available cash, which in turn may cause fluctuation in our Days Sales Outstanding (DSO).

We depend on good relations with our major clients, and any harm to these good relations may materially and adversely affect our business and our ability to compete effectively.

To attract and retain clients, we depend to a large extent on our relationships with our clients and our reputation for high quality analytics and related services. If a client is not satisfied with our services, it may be damaging to our reputation and business. Any defects or errors in our services or solutions or failure to meet our clients expectations could result in:

- Delayed or lost revenue;
- Obligations to provide additional services to a client at a reduced fee or at no charge;
- Negative publicity, which could damage our reputation and adversely affect our ability to attract or retain clients; and
- Claims for damages against us, regardless of our responsibility for such failure.

If we fail to meet our contractual obligations with our clients, then we could be subject to legal liability or loss of clients. Although our contracts include provisions to limit our exposure to legal claims related to the services and solutions we provide, these provisions may not protect us, or protect us sufficiently, in all cases.

We must maintain our reputation and expand our name recognition to remain competitive.

We believe that establishing and maintaining a good reputation and brand name is critical for attracting and expanding our targeted client base. This is particularly the case given that we relaunched our business under a new brand name in June 2011. We continue to invest substantially in marketing in order to make our new name known in the marketplace for our services and solutions. If potential clients do not know what solutions we provide, or if our reputation is damaged, then we may become less competitive or lose our market share. Promotion and enhancement of our name and brand will depend largely on both the efficacy of our relatively nascent marketing efforts and our success in providing high quality services, software, and solutions, neither of which can be assured.

Our clients use our solutions for critical applications. If clients do not perceive our solutions to be effective or of higher quality than those available from our competitors, or if our solutions result in errors, defects, or other performance problems, then our brand name and reputation could be materially and adversely affected.

Our industry is very competitive and, if we fail to compete successfully, our market share and business will be adversely affected.

Although we view the manner in which we provide Behavioral Analytics, and its benefits, to be unique, nonetheless we operate in a highly competitive and rapidly changing market and compete with a variety of organizations that offer services that may be viewed as similar to ours. These competitive organizations include data analytics solutions providers, voice recording and voice analytic service providers and software licensors, call routing solution providers, and strategic consulting firms. We compete with these organizations on factors such as expertise, price, and capacity.

Many of our competitors have longer operating histories, more clients, longer relationships with their clients, greater brand or name recognition, more registered patents, and significantly greater financial, technical, marketing, and public relations resources than we do. As a result, our competitors may be in a better position to respond quickly to new or emerging technologies and changes in client requirements. They may also develop and promote their products and services more effectively than we do. New market entrants also pose a threat to our business. Existing or future competitors may develop or offer solutions that are comparable or superior to ours at a lower price.

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We must keep pace with the rapid rate of innovation in our industry in order to build our business.

The data analytics market, and particularly behavioral analytics, is relatively new and rapidly evolving. Our future business depends in part upon continued growth in the acceptance and use of Behavioral Analytics by our current and prospective clients. Their acceptance and usage in turn may depend upon factors such as: the actual or perceived benefits of adoption of Behavioral Analytics and related methodologies and technologies, including the predictability of a meaningful return on investment, cost efficiencies, or other measurable economic benefits; the actual or perceived reliability, scalability, ease of use, and access to such new technologies and methodologies; and the willingness to adopt new business methods. Furthermore, our future growth depends on our continuing ability to innovate in the field of data analytics and to incorporate emerging industry standards.

We cannot assure that we will be successful in anticipating or responding to these challenges on a timely or competitive basis or at all, or that our ideas and solutions will be successful in the marketplace. In addition, new or disruptive technologies and methodologies by our competitors may make our service or solution offerings uncompetitive. Any of these circumstances could significantly harm our business and financial results.

Because our services and solutions are sophisticated, we must devote significant time and effort to our sales and installation processes, with significant risk of loss if we are not successful.

Because our services and solutions are not simple, mass-market items with which our potential clients are already familiar, it is necessary for us to devote significant time and effort to the process of educating our potential clients about the benefits and value of our services and solutions as part of the sales process. In addition, because our services and solutions are sophisticated and in most cases are not readily usable by clients without our assistance in integration and configuration, training, and analysis, we must devote significant time during the installation and ongoing analysis process in order for our services and solutions to be successfully deployed. These efforts during both the sales and installation processes increase the time and difficulty of completing transactions, make it more difficult to efficiently deploy our limited resources, and create risk that we will have invested in an opportunity that ultimately does not come to fruition. If we are unable to demonstrate the benefits and value of our services and solutions to clients and efficiently convert our sales leads into successful sales and installations, our results of operations may be adversely affected.

The unauthorized disclosure of the confidential customer data that we maintain could result in a significant loss of business and subject us to substantial liability.

In providing Behavioral Analytics, we record and analyze telephone calls and other interactions between our clients call center and back office agents and their customers. These interactions may contain numerous references to highly sensitive confidential or personally-identifiable data of the customers of our clients, and many of our clients are required to comply with Federal and state laws concerning privacy and security, such as the Health Insurance Portability and Accountability Act of 1996 and the Gramm-Leach-Bliley Act of 1999. In addition, we have made certain contractual commitments to our clients regarding this confidential data.

Particularly with regard to clients in highly-regulated industries such as healthcare and financial services, many of our clients demand that we agree not to limit our liability in the event of a security breach resulting in the loss of, or unauthorized access to, personally-identifiable data. As a result, the disclosure or loss of such data despite the extensive precautions we undertake could result in the considerable diminution of our business and prospects and could subject us to substantial liability.

In addition, the laws, regulations, and industry standards governing these matters are changing rapidly. It is possible that the resources we devote to comply with such laws, regulations, and industry standards, and our clients particular requirements, could increase materially. In our contracts, we generally agree to indemnify our clients for expenses and liabilities resulting from unauthorized access to or disclosure of confidential data. These indemnity obligations are generally not subject to contractual limitations on liability. As a result, the amount of liability we could incur in connection with these indemnity obligations could exceed the revenue we receive from the client under the applicable contract.

Our financial results could be adversely affected by economic and political conditions and the effects of these conditions on our clients businesses and levels of business activity.

Economic and political conditions in the U.S. affect our clients businesses and the markets they serve. A severe and/or prolonged economic downturn or a negative or uncertain political climate could adversely affect our clients financial conditions and the levels of business activity of our clients and the industries we serve. This may reduce demand for our services or depress pricing of those services and have a material adverse effect on our results of operations. Changes in U.S. economic conditions could also shift demand to services for which we do not have competitive advantages, and this could negatively affect the amount of business that we are able to obtain. In addition, these economic conditions may cause our clients to delay payments for services we have provided to them, resulting in a negative impact to our cash flow. If we are unable to successfully anticipate changing economic and political conditions, then we may be unable to effectively plan for and respond to those changes, and our business could be negatively affected.

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We rely heavily on our senior management team for the success of our business.

Given the highly specialized nature of our services, senior management must have a thorough understanding of our service offerings as well as the skills and experience necessary to manage the organization. If one or more members of our senior management team leaves and we cannot replace them with a suitable candidate quickly, then we could experience difficulty in managing our business properly, and this could harm our business prospects, client relationships, employee morale, and results of operations. We recently announced that our Vice President and Chief Financial Officer, Mark Iserloth, is resigning effective March 13, 2015. While his responsibilities are being assumed by our Executive Vice President of Product and Customer Operations, this change could be disruptive to our operations.

Our ability to recruit talented professionals and retain our existing professionals is critical to the success of our business.

We believe that our success depends substantially on our ability to attract, train, motivate, and retain highly skilled management, strategic, technical, product development, data analysis, and other key professional employees. Our business straddles the information-technology and data analytics services industries, which are people-intensive and face shortages of qualified personnel, especially those with specialized skills or experience. We compete with other companies to recruit and hire from this limited pool, particularly in Austin, Texas, the location of our research and development team and in Chicago, Illinois, the location of our data science and analytics teams.

If we cannot hire and retain qualified personnel, or if a significant number of our current employees should leave, and we have difficulty replacing such persons, then we could potentially suffer the loss of client relationships or new business opportunities and our business could be seriously harmed. In addition, there is no guarantee that the employee and client non-solicitation and non-competition agreements we have entered into with our senior professionals would deter them from departing us for our competitors or that such agreements would be upheld and enforced by a court or other arbiter across all jurisdictions where we engage in business.

We have a limited ability to protect our intellectual property rights, which are important to our success and competitive position.

Our ability to protect our software, algorithms, databases, methodologies, and other intellectual property is important to our success and our competitive position. We view as proprietary the software (including source code), algorithms, databases, analysis, and other ideas, concepts, and developments that we create in order to provide, improve, and enhance our service offerings, as well as the work product we create in the course of providing services for clients. We seek to protect our intellectual property rights in these developments and work product by applying for patents, copyrights, and trademarks, as appropriate, as well as by enforcing applicable trade secret laws and contractual restrictions on scope of use, disclosure, copying, reverse engineering, and assignment.

Despite our efforts to protect our intellectual property rights from unauthorized use or disclosure, others may attempt to disclose, obtain, or use our rights. The steps we take may not be adequate to prevent or deter infringement or other misappropriation of our intellectual property rights. In addition, we may not detect unauthorized use of, or take timely and effective actions to enforce and protect, our intellectual property rights.

We may be required to obtain licenses from others to refine, develop, market, and deliver current and new services and solutions. There can be no assurance that we will be able to obtain any of these licenses on commercially reasonable terms or at all, or that rights granted by these licenses ultimately will be valid and enforceable.

Others could claim that our services, products, or solutions infringe upon their intellectual property rights or violate contractual protections.

We or our clients may be subject to claims that our services, products, or solutions, or the products of our software providers or other alliance partners, infringe upon the intellectual property rights of others. Any such infringement claims may result in substantial costs, divert management attention and other resources, harm our reputation, and prevent us from offering some services, products, or solutions. A successful infringement claim against us could materially and adversely affect our business.

In our contracts, we agree to indemnify our clients for expenses and liabilities resulting from claimed infringement by our services, products, or solutions, in most cases excluding third-party components, of the intellectual property rights of others. In some instances, the amount of these indemnity obligations may be greater than the revenue we receive from the client under the applicable contract. In addition, we may develop work product in connection with specific projects for our clients. Although our contracts with our clients generally provide that we retain the ownership rights to our work product, it is possible that clients may assert rights to, and seek to limit our ability to resell or reuse, our work product. Furthermore, in some cases we assign to clients the copyright and, at times, other intellectual property rights, in and to some aspects of the software, documentation, or other work product developed for these clients in connection with these projects, which limits our ability to resell or reuse this intellectual property.

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Increasing government regulation could cause us to lose clients or impair our business.

We are subject not only to laws and regulations applicable to businesses generally, but we are also subject to certain U.S. and foreign laws and regulations applicable to our service offerings, including, but not limited to, those related to data privacy and security, electronic commerce, and call recording. Laws and regulations enacted in the U.S., both at the state and Federal level, as well as significant new rules issued with respect thereto, impose substantial requirements relating to the privacy and security of personal data, as well as the reporting of breaches with respect to personal data. Legislation that may be enacted in the future may add further requirements in these and other areas. In addition, we may be affected indirectly by legislation that impacts our existing and prospective clients, who may pass along to us by contract their legal obligations in these and other areas. Any such laws and regulations therefore could affect our existing business relationships or prevent us from obtaining new clients.

It may be difficult for us to access debt or equity markets to meet our financial needs.

In the event, for any reason, we need to raise additional funds in the future, through public or private debt or equity financings, such funds may not be available or may not be available on terms favorable to us. The failure by us to obtain such financing, if needed, may have a material adverse effect upon our business, financial condition and results of operations.

Item 1B. ***Unresolved Staff Comments.***

Not applicable.

Item 2. ***Properties.***

Our principal physical properties employed in our business consist of our leased office facilities in Chicago, Illinois; Edina, Minnesota; and Austin, Texas. Our executive offices are located at 200 South Wacker Drive, Suite 820, Chicago, Illinois 60606.

Our total employable space is approximately 44,000 square feet. We do not own any real estate. We believe that our leased facilities are appropriate for our current business requirements; however, we are currently exploring opportunities to expand our space to accommodate the future growth of our Chicago operations.

Item 3. ***Legal Proceedings.***

From time to time, the Company has been subject to legal claims arising in connection with its business and the results of these claims, when they arise, cannot be predicted with certainty. There are no asserted claims against the Company that, in the opinion of management, if adversely decided, would have a material effect on the Company s financial position, results of operations, or cash flows.

Item 4. ***Mine Safety Disclosures***

Not applicable.

PART II.

Item 5. ***Market for Registrant s Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities.***

Our common stock, par value $0.01 per share (Common Stock), is traded on the NASDAQ Global Market under the symbol MATR. The following table sets forth, for the periods indicated, the quarterly high and low sales prices of our Common Stock on the NASDAQ Global Market.

	High	Low
Fiscal Year 2014		
Fourth Quarter	$ 6.62	$ 5.01
Third Quarter	6.25	4.41
Second Quarter	7.21	4.66
First Quarter	7.85	4.75
Fiscal Year 2013		
Fourth Quarter	$ 5.21	$ 3.74
Third Quarter	4.60	2.65
Second Quarter	5.25	2.76
First Quarter	5.19	3.71

There were approximately 120 owners of record of Common Stock as of March 4, 2015. The last reported sale price of the Common Stock on the NASDAQ Global Market on March 4, 2015 was $6.85.

See Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters included in Part III Item 12 of this Annual Report on Form 10-K for more information about securities authorized for issuance under our various compensation plans.

Sale of Unregistered Securities

On May 20, 2014, Silicon Valley Bank elected to fully exercise a warrant by exchanging 75,698 warrant shares through a cashless exercise on the terms provided in the applicable warrant agreement. As a result, the Company issued 47,404 shares of Common Stock to Silicon Valley Bank, in full settlement of the warrant.

On June 4, 2014, PfG elected to partially exercise a warrant by exchanging 57,196 of its 129,032 warrant shares through a cashless exercise on the terms provided in the applicable warrant agreement. As a result, the Company issued 35,862 shares of Common Stock to PfG on June 4, 2014.

On June 4, 2014, PfG Equity Investors, LLC elected to partially exercise a warrant by exchanging 4,945 of its 10,322 warrant shares through a cashless exercise on the terms provided the applicable warrant agreement. As a result, the Company issued 3,100 shares of Common Stock to PfG Equity Investors, LLC on June 4, 2014.

The shares of Common Stock issued upon exercise of the warrants have not been and will not be registered under the Securities Act of 1933, as amended, or any state securities law and were issued pursuant to an exemption from registration provided by Section 4(2) of the Securities Act and/or Regulation D promulgated thereunder.

On July 23, 2014, the Company entered into a Common Stock Purchase Agreement (the 2014 Purchase Agreement) with certain accredited investors party thereto (the 2014 Purchasers). Under the terms of the 2014 Purchase Agreement, the Company sold, and the 2014 Purchasers purchased from the Company, 2,891,566 shares of Common Stock (the 2014 Shares), at a price of $4.15 per share. The 2014 Shares represented 15% of the issued and outstanding shares of Common Stock immediately prior to the execution of the 2014 Purchase Agreement. The offering closed on July 29, 2014. The aggregate gross proceeds, net of fees, the Company received from the offering were approximately $11.1 million. Proceeds from the private placement are being used for general corporate and working capital purposes. Craig-Hallum Capital Group LLC, which acted as the sole placement agent for the offering, received a commission equal to 7% of the aggregate purchase price (excluding certain accounts), for an aggregate commission of $0.8 million, and was reimbursed for its out-of-pocket expenses.

The 2014 Shares were offered and sold to the 2014 Purchasers under the 2014 Purchase Agreement in transactions exempt from registration under the Securities Act of 1933, as amended, or state securities laws, in reliance on Section 4(2) thereof and Rule 506 of Regulation D of the Securities Act and in reliance on similar exemptions under applicable state laws. Each of the 2014 Purchasers represented that it is an accredited investor within the meaning of Rule 501(a) of Regulation D, and acquiring the 2014 Shares for investment only and not with a view towards, or for resale in connection with, the public sale or distribution thereof. The 2014 Shares were offered without any general solicitation by the Company or its representatives. The Company filed a registration statement on Form S-3 (the 2014 Registration Statement) with the SEC on August 12, 2014 to register the resale by the 2014 Purchasers of the 2014 Shares and the 2014 Registration Statement became effective on August 25, 2014.

On November 26, 2013, the Company entered into a Common Stock Purchase Agreement (the 2013 Purchase Agreement), with certain accredited investors party thereto (collectively, the 2013 Purchasers). Under the terms of the 2013 Purchase Agreement, the Company sold, and the 2013 Purchasers purchased from the Company, 1,538,462 shares of Common Stock (the 2013 Shares), at a price of $3.90 per share. The aggregate gross proceeds the Company received from the offering, net of fees, were approximately $5.6 million. Approximately 39.9% of the 2013 Shares were purchased by directors of the Company, or by their affiliates. Commissions of $0.3 million were paid in connection with the sale of the 2013 Shares. The 2013 Shares were sold without registration under the Securities Act or state securities laws, in reliance on Rule 506 of the Securities Act and in reliance on similar exemptions under applicable state laws. Each of the purchasers is an accredited investor within the meaning of Rule 501(a) of Regulation D and the 2013 Shares were sold without any general solicitation by the Company or its representatives. The Company filed a registration statement on Form S-3 with the SEC on December 31, 2013 to register the resale by the 2013 Purchasers of the 2013 Shares and the registration statement became effective on February 6, 2014.

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Stock Performance Graph

The following graph compares the cumulative total stockholder return on Common Stock with the cumulative total return of (i) a peer group of other publicly-traded information-technology consulting companies selected by the Company (the Peer Group Index), and (ii) the NASDAQ Global Market Index. Cumulative total stockholder return is based on the period from December 26, 2009 through the Company s fiscal year end on Wednesday, December 31, 2014. The comparison assumes that $100 was invested on December 26, 2009 in each of Mattersight Common Stock, the Peer Group Index, and the NASDAQ Global Market Index, and that any and all dividends were reinvested.

Comparative Cumulative Total Return for Mattersight Corporation,

Peer Group Index, and NASDAQ Global Market Index

	12/26/09	1/1/11	12/31/11	12/31/12	12/31/13	12/31/14
Mattersight Common Stock	$ 100.00	$ 91.43	$ 66.43	$ 71.00	$ 68.43	$ 89.29
Peer Group Index[(1)]	100.00	123.53	116.87	117.22	154.80	201.93
NASDAQ Global Market Index	100.00	117.43	118.27	138.47	196.27	223.17

(1) The Peer Group Index consists of Verint Systems, Inc. and Nice Systems Limited. In fiscal year 2011, The Hackett Group, Sapient Corporation, Ciber, Inc., and Convergys Corporation were removed because they had previously been included in the Peer Group Index in order to provide peer comparison for our ICS Business Unit, which was divested. In fiscal year 2010, Nice Systems Limited was added to the Peer Group Index to replace Diamond Management & Technology Consultants, which was removed because its public information was no longer available.

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Repurchase of Equity Securities

The following table provides information relating to the Company s purchase of shares of its Common Stock in the fourth quarter of 2014. These purchases reflect shares withheld upon vesting of restricted stock to satisfy tax-withholding obligations.

Period	Total Number of Shares Purchased	Average Price Paid Per Share
October 1, 2014 October 31, 2014		$
November 1, 2014 November 30, 2014		$
December 1, 2014 December 31, 2014	13,379	$ 5.93
Total	13,379	$ 5.93

Dividends

Historically, we have not paid cash dividends on our Common Stock, and we do not expect to do so in the future. Under the terms of its certificate of designations, our 7% Series B Convertible Preferred Stock (the Series B Stock) accrues dividends at a rate of 7% per year, payable semi-annually in January and July if declared by the Company s Board of Directors. If not declared, unpaid dividends are cumulative and accrue at the rate of 7% per annum. The Board of Directors did not declare a dividend payment on the Series B Stock, which was accrued, for each of the dividend periods from July 1, 2012 through December 31, 2014, (the aggregate amount of these dividends was approximately $1.5 million). During fiscal year 2012, the Company s Board of Directors declared a cash dividend of $0.1785 per share on the Series B Stock for the dividend period January 1, 2012 through June 30, 2012. The dividend payment of $0.3 million was paid on July 2, 2012. Payment of future dividends on the Series B Stock will be determined by the Company s Board of Directors based on the Company s outlook and macroeconomic conditions. If the Company s Board of Directors were to declare a semi-annual cash dividend on the Series B Stock for dividend periods subsequent to January 1, 2015, the dividend payment would be approximately $0.3 million, on the 1,648,185 shares of Series B Stock issued and outstanding as of December 31, 2014.

The amount of each dividend accrual would decrease by any conversions of the Series B Stock into Common Stock, as Series B Stock conversions require us to pay accrued but unpaid dividends at the time of conversion. Conversions of Series B Stock became permissible at the option of the holder after June 19, 2002. For further discussion see Liquidity and Capital Resources included in Part II, Item 7 of this Annual Report on Form 10-K.

During fiscal year 2012, the Company purchased 19,758 shares of Series B Stock and paid accrued and unpaid dividends of $2 thousand in connection with such purchase.

Equity Compensation Information

See Part III, Item 12 of this Annual Report on Form 10-K for information regarding shares of Common Stock that may be issued under the Company s existing equity compensation plans.

Item 6. ***Selected Financial Data.***

The following tables summarize our selected financial data. This information should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations, and the Consolidated Financial Statements of the Company and notes thereto, which are included elsewhere in this Annual Report on Form 10-K.

	(In thousands, except per share data)[1]				
	December 31, 2014	December 31, 2013	December 31, 2012	December 31, 2011	January 1, 2011

Total revenue	$ 30,319	$ 34,494	$ 33,863	$ 29,095	$ 30,885
Loss from continuing operations	$ (14,232)	$ (11,172)	$ (15,470)	$ (10,560)	$ (16,304)
Basic loss from continuing operations per share	$ (0.74)	$ (0.70)	$ (1.01)	$ (1.29)	$ (1.28)
Total assets	$ 32,078	$ 30,749	$ 31,362	$ 49,265	$ 66,192
Long-term obligations	$ 3,990	$ 4,473	$ 3,605	$ 4,437	$ 6,247
Series B Stock	$ 8,406	$ 8,411	$ 8,411	$ 8,521	$ 18,100
Capital leases	$ 2,813	$ 2,832	$ 2,305	$ 2,823	$ 2,217

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(1) See Note One Description of Business and Note Two Summary of Significant Accounting Principles of the Notes to Consolidated Financial Statements included in Part II Item 8 of this Annual Report on Form 10-K for business discussion.

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations.***

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the Selected Financial Data and the consolidated financial statements and notes thereto included elsewhere in this Annual Report on Form 10-K.

Critical Accounting Policies and Estimates

Our management s discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to the costs and timing of completion of client projects, our ability to collect accounts receivable, the timing and amounts of expected payments associated with cost reduction activities, and the ability to realize our net deferred tax assets, contingencies, and litigation. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

The fiscal year-end dates referenced herein for fiscal years 2014, 2013, and 2012 are December 31, 2014, December 31, 2013, and December 31, 2012, respectively.

We believe the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements.

Discontinued Operations

ICS Business Unit Transaction

The Company sold the ICS Business Unit and eLoyalty registered trademark / trade name to Magellan Acquisition Sub, LLC, a Colorado limited liability company and wholly-owned subsidiary of TeleTech Holdings, Inc., a Delaware corporation, closed on May 28, 2011, and the Company changed its name from eLoyalty Corporation to Mattersight Corporation effective May 31, 2011. Therefore, the results of operations of the ICS Business Unit are reported as discontinued operations.

Revenue Recognition

Behavioral Analytics Revenue

Behavioral Analytics revenue consists of Managed services revenue and Consulting services revenue derived from the performance of Behavioral Analytics.

Managed services revenue consists of planning, deployment, training, and subscription fees derived from Behavioral Analytics contracts. Planning, deployment, and training fees, which are considered to be installation fees related to Behavioral Analytics subscription contracts, are deferred until the installation is complete and are then recognized over the applicable subscription period. Subscription periods generally range from three to five years after the go-live date or, in cases where the Company contracts with a client for a short-term pilot of a Behavioral Analytics offering prior to committing to a longer subscription period, if any, the subscription or pilot periods generally range from three to twelve months after the go-live date. Installation costs incurred are deferred up to an amount not to exceed the amount of deferred installation revenue and additional amounts that are recoverable based on the contractual arrangement. These costs are included in Prepaid expenses and Other long-term assets. Such costs are amortized over the subscription period. Costs in excess of the foregoing revenue amount are expensed in the period incurred.

The amount of revenue generated from subscription fees is based on a number of factors, such as the number of users to whom the Behavioral Analytics offering is provided, the type and number of Behavioral Analytics offerings deployed to the client, and in some cases, the number of hours of calls analyzed during the relevant month of the subscription period. This revenue is recognized as the service is performed for the client.

Consulting services revenue primarily consists of fees charged to the Company s clients to provide post-deployment follow-on consulting services, which include custom data analysis, the implementation of enhancements, and training. These follow-on consulting services are generally performed for the Company s clients on a fixed-fee basis. Revenue is recognized as the services are performed, with performance generally assessed on the ratio of actual hours incurred to-date compared to the total estimated hours over the entire term of the contract.

Other Revenue

Other revenue consists of Marketing Managed Services revenue and CRM Services revenue.

Marketing Managed Services revenue is derived from marketing application hosting. This revenue is generally in the form of fixed monthly fees received from the Company s clients and is recognized as the services are performed for the client. Any related setup fee would be recognized over the term of the hosting contract.

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CRM Services revenue consists of fees generated from the Company s operational consulting services, which are provided to the Company s clients on a time-and-materials or fixed-fee basis. The Company recognizes revenue as the services are performed for time-and-materials projects. For fixed-fee projects, revenue is recognized based on the ratio of hours incurred to-date compared to the total estimated hours over the entire term of the contract.

Reimbursed Expenses

Reimbursed expenses revenue includes billable costs related to travel and other out-of-pocket expenses incurred while performing services for the Company s clients. The cost of third-party product and support may be included within this category if the transaction does not satisfy the requirements for gross reporting. An equivalent amount of reimbursable expenses is included in Cost of revenue.

Unearned Revenue

Payments received for Managed services contracts in excess of the amount of revenue recognized for these contracts are recorded as unearned revenue until revenue recognition criteria are met.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from clients not paying for unpaid or disputed invoices for contractual services provided. Additional allowances may be required if the financial condition of our clients deteriorates.

Stock Warrants

In accordance with ASC 480-10, *Distinguishing Liabilities from Equity*, the Company classified certain warrants to purchase Common Stock that do not meet the requirements for classification as equity, as liabilities. Such liabilities are initially recorded at fair value with subsequent changes in fair value recorded as a component of gain or loss on warrant liability on the consolidated statements of operations in each reporting period. If these warrants subsequently meet the requirements of equity classification, the Company will reclassify the fair value to equity. Fair value of the warrants was measured using a Monte Carlo option pricing model and in applying this model certain assumptions were used. See Note Twenty-One Stock Warrants of the Notes to Consolidated Financial Statements included in Part II Item 8 of this Annual Report on Form 10-K.

Stock-Based Compensation

Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period. Determining fair value of stock-based awards at the grant date requires certain assumptions. The Company uses historical information as the basis for the selection of expected life, expected volatility, expected dividend yield assumptions, and anticipated forfeiture rates. The risk-free interest rate is selected based on the yields from U.S. Treasury Strips with a remaining term equal to the expected term of the options being valued.

Goodwill

Goodwill is tested annually for impairment or more frequently if an event or circumstance indicates that an impairment loss may have been incurred. In performing our annual impairment test, we first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value, including goodwill. If it is concluded that this is the case for the reporting unit, we perform a detailed quantitative assessment using a two-step test approach. In the first step, the fair value of the reporting unit is compared with its carrying value. If the fair value exceeds the carrying value, then goodwill is not impaired and no further testing is performed. The second step is performed if the carrying value exceeds the fair value. The implied fair value of the reporting unit s goodwill must be determined and compared to the carrying value of the goodwill. If the carrying value of a reporting unit s goodwill exceeds its implied fair value, then an impairment loss equal to the difference will be recorded. The Company currently operates in a single business segment or reporting unit.

In 2014, after completing our annual qualitative review, we concluded that it was not more likely than not that the carrying value of our reporting unit exceeded its fair value. Accordingly, we concluded that further quantitative analysis and testing was not required, and no goodwill impairment charge was required.

There has been no impairment identified as a result of the annual reviews of goodwill as of December 31, 2014 and December 31, 2013. The carrying value of goodwill was $1.0 million as of December 31, 2014 and December 31, 2013.

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Intangible Assets

Intangible assets reflect costs related to patent and trademark applications, Marketing Managed Services customer relationships acquired in 2004, and the 2003 purchase of a license for certain intellectual property. Patent and trademark applications are amortized over 120 months. The other intangible assets are fully amortized. The original cost of intangible assets as of December 31, 2014 and December 31, 2013 was $3.4 million and $3.2 million, respectively. Accumulated amortization of intangible assets was $2.8 million as of December 31, 2014 and December 31, 2013. Currently, amortization expense of intangible assets is expected to be $91 thousand annually.

Severance and Related Costs

Severance and related costs includes cost-reduction actions, principally consisting of personnel reductions and an office consolidation. The portion of the accruals that related to employee severance represents contractual severance for identified employees and generally is not subject to a significant revision. The portion of the accruals that related to office space reductions, office closures, and associated contractual lease obligations are based in part on assumptions and estimates of the timing and amount of sublease rentals, which may be affected by overall economic and local market conditions. To the extent estimates of the success of our sublease efforts changed, adjustments increasing or decreasing the related accruals have been recognized.

Income Taxes

We have recorded income tax valuation allowances on our net deferred tax assets to account for the unpredictability surrounding the timing of realization of our U.S. and non-U.S. net deferred tax assets due to uncertain economic conditions. The valuation allowances may be reversed at a point in time when management determines realization of these tax assets has become more likely than not, based on a return to predictable levels of profitability.

The Company uses an asset and liability approach for financial accounting and reporting of income taxes. Deferred income taxes are provided when tax laws and financial accounting standards differ with respect to the amount of income for the year, the basis of assets and liabilities and for tax loss carryforwards. The Company does not provide U.S. deferred income taxes on earnings of U.S. or foreign subsidiaries, which are expected to be indefinitely reinvested.

The Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Significant judgment is used to determine the likelihood of the benefit. There is additional guidance on derecognition, classification, interest and penalties on income taxes, accounting in interim periods, and disclosure requirements.

Intraperiod tax allocation requires that the provision for income taxes be allocated between continuing operations and other categories of earnings (such as discontinued operations or other comprehensive loss) for each tax jurisdiction. In periods in which there is a year-to-date pre-tax loss from continuing operations and pre-tax income in other categories of earnings, the tax provision is first allocated to the other categories of earnings. A related tax benefit is then recorded in continuing operations. While intraperiod tax allocation in general does not change the overall tax provision, it does affect the amount of tax provision included in each category. For fiscal years 2014 and 2013, the intraperiod allocation was not applicable because we no longer have any discontinued operations activity. Included in continuing operations income tax provision was tax expense of $38 thousand for the year ended December 31, 2012. Included in discontinued operations income tax provision was a tax benefit of $0.3 million for the year ended December 31, 2012.

Other Significant Accounting Policies

For a description of the Company s other significant accounting policies, see Note Two Summary of Significant Accounting Policies of the Notes to Consolidated Financial Statements included in Part II Item 8 of this Annual Report on Form 10-K.

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Forward-Looking Statements

Statements in this Annual Report on Form 10-K that are not historical facts are forward-looking statements and are made pursuant to the safe harbor provisions of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These forward-looking statements, which may be identified by use of words such as plan, may, might, believe, expect, intend would, should, and other words and terms of similar meaning, in connection with any discussion of our prospects, financial statements, business, financial condition, revenues, results of operations, or liquidity, involve risks and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. In addition to other factors and matters contained or incorporated in this document, important factors that could cause actual results or events to differ materially from those indicated by such forward-looking statements include, without limitation, those noted under Risk Factors included in Part I Item 1A of this Annual Report on Form 10-K for the year ended December 31, 2014, as well as the following:

- Uncertainties associated with the attraction of, and the ability to execute contracts with, new clients, the continuation of existing, and execution of new, engagements with existing clients, the conversion of free pilots to paid subscription contracts, and the timing of related client commitments;

- Reliance on a relatively small number of clients for a significant percentage of our revenue;

- Risks involving the variability and predictability of the number, size, scope, cost, and duration of, and revenue from, client engagements;

- Management of the other risks associated with complex client projects and new service offerings, including execution risk; and

- Management of growth and development of, and introduction of, new service offerings.

We cannot guarantee any future results, levels of activity, performance, or achievements. The statements made in this Annual Report on Form 10-K represent our views as of the date of this Annual Report on Form 10-K, and it should not be assumed that the statements made in this Annual Report on Form 10-K remain accurate as of any future date. Moreover, we assume no obligation to update forward-looking statements, except as may be required by law.

Business Outlook

Based on research from third-party analysts, we believe the call center industry is ripe for disruption and innovation. We believe what the call center was designed to accomplish and how it was measured are parts of an outdated mode of business that is disconnected from the needs of today s consumer. In fact, research from the Corporate Executive Board suggests that any call center interaction is four times more likely to drive customer disloyalty. Given a rise in self-service, these interactions are only becoming more complex and fraught with greater risk.

Through Behavior Analytics, we seek to provide our clients with personality-based software applications that mitigate the complexity and reduce the risk of these call center interactions. According to Gartner, there are 6 million call center seats in North America. Our estimation is that less than 3% of this market is penetrated by personality-based software applications. We believe that we are uniquely positioned to capitalize on this opportunity. Our strategy to increase revenue and capture market share includes the following elements:

- Drive new bookings growth and increase operating leverage;

- Leverage a land & expand model, focused on personality-based routing as the catalyst for new client acquisition;

- Cross-sell coaching, quality assurance and analytic products after delivering a routing solution;

- Continue to invest in innovative linguistic models and behavioral science;

- Expand our sales and marketing capacity; and

- Test the applicability of our proprietary behavioral model with clients outside of the call center industry.

Our personality-based software applications, which have been developed through substantial investment over a decade, are deeply embedded into our clients infrastructure and workflows. Our long-term client relationships are made up largely of multi-year contracts and high contract renewal rates. Our aspiration is that the introduction of a land & expand model with our routing product will accelerate the acquisition of new clients.

Year Ended December 31, 2014 Compared with the Year Ended December 31, 2013

Services Revenue

Services revenue is total revenue excluding reimbursable expenses that are billed to our clients. Our services revenue decreased $4.0 million, or 12%, to $30.2 million in fiscal year 2014, from $34.2 million in fiscal year 2013. The $4.0 million decrease in services revenue in fiscal year 2014 was primarily due to the previously announced expiration of our contract with Vangent, Inc. on December 31, 2013.

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Behavioral Analytics revenue was $29.4 million in fiscal year 2014 and $33.0 million in fiscal year 2013. The $3.6 million, or 11%, decrease in Behavioral Analytics revenue in fiscal year 2014 was also primarily due to the previously announced expiration of our contract with Vangent, Inc. on December 31, 2013.

Other revenue decreased by $0.4 million, or 35%, to $0.8 million in fiscal year 2014, from $1.2 million in fiscal year 2013. This decrease in revenue was primarily due to the completion of our only remaining CRM Services contract.

The Company s top five clients accounted for 75% of total revenue in fiscal year 2014 and 69% of total revenue in fiscal year 2013. The top ten clients accounted for 91% of total revenue in fiscal year 2014 and 90% of total revenue in fiscal year 2013. In fiscal year 2014, three clients each accounted for 10% or more of total revenue and in fiscal year 2013 four clients each accounted for 10% or more of total revenue. In fiscal year 2014, United HealthCare Services, Inc., Progressive Casualty Insurance Company, and HealthCare Service Corporation accounted for 25%, 20%, and 11% of total revenue, respectively. In fiscal year 2013, Vangent, Inc., Progressive Casualty Insurance Company, Allstate Insurance Company, and United HealthCare Services, Inc., accounted for 21%, 15%, 13%, and 11% of total revenue, respectively. Higher concentration of revenue with a single client or a limited group of clients creates increased revenue risk if one of these clients significantly reduces its demand for our services.

Cost of Revenue Before Reimbursed Expenses, Exclusive of Depreciation and Amortization

Cost of Services

Cost of services primarily consists of labor costs, including salaries, fringe benefits, and incentive compensation, royalties, and other client-related third-party outside services. Cost of services excludes depreciation and amortization.

Cost of Behavioral Analytics revenue was $9.0 million, or 31% of Behavioral Analytics revenue, in fiscal year 2014, compared to $10.1 million, or 31% of Behavioral Analytics revenue, in fiscal year 2013. The favorable decrease in cost was primarily due to (i) improved productivity in our Delivery organization resulting in lower compensation costs, (ii) better leveraging of the cost structure supporting our subscription clients, and (iii) the decline in revenue.

Cost of other revenue was $0.3 million, or 36% of Other revenue in fiscal year 2014, compared to $0.6 million, or 51% of Other revenue, in fiscal year 2013.

Sales, Marketing and Development

Sales, marketing and development expenses consist primarily of salaries, incentive compensation, commissions, and employee benefits for business development, account management, marketing, and product development personnel. The personnel costs included in this item are net of any labor costs directly related to the generation of revenue, which are represented in Cost of services.

Sales, marketing and development expenses decreased $0.2 million, or 1%, to $21.6 million in fiscal year 2014 from $21.8 million in fiscal year 2013. The decrease is primarily due to lower compensation expense offset by higher operating lease expense.

General and Administrative

General and administrative expenses consist primarily of salaries, incentive compensation, and employee benefits for administrative personnel, as well as facilities costs, a provision for uncollectible amounts, and costs for our corporate technology infrastructure and applications.

General and administrative expenses increased $0.3 million, or 4%, to $9.1 million in fiscal year 2014 from $8.8 million in fiscal year 2013. The $0.3 million increase is due to higher compensation expense.

Severance and Related Costs

There were no severance and related costs in fiscal year 2014. In fiscal year 2013, there was $0.2 million of expense, which was related to severance and related costs for the elimination of one position.

Depreciation and Amortization

Depreciation and amortization decreased $0.4 million, or 12%, to $3.0 million in fiscal year 2014 from $3.4 million in fiscal year 2013. The decrease is due to capital lease disposals and assets that became fully depreciated near the end of the second and third quarters of 2014.

Amortization of Intangibles

Amortization of intangibles remained constant at $0.1 million in fiscal years 2014 and 2013.

Operating Loss

Primarily as a result of the factors described above, we experienced an operating loss of $13.0 million in fiscal year 2014, compared to an operating loss of $10.8 million in fiscal year 2013.

Interest and Other Expense, Net

Interest and other expense was $1.1 million of expense in fiscal year 2014 compared to $0.5 million of expense in fiscal year 2013. The increase was primarily related to a $0.5 million write-off of deferred financing fees in connection with the termination effective August 14, 2014 of the Loan and Security Agreement dated August 19, 2013, entered into by the Company, together with its wholly-owned subsidiaries Mattersight Europe Holding Corporation and Mattersight International Holding, Inc., as co-borrowers, and Partners for Growth IV, L.P.

Change in Fair Value of Warrant Liability

The change in fair value of warrant liability remained constant at $0.1 million in fiscal years 2014 and 2013. Changes in our common stock price are the main driver in calculating the fair value of our outstanding warrants.

Income Tax (Provision) Benefit

The income tax provision was less than $0.1 million in fiscal year 2014 and the tax benefit was $0.2 million in fiscal year 2013. The income tax benefit in fiscal year 2013 was due to a favorable tax ruling on a previously accrued income tax liability. As of December 31, 2014, total net deferred tax assets of $71.0 million were fully offset by a valuation allowance. The level of uncertainty in predicting when we will achieve profitability, sufficient to utilize our net U.S. and non-U.S. operating losses and realize our remaining deferred tax assets, requires that an income tax valuation allowance be recognized in the financial statements.

Income from Discontinued Operations

There was no income from discontinued operations in fiscal year 2014.

Net Loss Available to Common Stockholders

We reported net loss available to holders of Common Stock of $14.8 million in fiscal year 2014 compared to net loss available to holders of Common Stock of $11.8 million in fiscal year 2013. Accrued dividends to holders of Series B Stock were $0.6 million in both fiscal years 2014 and 2013. In fiscal year 2014, there was net loss of $0.74 per share on a basic and diluted basis, compared to net loss of $0.70 per share on a basic and diluted basis in fiscal year 2013.

Year Ended December 31, 2013 Compared with the Year Ended December 31, 2012

Services Revenue

Services revenue was total revenue excluding reimbursable expenses that are billed to our clients. Our services revenue increased $0.7 million, or 2%, to $34.2 million in fiscal year 2013, from $33.5 million in fiscal year 2012.

Behavioral Analytics revenue was $33.0 million in fiscal year 2013 and was $32.1 million in fiscal year 2012. The $0.9 million, or 3%, increase in Behavioral Analytics revenue in fiscal year 2013 was primarily due to revenue associated with new client agreements, expansion of several existing clients, and the payment by a customer of an early termination fee in connection with the cancellation of a contract.

Other revenue decreased by $0.1 million, or 8%, to $1.2 million in fiscal year 2013, from $1.3 million in fiscal year 2012. The decrease in revenue was mainly due to the completion of several contracts for Marketing Managed Services.

The Company s top five clients accounted for 69% of total revenue in fiscal year 2013 and 66% of total revenue in fiscal year 2012. The top ten clients accounted for 90% of total revenue in fiscal year 2013 and 89% of total revenue in fiscal year 2012. In fiscal year 2013, there were four clients that accounted for 10% or more of total revenue, whereas three clients accounted for 10% or more of total revenue in fiscal year 2012. In fiscal year 2013, Vangent, Inc., Progressive Casualty Insurance Company, Allstate Insurance Company, and United HealthCare Services, Inc., accounted for 21%, 15%, 13%, and 11% of total revenue, respectively. In fiscal year 2012, Vangent, Inc., Allstate Insurance Company, and

Progressive Casualty Insurance Co. accounted for 19%, 16%, and 13% of total revenue, respectively. Higher concentration of revenue with a single client or a limited group of clients creates increased revenue risk if one of these clients significantly reduces its demand for our services. As previously announced, our contract with Vangent, Inc. expired on December 31, 2013.

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Cost of Revenue Before Reimbursed Expenses, Exclusive of Depreciation and Amortization

Cost of Services

Cost of services primarily consists of labor costs, including salaries, fringe benefits, and incentive compensation, royalties, and other client-related third-party outside services. Cost of services excludes depreciation and amortization.

Cost of Behavioral Analytics revenue was $10.1 million, or 31% of Behavioral Analytics revenue, in fiscal year 2013, compared to $12.2 million, or 38% of Behavioral Analytics revenue, in fiscal year 2012. The favorable decrease in cost and percentage was primarily due to improved productivity in our Delivery organization resulting in lower compensation costs and better leverage of our cost structure supporting our subscription clients.

Cost of other revenue was $0.6 million, or 51% of Other revenue, in fiscal year 2013, compared to $0.7 million, or 53% of Other revenue, in fiscal year 2012. The favorable $0.1 million decrease in cost and percentage was primarily due to lower CRM Service revenue.

Sales, Marketing and Development

Sales, marketing and development expenses consist primarily of salaries, incentive compensation, commissions, and employee benefits for business development, account management, marketing, and product development personnel. The personnel costs included in this item are net of any labor costs directly related to the generation of revenue, which are represented in Cost of services.

Sales, marketing and development expenses decreased $1.3 million, or 6%, to $21.8 million in fiscal year 2013 from $23.1 million in fiscal year 2012. This decrease was primarily due to lower compensation expense.

General and Administrative

General and administrative expenses consist primarily of salaries, incentive compensation, and employee benefits for administrative personnel, as well as facilities costs, a provision for uncollectible amounts, and costs for our corporate technology infrastructure and applications.

General and administrative expenses increased $0.5 million, or 6%, to $8.8 million in fiscal year 2013, from $8.3 million in fiscal year 2012. This increase was primarily due to higher compensation expense.

Severance and Related Costs

Severance and related costs includes cost-reduction actions, principally consisting of personnel reductions and an office consolidation. Cash savings related to cost-reduction actions taken during fiscal year 2013 are anticipated to be $0.2 million annually. Costs related to office space reductions and office closures were paid pursuant to contractual lease terms through January 2012.

In fiscal year 2013, there was $0.2 million of expense which was related to severance and related costs for the elimination of one position. In fiscal year 2012, the $0.7 million of expense was related to severance and related costs for the elimination of one position.

Depreciation and Amortization

Depreciation expense remained constant at $3.4 million in fiscal years 2013 and 2012.

Amortization of Intangibles

Amortization of intangibles remained constant at $0.1 million in fiscal years 2013 and 2012.

Operating Loss

Primarily as a result of the factors described above, we experienced an operating loss of $10.8 million for fiscal year 2013, compared to an operating loss of $15.0 million for fiscal year 2012, a $4.3 million, or 28%, improvement.

Interest and Other Expense, Net

Non-operating interest and other expense was $0.7 million of expense in fiscal year 2013 compared to $0.4 million of expense in fiscal year 2012. The increase of $0.3 million of expense was primarily related to interest expense on our short-term debt and capital lease obligation.

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Income Tax Benefit (Provision)

The income tax benefit was $0.2 million in fiscal year 2013 and the tax provision was less than $0.1 million in fiscal year 2012. The income tax benefit in fiscal year 2013 was due to a favorable tax ruling on a previously accrued income tax liability. As of December 31, 2013, total net deferred tax assets of $67.6 million were fully offset by a valuation allowance. The level of uncertainty in predicting when we will achieve profitability, sufficient to utilize our net U.S. and non-U.S. operating losses and realize our remaining deferred tax assets, requires that an income tax valuation allowance be recognized in the financial statements.

Income from Discontinued Operations

There was no income from discontinued operations in fiscal year 2013. The income from discontinued operations in fiscal year 2012 was $0.2 million, net of tax benefit of $0.3 million, due to a favorable Internal Revenue Service (IRS) ruling on a previously accrued income tax liability partially offset by settlement costs relating to a former employee of the ICS Business Unit.

Net Loss Available to Common Stockholders

We reported net loss available to holders of Common Stock of $11.8 million in fiscal year 2013 compared to net loss available to holders of Common Stock of $15.9 million in fiscal year 2012. Accrued dividends to holders of Series B Stock were $0.6 million in both fiscal years 2013 and 2012. In fiscal year 2013, there was net loss of $0.70 per share on a basic and diluted basis, compared to net loss of $0.99 per share on a basic and diluted basis in fiscal year 2012.

Liquidity and Capital Resources

Introduction

Our principal capital requirements are to fund working capital needs, capital expenditures for Behavioral Analytics and infrastructure requirements, and other revenue generation and growth investments. As of December 31, 2014, our principal capital resources consisted of our cash and cash equivalents balance of $14.2 million, which includes $0.1 million in foreign bank accounts.

The increase in cash during fiscal year 2014 was primarily from proceeds received from the sale of the 2014 Shares pursuant to the 2014 Purchase Agreement of $11.1 million, net of fees, partially offset by the net loss before non-cash items, payment of Company bonuses, capital lease principal payments, capital expenditures, the acquisition of treasury stock, and an increase in accounts receivable.

The decrease in cash during fiscal year 2013 was primarily the result of the net loss before non-cash items, a $3.7 million net payment under our credit facility, capital lease principal payments, capital expenditures, and the acquisition of treasury stock, partially offset by proceeds of $5.6 million, net of fees, received from the sale of the 2013 Shares pursuant to the terms of the 2013 Purchase Agreement and a $1.9 million increase in unearned revenue.

Cash Flows from Operating Activities

Net cash used in operating activities during fiscal year 2014 was $6.9 million compared to cash of $1.6 million during fiscal year 2013. During fiscal year 2014, net cash used in operating activities consisted primarily of the net loss before non-cash items of $6.8 million and an increase in accounts receivable.

During fiscal year 2013, net cash provided by operating activities was $1.6 million. During fiscal year 2013, net cash provided by operating activities consisted primarily of a $1.9 million increase in unearned revenue, partially offset by the net loss before non-cash items of $1.9 million.

There was no net cash used in operating activities of discontinued operations during fiscal years 2014 and 2013.

Days Sales Outstanding (DSO) was 38 days at December 31, 2014, compared to 23 days at December 31, 2013, an increase of fifteen days. DSO increased due to two clients with higher 2014 Accounts Receivable associated with significant revenue growth, compared to an unusually low 2013 DSO that included revenue from a large client which had fully paid all outstanding invoices by the end of 2013. Because a high percentage of our revenue is dependent on a relatively small number of clients, delayed payments by a few of our larger clients could result in a reduction of our available cash, which in turn may cause fluctuation in our DSO. We do not expect any significant collection issues with our clients; see

Accounts Receivable Customer Concentration for additional information on cash collections.

As of December 31, 2014, there were no outstanding liabilities for severance and related costs.

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Cash Flows from Investing Activities

The Company used $1.0 million and $1.5 million of cash in investing activities during fiscal years 2014 and 2013, respectively.

Capital expenditures were primarily used to purchase computer hardware and software during fiscal years 2014 and 2013. We currently expect to incur new capital investments of between $3.0 million and $4.0 million for fiscal year 2015 and plan on funding approximately $1.5 million to $2.0 million of these purchases with capital leases.

There was no net cash used in discontinued investing activities during fiscal years 2014 and 2013.

Cash Flows from Financing Activities

Net cash provided by financing activities was $8.8 million during fiscal year 2014 compared to cash used in financing activities of $1.1 million during fiscal year 2013. Net cash proceeds of $8.8 million during fiscal year 2014 were primarily attributable to proceeds of $11.1 million, net of fees, from the sale of the 2014 Shares pursuant to the 2014 Purchase Agreement, partially offset by (i) $1.7 million of principal payments under our capital lease obligations and (ii) $0.8 million of cash used to acquire treasury stock to meet employee tax obligations associated with the Company s stock-based compensation programs.

During fiscal year 2013, the Company used net cash of $1.1 million in financing activities primarily attributable to a $3.7 million net payment under our credit facility, $2.1 million of principal payments under our capital lease obligations, and $1.1 million of cash used to acquire treasury stock, partially offset by proceeds of $5.6 million, net of fees, from the sale of the 2013 Shares pursuant to the 2013 Purchase Agreement.

There was no net cash used in discontinued financing activities during fiscal year 2014 and 2013.

Historically, we have not paid cash dividends on our Common Stock, and we do not expect to do so in the future. Under the terms of its certificate of designations, our Series B Stock accrues dividends at a rate of 7% per year, payable semi-annually in January and July if declared by the Company s Board of Directors. If not declared, unpaid dividends are cumulative and accrue at the rate of 7% per annum. The Board of Directors did not declare a dividend payment on the Series B Stock, which was accrued, for each of the dividend periods from July 1, 2012 through December 31, 2014, (the aggregate amount of these dividends was approximately $1.5 million). During fiscal year 2012, the Company s Board of Directors declared a cash dividend of $0.1785 per share on the Series B Stock for the dividend period January 1, 2012 through June 30, 2012. The dividend payment of $0.3 million was paid on July 2, 2012. Payment of future dividends on the Series B Stock will be determined by the Company s Board of Directors based on the Company s outlook and macroeconomic conditions. If the Company s Board of Directors were to declare a semi-annual cash dividend on the Series B Stock for dividend periods subsequent to January 1, 2015, the dividend payment would be approximately $0.3 million on the 1,648,185 shares of Series B Stock issued and outstanding as of December 31, 2014. The amount of each dividend accrual will be decreased by any conversions of the Series B Stock into Common Stock, as such conversions require the Company to pay accrued but unpaid dividends at the time of conversion. Conversions of Series B Stock became permissible at the option of the holder after June 19, 2002.

The Company expects to acquire between $0.3 million and $0.4 million of treasury stock during the first quarter of 2015 to meet employee tax obligations associated with the Company s stock-based compensation programs.

Liquidity

Our near-term capital resources consist of our current cash balance, together with anticipated future cash flows, financing from capital leases, and our revolving line of credit (see Credit Facility below). Our balance of cash and cash equivalents was $14.2 million as of December 31, 2014.

We anticipate that our current unrestricted cash resources, together with operating revenue and capital lease financing, should be sufficient to satisfy our short-term working capital and capital expenditure needs for the next twelve months. Management will continue to assess opportunities to maximize cash resources by actively managing our cost structure and closely monitoring the collection of our accounts receivable. If, however, our operating activities, capital expenditure requirements, or net cash needs differ materially from current expectations due to uncertainties surrounding the current capital market, credit and general economic conditions, competition, or the termination of a large client contract, then there is no assurance that we would have access to additional external capital resources on acceptable terms.

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Credit Facility

During fiscal year 2014, the Company, together with its wholly-owned subsidiaries Mattersight Europe Holding Corporation and Mattersight International Holding, Inc., as co-borrowers (the Co-Borrowers), entered into a Second Amendment to the Amended and Restated Loan and Security Agreement with Silicon Valley Bank (the Second Amendment) on June 27, 2014. The Second Amendment amended our financial covenants under the Amended and Restated Loan Agreement entered into by the Company, together with the Co-Borrowers, and Silicon Valley Bank on May 20, 2013 (the Credit Facility) by: (i) reducing the tangible net worth requirement from $3.0 million to $1.25 million and (ii) adding a minimum revenue requirement.

As of December 31, 2014, the Company s $10.0 million revolving line of credit was set to mature in May 2015. Through the maturity date, the Company was obligated to pay a fee equal to one-eighth of one percent (0.125%) per annum of the average unused portion of the Credit Facility, payable quarterly in arrears. The Company had a zero balance outstanding under the Credit Facility as of December 31, 2014.

The Credit Facility imposes various restrictions on the Company, including usual and customary limitations on the ability of the Company or any of its subsidiaries to incur debt and to grant liens upon their assets, and prohibits certain consolidations, mergers, and sales and transfers of assets by the Company and its subsidiaries. The Credit Facility includes usual and customary events of default for facilities of this nature (with customary grace periods, as applicable) and provides that, upon the occurrence of an event of default, payment of all amounts payable under the Credit Facility may be accelerated and/or the lenders commitments may be terminated. In addition, upon the occurrence of certain insolvency or bankruptcy related events of default, all amounts payable under the Credit Facility will automatically become immediately due and payable, and the lenders commitments will automatically terminate. The Company was in compliance with all of its debt covenants under the Credit Facility as of December 31, 2014, except for the minimum revenue covenant, for which the Company received a waiver from Silicon Valley Bank.

On March 10, 2015, the Company entered into a Second Amended and Restated Loan and Security Agreement (Second Amended and Restated Credit Agreement) with Silicon Valley Bank. The Second Amended and Restated Credit Agreement provides for, among other things, an increase of the maximum credit limit from $10 million to $15 million, an extension of the term from May 2015 to March 2017, and a change in interest rate from a variable interest grid to prime plus 1.25%. The Second Amended and Restated Credit Agreement additionally provides for an annual commitment fee of $56,250 and early termination fee of 1.0% in the first year, and 0.25% thereafter, prior to maturity.

See Note Ten Short-Term Debt of the Notes to Consolidated Financial Statements included in Part II Item 8 of this Annual Report on Form 10-K.

Accounts Receivable Customer Concentration

As of December 31, 2014, two clients, United HealthCare Services, Inc., and CVS Pharmacy, Inc., accounted for 41% and 19% of total gross accounts receivable, respectively. Of these amounts, we have collected 100% from United HealthCare Services, Inc., and 89% from CVS Pharmacy, Inc., through March 3, 2015. Of the total December 31, 2014 gross accounts receivable, we have collected 88% as of March 3, 2015. Because we have a high percentage of our revenue dependent on a relatively small number of clients, delayed payments by a few of our larger clients could result in a reduction of our available cash.

Capital Lease Obligations

Capital lease obligations as of December 31, 2014 and December 31, 2013 remained constant at $2.8 million. We are a party to a capital lease agreement with a leasing company to lease hardware and software. We expect to incur new capital lease obligations of between $1.5 million to $2.0 million for fiscal year 2015 as we continue to expand our investment in the infrastructure for Behavioral Analytics.

Contractual Obligations

Cash will also be required for operating leases and non-cancellable purchase obligations, as well as various commitments reflected as liabilities on our balance sheet as of December 31, 2014. These commitments are as follows:

(In millions) **Contractual Obligations**	**Total**	**Less Than 1 Year**	**1 3 Years**	**3 5 Years**	**More Than 5**

					Years
Letters of credit	$ 0.9	$ 0.9	$	$	$
Operating leases	2.0	1.1	0.9		
Capital leases	3.2	1.9	1.3		
Purchase obligations	2.1	2.1			
Total	$ 8.2	$ 6.0	$ 2.2	$	$

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Letters of Credit

The amounts set forth in the chart above reflect standby letters of credit issued as collateral for capital leases. Specifically, these amounts reflect the face amount of these letters of credit that expire in each period presented.

Leases

The amounts set forth in the chart above reflect future principal, interest, and executory costs of the leases entered into by the Company for technology and office equipment, as well as office and data center space. Liabilities for the principal portion of the capital lease obligations are reflected on our balance sheet as of December 31, 2014 and December 31, 2013.

Purchase Obligations

Purchase obligations include $1.5 million of commitments reflected as liabilities on our balance sheet as of December 31, 2014, as well as $0.6 million of non-cancellable obligations to purchase goods or services in the future. Purchase obligations include $0.9 million of commitments reflected as liabilities on our balance sheet as of December 31, 2013, as well as $0.6 million of non-cancellable obligations to purchase goods or services in the future.

Recent Accounting Pronouncements

In November 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity. ASU 2014-16 does not change the current criteria in GAAP for determining when separation of certain embedded derivative features in a hybrid financial instrument is required, but clarifies how current GAAP should be interpreted in the evaluation of the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share, reducing existing diversity in practice. The adoption of this ASU is not expected to have a material impact on the Company s consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15: Presentation of Financial Statements Going Concern (Subtopic 205-40) (ASU 2014-15): Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern. The update sets forth a requirement for management to evaluate whether there are conditions and events that raise substantial doubt about an entity s ability to continue as a going concern, a responsibility that did not previously exist in GAAP. The amendments included in this update require management to assess an entity s ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards. Specifically, the amendments (i) provide a definition of the term substantial doubt , (ii) require an evaluation every reporting period, including interim periods, (iii) provide principles for considering the mitigating effect of management s plans, (iv) require certain disclosures when substantial doubt is alleviated as a result of consideration of management s plans, (v) require an express statement and other disclosures when substantial doubt is not alleviated, and (vi) require an assessment for a period of one year after the date that the financial statements are issued (or available to be issued). ASU 2014-15 will be effective for the Company in fiscal year 2016. The adoption of this ASU is not expected to have a material impact on the Company s consolidated financial statements.

In May 2014, FASB issued ASU 20-14-09: Revenue from Contracts with Customers (Topic 606) (ASU 2014-09). The new guidance sets forth a new five-step revenue recognition model that replaces the prior revenue recognition guidance in its entirety and is intended to eliminate numerous industry-specific pieces of revenue recognition guidance that have historically existed in GAAP. The underlying principle of the new standard is that a business or other organization will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects what it expects in exchange for the goods or services. ASU 2014-09 provides alternative methods of initial adoption and is effective for annual periods beginning after December 15, 2016 and interim periods within those annual periods. Early adoption is not permitted. The Company is currently evaluating the impact that this standard will have on the Company s consolidated financial statements.

Item 7A. ***Quantitative and Qualitative Disclosures about Market Risk.***

Historically, we have not experienced material fluctuations in our results of operations due to foreign currency exchange rate changes. We do not currently engage, nor is there any plan to engage, in hedging foreign currency risk.

We also have interest rate risk with respect to changes in variable interest rates on our revolving line of credit, and our cash and cash equivalents and restricted cash. Interest on the line of credit is currently based on either Silicon Valley Bank s prime rate, or LIBOR, which varies in accordance with prevailing market conditions. A change in interest rate impacts the interest expense on the line of credit and cash flows. This interest rate risk will not have a material impact on our financial position or results of operations.

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Item 8. ***Financial Statements and Supplementary Data.***

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS OF MATTERSIGHT CORPORATION

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders

Mattersight Corporation

We have audited the accompanying consolidated balance sheets of Mattersight Corporation (a Delaware corporation) and subsidiaries (the Company) as of December 31, 2014 and 2013, and the related consolidated statements of operations, comprehensive loss, changes in stockholders equity, and cash flows for each of the three years in the period ended December 31, 2014. Our audits of the basic consolidated financial statements included the financial statement schedule listed in the index appearing under Schedule II Valuation and Qualifying Accounts. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company s internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mattersight Corporation and subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

/s/ GRANT THORNTON LLP

Chicago, IL

March 12, 2015

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MATTERSIGHT CORPORATION

CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	December 31, 2014	December 31, 2013
ASSETS:		
Current Assets:		
Cash and cash equivalents	$ 14,238	$ 13,392
Receivables, net	3,460	2,384
Prepaid expenses	4,449	3,576
Other current assets	236	427
Total current assets	22,383	19,779
Equipment and leasehold improvements, net	4,657	5,158
Goodwill	972	972
Intangibles, net	571	409
Other long-term assets	3,495	4,431
Total assets	$ 32,078	$ 30,749
LIABILITIES AND STOCKHOLDERS EQUITY:		
Current Liabilities:		
Accounts payable	$ 1,183	$ 752
Accrued compensation and related costs	2,241	1,844
Unearned revenue	7,859	7,215
Capital leases	1,637	1,599
Other current liabilities	2,549	2,499
Total current liabilities	15,469	13,909
Long-term unearned revenue	2,532	2,866
Long-term capital leases	1,176	1,233
Other long-term liabilities	282	374
Total liabilities	19,459	18,382
Series B Stock, $0.01 par value; 5,000,000 shares authorized and designated; 1,648,185 and 1,649,122 shares issued and outstanding at December 31, 2014 and December 31, 2013, respectively, with a liquidation preference of $9,877 and $9,294 at December 31, 2014 and December 31, 2013, respectively	8,406	8,411
Stockholders Equity:		
Preferred Stock, $0.01 par value; 35,000,000 shares authorized; none issued and outstanding		
Common Stock, $0.01 par value; 50,000,000 shares authorized; 24,046,977 and 20,465,984 shares issued at December 31, 2014 and December 31, 2013, respectively; and 22,324,093 and 18,886,966 outstanding at December 31, 2014 and December 31, 2013, respectively	240	205
Additional paid-in capital	243,282	228,038
Accumulated deficit	(226,404)	(212,172)
Treasury stock, at cost, 1,722,884 and 1,579,018 shares at December 31, 2014 and December 31, 2013, respectively	(8,879)	(8,082)
Accumulated other comprehensive loss	(4,026)	(4,033)

Total stockholders equity		4,213		3,956
Total liabilities and stockholders equity	$	32,078	$	30,749

See accompanying notes to consolidated financial statements.

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MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	For the Fiscal Years Ended		
	2014	**2013**	**2012**
Revenue:			
Behavioral Analytics revenue	$ 29,427	$ 33,005	$ 32,138
Other revenue	779	1,206	1,314
Total services revenue	30,206	34,211	33,452
Reimbursed expenses	113	283	411
Total revenue	30,319	34,494	33,863
Operating expenses:			
Cost of Behavioral Analytics revenue	9,007	10,139	12,208
Cost of Other revenue	279	617	702
Cost of services	9,286	10,756	12,910
Reimbursed expenses	113	283	411
Total cost of revenue, exclusive of depreciation and amortization shown below:	9,399	11,039	13,321
Sales, marketing and development	21,647	21,760	23,142
General and administrative	9,140	8,782	8,255
Severance and related costs		154	693
Depreciation and amortization	3,022	3,450	3,419
Amortization of intangibles	106	66	81
Total operating expenses	43,314	45,251	48,911
Operating loss	(12,995)	(10,757)	(15,048)
Interest and other (expense) income, net	(1,090)	(534)	(384)
Change in fair value of warrant liability	(124)	(125)	
Loss from continuing operations before income taxes	(14,209)	(11,416)	(15,432)
Income tax (provision) benefit	(23)	244	(38)
Loss from continuing operations	(14,232)	(11,172)	(15,470)
Income from discontinued operations, net of tax			249
Net loss	(14,232)	(11,172)	(15,221)
Series B Stock fair value over stated value			(69)
Dividends related to Series B Stock	(589)	(589)	(591)
Net loss available to Common Stock holders	$ (14,821)	$ (11,761)	$ (15,881)
Per share of Common Stock:			
Basic loss from continuing operations	$ (0.74)	$ (0.70)	$ (1.01)

Basic income from discontinued operations	$	$	$ 0.02
Basic net loss available to Common Stock holders	$ (0.74)	$ (0.70)	$ (0.99)
Per share of Common Stock:			
Diluted loss from continuing operations	$ (0.74)	$ (0.70)	$ (1.01)
Diluted income from discontinued operations	$	$	$ 0.02
Diluted net loss available to Common Stock holders	$ (0.74)	$ (0.70)	$ (0.99)
Shares used to calculate basic net loss per share	19,923	16,722	16,002
Shares used to calculate diluted net loss per share	19,923	16,722	16,002
Stock-based compensation, primarily restricted stock, is included in individual line items above:			
Cost of Behavioral Analytics revenue	$ 181	$ 267	$ 16
Sales, marketing and development	2,022	3,436	2,308
General and administrative	1,975	1,872	1,405
Severance and related costs		29	268

See accompanying notes to consolidated financial statements.

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MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands)

	For the Fiscal Years Ended		
	2014	**2013**	**2012**
Net loss	$ (14,232)	$ (11,172)	$ (15,221)
Other comprehensive loss:			
Effect of currency translation	7	6	(1)
Comprehensive net loss	$ (14,225)	$ (11,166)	$ (15,222)

See accompanying notes to consolidated financial statements.

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MATTERSIGHT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	For the Fiscal Years Ended		
	2014	**2013**	**2012**
Cash Flows from Operating Activities:			
Net loss	$ (14,232)	$ (11,172)	$ (15,221)
Less: net income from discontinued operations			249
Net loss from continuing operations	(14,232)	(11,172)	(15,470)
Adjustments to reconcile net loss from continuing operations to net cash (used in) provided by operating activities:			
Depreciation and amortization	3,128		