APPFOLIO INC
Form 10-K
February 27, 2017

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

FORM 10-K

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

For the fiscal year ended December 31, 2016

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

For the transition period from to

Commission File Number 001-37468

AppFolio, Inc.
(Exact name of registrant as specified in its charter)

Delaware	26-0359894
(State of incorporation or organization)	(I.R.S. Employer Identification No.)
50 Castilian Drive Goleta, California	93117
(Address of principal executive offices)	(Zip Code)

(805) 364-6093
Registrant's telephone number, including area code

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

Title of each class	Name of exchange on which registered
Class A common stock, par value $0.0001 per share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Exchange 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 o NO x

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

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 o

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K(§ 229.405 of this chapter) 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 Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer ¨ Accelerated filer x

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO x

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based on the closing price of the registrant's Class A common stock on June 30, 2016 (the last business day of the registrant's mostly recently completed second fiscal quarter), as reported on the NASDAQ Global Market on such date, was approximately $181.8 million. Shares of the registrant's Class A common stock and Class B common stock held by each executive officer, director and holder of 10% or more of the registrant's outstanding Class A common stock and Class B common stock have been excluded from this calculation as such persons may be deemed to be affiliates. This calculation does not reflect a determination that these persons are affiliates of the registrant for any other purpose.

As of February 16, 2017, the number of shares of the registrant's Class A common stock outstanding was 11,720,831 and the number of shares of the registrant's Class B common stock outstanding was 22,015,455.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for the 2017 Annual Meeting of Stockholders (the "Proxy Statement"), to be filed with the Securities and Exchange Commission (the "SEC") pursuant to Regulation 14A not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K (the "Annual Report"), are incorporated by reference in Part III, Items 10-14 of this Annual Report. Except for the portions of the Proxy Statement specifically incorporated by reference in this Annual Report, the Proxy Statement shall not be deemed to be filed as part hereof.

APPFOLIO, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2016

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K for the fiscal year ended December 31, 2016, or Annual Report, includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, which statements are subject to considerable risks and uncertainties. Forward-looking statements include all statements that are not statements of historical facts contained in this Annual Report and can be identified by words such as "anticipates," "believes," "seeks," "estimates," "expects," "intends," "may," "plans," "potential," "predicts, "projects," "should "would" or similar expressions and the negatives of those expressions. In particular, forward looking statements contained in this Annual Report relate to, among other things, our future or assumed financial condition, results of operations, business forecasts and plans, capital needs and financing plans, research and product development plans, services provided, growth in the size of our business and number of customers, strategic plans and objectives, acquisitions and investments, and the application of accounting guidance. We caution you that the foregoing list may not include all of the forward-looking statements made in this Annual Report.

Forward-looking statements represent our management's current beliefs and assumptions based on information currently available. Forward-looking statements involve numerous known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. We discuss these risks and uncertainties in greater detail in the section entitled "Risk Factors" in Part I, Item 1A of this Annual Report, as well as in our other filings with the Securities and Exchange Commission, or SEC. You should read this Annual Report, and the other documents that we have filed with the SEC, with the understanding that our actual future results may be materially different from the results expressed or implied by these forward-looking statements.

Moreover, we operate in an evolving environment. New risks and uncertainties emerge from time to time and it is not possible for our management to predict all risks and uncertainties, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual future results to be materially different from those expressed or implied by any forward-looking statements.

Except as required by applicable law or the rules of the NASDAQ Stock Market, we assume no obligation to update any forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

We qualify all of our forward-looking statements by these cautionary statements.

PART I

ITEM 1. BUSINESS

Unless otherwise stated in this Annual Report, references to "AppFolio," "we," "us," and "our" refer to AppFolio, Inc. and its consolidated subsidiaries.

Overview

We were formed in 2006 with a vision to revolutionize the way that small and medium-sized businesses, or SMBs, grow and compete by enabling their digital transformation. Today we provide industry-specific, cloud-based software solutions for SMBs, in the property management industry, and solo practitioners and small law firms in the legal industries. We refer to solo practitioners and small law firms as SMBs for purpose of our legal vertical in this Annual Report. We initially chose to enter the market for property management because it met our criteria for selecting industries that cloud-based solutions are ideally suited to address, including the prevalence of unique workflows, compliance requirements and relationships among multiple industry participants. We launched our first product, AppFolio Property Manager, or APM, a property management solution, in 2008. In 2012, after completing our market validation process, we decided to enter the legal market. We expedited our time-to-market by acquiring MyCase, a legal practice and case management solution, and we leveraged our AppFolio Business System, including our experience gained in the property management vertical, to advance our software solution in the legal vertical.

SMBs face a common set of issues that divert limited time and resources away from serving their clients and growing their businesses. Their day-to-day operations are often managed through inefficient manual processes and disparate software systems. This lack of automation and integrated technology places a significant administrative burden on these businesses, particularly in industries that involve unique workflows, relationships among multiple industry participants, significant data inputs and management, and compliance or regulatory requirements. While larger enterprises and consumers have been experiencing a transformational shift into the digital age, the legacy systems and manual business processes currently used by many SMBs are lagging behind in terms of technological sophistication and ease of use. In particular, many small and medium-sized property managers are still running their businesses using spreadsheets, older technology and a variety of point solutions that are not web-optimized. Similarly, solo practitioners and small law firms continue to be plagued by manual processes and outdated software that divert time away from practicing law and working with clients.

Our mission is to revolutionize the way that SMBs grow and compete by enabling their digital transformation. We accomplish our mission by delivering a software platform that is designed to be the system of record to automate essential business processes and the system of engagement to enhance business interactions between our customers and their clients and vendors. Our mobile-optimized software solutions have a user-friendly interface designed for use across multiple devices, enabling our customers to work at any time and from anywhere. Our property management software provides small and medium-sized property managers with an end-to-end solution to their business needs, enabling them to manage their portfolio of properties quickly and easily in a single, unified environment. Our legal software provides solo practitioners and small law firms with a streamlined practice and case management solution, allowing them to manage their practices and case load within a single system. We also offer optional, but often mission-critical, Value+ services, such as our professionally designed websites and electronic payment services, which are seamlessly built into our core solutions.

We refer to our approach to addressing similar, fundamental business needs of SMBs across our targeted verticals as our AppFolio Business System. At the center of our AppFolio Business System is a systemized set of best practices and common technology platform that can be applied to existing and future vertical markets. We apply a disciplined approach of using market validation to select and develop new core functionality and Value+ services for our existing markets and to identify the most suitable adjacent markets and new verticals to pursue. We continuously expand the core functionality and add new Value+ services to our existing software solutions based on industry trends, research and feedback from our customers. We use online marketing, participation at customer and industry events, and in-app messaging to educate new and existing customers on how our software solutions can benefit their businesses. Based on the foundation created by our marketing activities, our sales team builds relationships with potential customers, assesses their business challenges and demonstrates the benefits of our software solution. We then partner with our customers to navigate their digital transformation by streamlining the on-boarding process and providing ongoing

advice on best practices. Our customer-centric culture serves to deepen our relationships with our customers and helps to maximize the value of our software solutions for their businesses.

Our core solutions address common business functions and interactions of SMBs in our targeted verticals by providing key functionality, including accounting, document management, real-time interactive search, data analytics and communication options. We currently offer APM for property managers and MyCase for solo practitioners and small law firms. APM is a software solution designed to address the operational requirements of small and medium-sized property managers, including activities such as posting and tracking tenant vacancies, handling the entire leasing process electronically, administering maintenance and repairs

with their vendor networks, managing accounting and reporting to property owners, and communicating with tenants and owners. MyCase is a flexible practice and case management solution that provides time tracking, billing, calendaring, client communication, coordination with other lawyers and support staff, and legal document management and assembly for solo practitioners and small law firms. As MyCase is in an earlier stage of development than APM, we are continuing to expand its core functionality.

In addition to our core solutions, we offer a range of optional, but often mission-critical, Value+ services. Our Value+ services are available on an as-needed basis and enable our customers to adapt our platform to their specific operational requirements. Today, we offer certain Value+ services to both our property manager and law firm customers, namely, professionally designed websites and electronic payment services. In addition, we offer the following Value+ services to our property manager customers: resident screening services; tenant liability insurance; maintenance contact center services; lead generation services; and debt collection services. Over time, we anticipate offering additional Value+ services across our targeted verticals as appropriate for each particular market. We apply our disciplined market validation approach and customer-focused philosophy to select and develop additional Value+ services as well as new core functionality, and to identify the most suitable adjacent markets and new verticals to target.

For the years ended December 31, 2016, 2015 and 2014, our revenue was $105.6 million, $75.0 million and $47.7 million, respectively, representing year-over-year growth of 41% when comparing 2016 to 2015, and year-over-year growth of 57% when comparing 2015 to 2014. Our revenue has limited seasonality as discussed in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations within Quarterly Revenue and Cost Trends. As a result of a substantial increase in headcount, as well as other investments to expand our research and product development, customer service, and sales and marketing organizations, and to maintain and expand our technology infrastructure and operational support, we incurred net losses of $8.3 million, $15.7 million and $8.6 million for the years ended December 31, 2016, 2015 and 2014, respectively. We have invested, and intend to continue to invest, heavily in our business to capitalize on our market opportunity.

Our AppFolio Business System

We refer to our approach to addressing the specific needs of SMBs in each of our targeted verticals as our AppFolio Business System. Our AppFolio Business System has been developed to find, evaluate and serve verticals in which we can deliver a transformative, easy-to-use and cost-effective software solution that can handle the key operational requirements of SMBs. Key elements of our AppFolio Business System include:

Disciplined Market Validation Process. Since our founding, we have worked closely with our customers, partners and other industry participants to inform our product roadmap. We have consistently applied a disciplined market validation process to select and develop new core functionality and Value+ services, and to identify the most suitable adjacent markets and new verticals to target. This approach facilitates faster and more focused product development, with higher confidence that our software solutions will rapidly find market acceptance within our targeted verticals.

AppFolio Technology Platform. At the center of our AppFolio Business System is our modern, cloud-based technology platform, which encompasses a wide variety of reusable core functionality and Value+ services that can be leveraged to provide frequent updates and enhancements across our software solutions in our targeted verticals. The functionality of our platform has been developed with a view to improving business efficiency and productivity for SMBs.

Innovative Marketing Approach. We believe a key element of our AppFolio Business System is our efficient and targeted go-to-market strategy across our verticals. We employ sophisticated online marketing techniques, including content marketing, search engine optimization, or SEO, and search engine marketing, or SEM, industry thought leadership and education, and participation at customer and industry events, which are used by our sales development team to further nurture potential sales leads. Customer ‘word of mouth’ marketing, reviews and testimonials are also leveraged throughout the marketing and sales process. We then use thoughtful in-app messaging to remind existing customers of our Value+ services at natural points in their workflow, making it easy for our customers to become informed about and increase their adoption and usage of new Value+ services.

Efficient Sales Process. Based on the foundation created by our marketing programs and sales development team, we are able to quickly build relationships with potential customers, assess their business challenges and demonstrate the

benefits of our software solutions. Following on-boarding of our core solution, our sales team identifies specific Value+ services that enable our customers to further streamline and grow their businesses. Our transparent pricing model is designed to simplify the sales process by pricing subscriptions in a uniform manner based on the size of our customers' businesses.

Customer Service as a Partnership. Our customer service team partners with our customers to assist them with on-boarding and help ensure they are optimally using our software solution early in their relationship with us. We believe

this process is critical to our customers' success and plays an important role in customer retention. We also provide ongoing training and support, and regularly provide advice on best practices. Our customer service is an essential component of our AppFolio Business System, serving to deepen our relationships with our customers, maximize the value of our software solutions for their businesses, and encourage word-of-mouth referrals from satisfied customers.

- Customer Feedback Loop. We are committed to listening to, understanding and anticipating our customers' business challenges as the foundation for our product management team to determine and set development priorities. We regularly track customer sentiment and gather feedback at key milestones throughout the customer lifecycle. Our agile, team-based engineering approach and continual integration of customer feedback allows us to release frequent updates to our software solutions quickly and seamlessly.

These components of our AppFolio Business System strengthen our brands and customer loyalty, often resulting in customer promotion and feedback that we then leverage in developing, marketing and selling our software solutions across our targeted verticals.

Our Solutions

We provide SMBs with cloud-based business management software solutions that are designed and developed with our customers' industry-specific business needs in mind.

- All-in-One System. Our core solutions have been designed and developed to suit the specific workflows of SMBs in our targeted verticals. We believe that, by focusing on specific industries, we are better able to provide our customers with broad functionality that meets their key business needs and eliminates their need for a myriad of disparate point solutions. Our vision for each vertical software solution includes fully integrated functionality that provides a single system of record to automate routine processes and a system of engagement to optimize business interactions among our customers and their clients and vendors.
- Essential Value+ Services. Our software solutions include optional, but often mission-critical, Value+ services that our customers can adopt to enhance our core solutions. These services range from upfront professional website design to ongoing high-volume transactional services, such as electronic payment services, in addition to industry-specific services, such as resident screening, for our property manager customers.

Modern and Secure Cloud-Based Solutions. We have designed and developed our software solutions on a modern cloud-based platform, allowing for rapid and cost-effective deployment of our enterprise-class software solutions and frequent updates to help ensure our software solutions incorporate the latest technological advances and adapt to industry trends.

Built for Any Device, Anytime, Anywhere. We recognize that SMBs handle multiple responsibilities that require them to be available 24/7, and they demand flexible software solutions that are compatible with the laptops, tablets and smartphones they already own to allow them to work at any time and from anywhere. Our software solutions are designed to enable users to move seamlessly from one device to another, to run on multiple operating systems and to launch in a variety of browsers.

User-Friendly Interface. We invest significant time and resources to understand and watch customers interact with our software as they accomplish daily tasks. This allows us to design and build functionality that results in an intuitive and user-friendly customer experience. We have found that our users are often able to benefit immediately from our software solutions with little to no training.

- Ever-Evolving Functionality. We direct our investment in research and product development based on our market validation findings and customer feedback loop, which inform the development of new core functionality and Value+ services that are directly relevant to our customers' businesses and industry trends.
- Vertical Data Analytics. As a vertical cloud-based solution provider, we are uniquely positioned to capture data across our customer base, forming a new source of industry-specific business data. Our customers benefit from having access to a wide variety of customizable business performance management reports that aggregate industry benchmarking data and provide optimization opportunities.

Benefits of Our Solutions

Benefits to Our SMB Customers. Our cloud-based business management software solutions enable our customers to eliminate manual processes and collapse a myriad of point solutions into a single system of record and system of engagement. Our software solutions facilitate the automation of recurring transactions, enable seamless communication with multiple stakeholders and provide various reports and analytics that combine to produce tangible time savings, reduced expenses and increased revenue for our customers.

Benefits to Clients of SMBs. Our software solutions help ensure clients of SMBs experience high quality professional service, improved responsiveness and easy access to useful information. Clients of SMBs are able to interact with the owners and managers of SMBs through our intuitive, consumer-friendly interfaces and to complete a variety of tasks online.

Benefits to Vendors of SMBs. Our software solutions enable vendors of SMBs to streamline transactions with the owners and managers of SMBs by automating processes and facilitating communications.

Our Growth Strategy

Our growth strategy is to provide increasingly valuable cloud-based business management software solutions to SMBs within each specific vertical we choose to target. We have managed, and plan to continue to manage, our business towards the achievement of long-term growth that we believe will positively impact long-term stockholder value, and not towards the realization of short-term financial or business metrics, or short-term stockholder value. Key components of growth strategy include:

Maintain Product and Technology Leadership. We have made, and will continue to make, significant investments in research and product development to expand our core functionality and add new Value+ services in existing and/or new vertical markets. We intend to continue using our disciplined market validation techniques and close relationships with our customers as a key source of feedback to inform and direct our product roadmap. We may also choose to acquire technologies to accelerate our time-to-market for certain functionality or entry into adjacent markets or new verticals.

Keep Our Existing Customers Happy. Customer success is essential to our long-term success. We place significant emphasis on customer service to differentiate our software solutions from competing products and this will continue to be a critical component of our business strategy in the future. We do not separately charge our customers for ongoing training and support, which we believe is a key factor in retaining our existing customers and deepening their understanding of our core functionality and Value+ services. We believe that maintaining our focus on customer satisfaction will drive greater adoption and utilization of our software solutions over time.

Expand Adoption and Use By Existing Customers. We intend to expand our core functionality and add new Value+ services to meet the evolving needs and requirements of our customers in each vertical market in which we participate. We believe that our customers will have the opportunity to invest newly available resources to grow their businesses as they save time and money using our software solutions. As our customers grow, we expect they will use our technology to manage their larger businesses on our platform and increasingly adopt and use additional Value+ services.

Target New Customers. We plan to grow our customer base with our sales and marketing programs, including evolving industry thought leadership and education, and the referral power of satisfied customers promoting our software solutions within our targeted verticals. We believe that the market for cloud-based business management software is large and generally underserved both within the industries in which we currently operate and the broader SMB market. We believe that our prominent online presence and efficient sales and marketing infrastructure will continue to attract new customers in our targeted verticals.

Enter New Adjacent Markets. We currently participate in a number of markets within the property management vertical and are constantly evaluating adjacent markets in both of our current verticals based on our deliberate market validation strategy and customer feedback. We firmly believe that, while we are continuously developing our software solution within one market, we can apply certain relevant product enhancements and learnings from that market as we extend our platform into each successive adjacent market.

Expand into New Verticals. We consistently review potential opportunities to expand into additional vertical markets. In that regard, we enforce a disciplined approach to growth by using market validation techniques to assess the scope

and nature of business challenges in any potential new vertical, as well as the likelihood that SMBs may purchase a cloud-based solution to solve their problems in that vertical, and their potential spend on such solutions. Any new

vertical also must fit within our overall business strategy, including our management team's assessment of available alternatives, such as the number and size of potential adjacent market opportunities, and the relative risk and return of these opportunities.

AppFolio Technology Platform

We have developed a common technology platform that enables us to create business management software solutions for SMBs within our targeted verticals. Our suite of applications integrated within our core solution spans many of our customers' most critical business needs by providing them with a system of record and a system of engagement. In conjunction with our core solution, we offer a number of Value+ services, which currently consist of website services, electronic payment services, background and credit checks, insurance services, contact center services, lead generation services and debt collection services. We have built our platform using a modern cloud-based architecture, and our software solutions are designed to run on any device and are compatible with any operating system. As a result, our customers' data is available at any time and from any location.

Products - AppFolio Property Manager

Core Functionality

Our property management software solution provides small and medium-sized property managers (including both third-party managers and owner-operators) with a multi-faceted solution for their operational requirements. We built APM from the ground up based on our analysis of the industry and input directly from property managers. APM includes the following core functionality:

- Powerful Accounting Software. APM provides integrated accounting software specifically designed for property managers, including accounts payable, accounts receivable, trust accounting, Form 1099 creation, check printing, automatic bank reconciliation and ratio utility billing to calculate a resident's share of monthly utility costs based on predetermined allocations.

Data-Driven Management. Unlimited storage allows all data to be centralized in APM, making it available to property managers on-demand through our dynamic search capabilities. APM also allows property managers to better understand and track their business performance through property-level budgets and many customizable reports covering accounting details, property details, and resident and vendor information.

- Effective Online Marketing. Our tenant vacancy tracking software capitalizes on property data centralized in APM to streamline the listing process. In just a few clicks, property managers can manage listings on their own websites and make automatic feeds available to a wide variety of third-party listing sites, dramatically increasing the visibility of listings. Our core functionality also improves the quality of listings by allowing property managers to embed YouTube videos and use our professionally formatted HTML code for listings on third-party websites. All vacancy listings and tasks are then consolidated in real time to reflect the status of a property manager's current vacancies, with detailed metrics showing how vacancy rates are affected by changes in rent or marketing.
- Seamless End-to-End Lease Processing. APM provides a mobile-friendly online leasing solution that allows prospective residents to complete online rental applications from the vacancy listings and upload photographs of their drivers licenses and other important documents. If approved, the property manager can generate a lease agreement pre-populated with the applicant's data that can be electronically signed by the new resident in real time. Our online lease template can be customized to create multiple lease agreements for different property types and requirements, including forms required by applicable law. In addition, our lease renewal workflow automatically incorporates designated increases in rent into the relevant documentation.
- Streamlined Resident Communications. Mass emailing capability and text messaging functionality in APM streamline communications and social interactions with residents. Our messaging center facilitates a range of communications from move-in and move-out instructions to invitations to resident events, as well as short, time-sensitive communications, such as maintenance alerts and late rent reminders. Our messaging center allows property managers to personalize communications and interact with property owners and vendors.
- Accessible Property Owner Reporting. APM enables property managers to post to private and secure online owner portals. These postings typically include owner statements, completed work orders and other reports to which owners have on-demand access. Our owner statements are designed to be easy to read and user friendly, providing a helpful

overview of transactions affecting the property in the past month, and facilitating better service by property managers to their clients.

Transparent Property Maintenance. APM's built-in property maintenance software facilitates electronic work orders to vendors for both one-time and recurring tasks, which are organized in real time to provide a snapshot of all past and in-progress work orders. Residents can access tenant portals to submit online maintenance requests, which automatically create work orders upon acceptance by the property manager. This allows property managers to expedite response times, track and edit the status of repairs, and ensure that property issues are addressed in a timely manner.

Convenient Payments to Owners and Vendors. As an alternative to cash or checks, APM enables property managers to make payments to owners and vendors faster and more securely by depositing funds directly into their bank accounts. Like our other payment solutions, this functionality is built into APM so that payments are automatically entered into our accounting software.

Property Inspection on Any Device. Built-in property inspection functionality allows property managers to perform and manage on-site property inspections remotely on their preferred mobile device. Property managers can make notes directly in the application (or use their phone's speech-to-text functionality) and upload related photographs as they walk through the property. APM then generates an inspection report in a fraction of the time it would take to type up handwritten notes and allows property managers to create work orders from flagged inspection items.

Optimized Rent Comparison. RentMatch, our rent comparison tool, quickly analyzes the rental price and characteristics of any appropriate unit and uses data analytics to compare them to actual rental prices of units of similar size and bedroom count in the same geographical area, presenting the results in a user-friendly report.

Variable Functionality for Different Property Types. APM allows property managers to manage single- and multi-family residences, student housing, commercial property, home owners' associations, or mixed real estate portfolios, as well as optional rentable items such as parking spaces or storage. We are continually adding new core functionality, including rent-by-the-bed for student housing and the ability to allocate common area maintenance charges.

Value+ Services

Our Value+ services enable property managers to activate certain optional, but often mission-critical, functionality that is seamlessly built into APM and designed to improve the user experience in a number of significant ways.

Professionally Designed Websites. We collaborate with our customers to deliver and maintain websites that showcase modern and mobile-optimized designs, with unique sites customized for individual properties, including image galleries and floor plans. Our websites are fully integrated with APM's functionality, including but not limited to vacancy postings, payment options, owner portals and maintenance requests. Property managers can track and analyze site traffic and lead generation and identify prospects by evaluating the guest cards on vacancy postings that are filled in by prospective residents.

Electronic Payment Services. Our payments platform provides prospective and current residents with a number of convenient and secure payment options. Prospective residents can pay rental application fees through our secure online rental applications. APM supports ACH payment processing (e-Check) and credit or debit card payments of security deposits and rent through our secure online tenant portals. As an even more secure alternative to cash and money orders, residents can make regular or last-minute Electronic Cash Payments at any 7-Eleven or ACE Cash Express location.

Instant Background and Credit Checks. APM offers instant background screening and credit checks for use during the rental application process. Instead of manually entering or faxing information to third-party service providers, APM allows property managers to simply press a "Screen Now" button upon receipt of a new online rental application and receive an easy-to-read report summarizing the results of a credit check and nationwide eviction and criminal records search. Customers also gain access to, and have the option to contribute to, Experian Rent Bureau rental payment history data, updated every 24 hours, to identify the highest quality residents and reduce the risk of bad debts.

Reliable Insurance Coverage. Property managers are increasingly requiring residents to carry tenant liability insurance to reduce the hassle and expense associated with resident-caused damage. APM facilitates enrollment of residents in a simple, easy-to-understand tenant liability insurance program, and allows property managers to link this service to lease signings and renewals and easily track resident compliance. Our tenant liability insurance program seeks to provide residents with a cost-effective, integrated solution that provides property managers with a competitive

advantage when marketing their services to owners.

24/7 Maintenance Contact Center. APM's contact center is manned 24 hours a day, 7 days a week, by professionally trained agents. These agents can act as an extension of the property manager's office to resolve or route incoming maintenance requests. Our answering service is designed to work seamlessly with APM's property maintenance software. APM agents are equipped to enter non-emergency work orders directly into APM for the property manager's approval and dispatch vendors immediately in case of an emergency.

Premium Leads. APM customers have the option to upgrade a vacancy listing to premium status, syndicating it instantly to dozens of pay-to-list websites, including featured placement on most sites. There is no need to maintain separate contracts or sign up for individual listing sites, and the property manager only pays for verified leads signifying unique, real people who are interested in the subject property.

Debt Collection Services. APM offers its property manager customers the ability to utilize a nationwide contingency-based debt collection service provided by a nationally licensed third party partner. Because the relevant data is stored in APM, property managers can easily and electronically submit past due tenant debt from their APM database directly to the collections service for processing.

Products - MyCase

Core Functionality

Our legal software solution is designed to assist solo practitioners and small law firms with administering their practice and managing their case load. We acquired MyCase in 2012 and are continuing to expand its functionality by leveraging our AppFolio Business System, including our experience gained in the property management vertical, to advance our software solution in the legal vertical. MyCase includes the following core functionality:

On-the-Go Time Tracking. MyCase allows attorneys to enter billable hours on their preferred mobile device, automatically linking time entries to the appropriate case or matter. Lawyers are able to handle multiple court appearances, meetings and other interactions without having to recreate their days after the fact. MyCase can also be used to track non-billable entries to monitor the performance and efficiency of flat-fee arrangements and contributions to pro bono work.

Flexible Legal Billing Software. MyCase's legal billing software can be used to generate detailed trust account balances and a wide variety of reports to track productivity and other firm metrics. It can also quickly pull unbilled time and expenses or flat fee balances into a professionally formatted invoice, which can be customized with the law firm's logo. Attorneys can use our Payment Plan Generator to easily define a payment schedule for a client with flexible due dates and balances. Our QuickBooks integration functionality provides a one-way sync of detailed accounting data into QuickBooks, ensuring consistency across accounting software.

Secure Client Portals. MyCase's integrated client portals provide clients with on-demand access to a variety of information, including invoices and sensitive and privileged communications, with the knowledge that such correspondence is private and secure and better protected than messages sent over unsecure email. Our client portals have a modern interface similar to that of social networking sites, with real-time activity streams to provide an overview of recent developments and a comment stream associated with uploaded items shared with clients, who get automatic notifications of updates.

Automated Organizational Tasks. MyCase offers broad functionality to facilitate better organization of cases and matters, including centralized contacts, tasks, calendars and reminders accessible by the entire firm. Our workflow software allows lawyers to automate processes for routine tasks tailored to the type of case or matter. Calendars and reminders are synchronized in real time across all devices to assist the entire team with time management, and colleagues and clients receive notifications when calendar events are added. Practitioners can also link calendar events to the applicable case or matter to track associated billable hours.

Robust Document Management and Collaborative Assembly. MyCase provides a robust legal document management system, which, together with our unlimited storage and drag-and-drop upload tool, allows law firms to organize correspondence and other documentation in a searchable, centralized firm library. Our cloud-based platform allows colleagues to collaborate in drafting new documents, which can be assembled quickly and easily by capitalizing on our customizable templates.

Value+ Services

We currently offer two optional, but frequently essential, services to our law firm customers.

Professionally Designed Websites. Our professionally designed websites are fully integrated with MyCase so that practitioners and their clients can easily login to the site to access case and matter information, communicate and manage bills. Our websites are geared towards improving the effectiveness of law firm marketing and building a mobile presence. We work with our law firm customers to build their brand by tailoring website content, providing professional images, creating a logo and purchasing their unique domain.

Electronic Payment Services. MyCase enables practitioners to accept credit or debit cards online for a simple flat-rate merchant processing fee. Clients can easily view invoices in the secure Client Portal and submit payment from any device. In addition, by linking operating and trust accounts, practitioners can accept online payment of retainers and other amounts directly into these accounts.

Our Customers

As of December 31, 2016, we had 10,038 property manager customers and 8,135 law firm customers. Our property manager customers include third-party managers and owner-operators, managing single- and multi-family residences, commercial property, home owners' associations and student housing, as well as mixed real estate portfolios. Our property manager customers typically manage portfolios ranging from 50 to 3,000 units. Our customers in the legal vertical are generally solo practitioners and small law firms with less than 20 lawyers. No customer represented 10% or more of our total revenue, and our property manager customers represented more than 90% of our revenue for our fiscal year ended December 31, 2016.

Our Culture and Employees

We believe our people are at the heart of our success and our customers’ success, and have worked hard not only to attract and hire quality individuals but also to nurture and develop our valuable human resources. We believe in the strong team we have cultivated, particularly in our deep bench of leaders who continue to execute our strategic plans and encourage innovation across the organization. We further believe that our company culture, driven by a dedication to the following six core values, provides us with a significant competitive advantage:

Simpler Is Better

Great, Innovative Products Are Key To A Great Business

Great People Make A Great Company

Listening To Customers Is In Our DNA

Small, Focused Teams Keep Us Agile

We Do The Right Thing Because It’s Good For Business

As of December 31, 2016, we had 626 employees, and we consider our relationship with them to be good. We also hire temporary employees and consultants, and feel similarly about our relationships with them. None of our employees is represented by a labor union or covered by a collective bargaining agreement.

Technology and Operations

Data Security and Availability

We use Ruby-on-Rails as our web application framework for both APM and MyCase. Our software solutions run on a combination of both public and private cloud infrastructure, consisting of both our own servers and Amazon’s Elastic Compute Cloud, or EC2, platform. Our servers are located in state-of-the-art data centers operated by third-party service providers. Physical security at these facilities includes a variety of access controls, including electronic keycards, pin codes, biometric hand scans and mantraps, and policing by high resolution, motion sensitive video surveillance. These facilities provide redundant power and a system of heating, ventilating and air conditioning, as well as fire-threat detection and suppression. We utilize a system of redundant routers, switches, server clusters and back-up systems to help ensure high availability. Amazon is widely recognized for operating state-of-the-art, highly available data centers.

With respect to Internet security, sensitive data, such as passwords, Social Security and tax identification numbers, are encrypted before being written to disk. In addition, all sensitive data is encrypted both in transit and at rest. Data is backed up

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using Amazon's Simple Storage Service, or S3, providing high durability, and we also perform regular backups of all customer data. We evaluate our Internet security regularly, including through third-party penetration testing.

In addition, our software solutions allow our customers to define roles that provide different levels of access to users, allowing them to view and modify specific items depending on their role. Supervisors can distribute work to on-site staff in a secure and controlled environment, while leadership retains visibility across the entire system.

Research and Product Development

We entrust product design, development and testing to our team of engineers, who coordinate closely with our product management team to launch new core functionality and Value+ services. Our engineers are organized in smaller groups to foster agility and continued innovation in responding to the evolving needs of our customers. We leverage a collaborative, team-based and test-driven approach to engineering to release new code frequently. We believe that it is easier for our customers to adjust to these continuous updates to our software solutions, which incrementally change and improve their user experience, than it is to adapt to infrequent, but more drastic, upgrades of legacy on-premise software.

We rely heavily on input from our customers in developing products that meet their needs and anticipate developments in their respective industries. Our product management team leads our research and market validation efforts and provides guidance to management and our engineering team based on our collective domain expertise and in-depth knowledge and understanding of our customers. As a result, our product management team engages regularly with customers, partners and other industry participants, as well as our customer service and sales and marketing organizations. Our product management team manages our development projects generally and serves to align separate functions within the company with a single strategic vision.

Our research and product development expenses were $12.6 million, $9.6 million and $6.5 million for the years ended December 31, 2016, 2015 and 2014, respectively.

Sales and Marketing

We leverage a modern marketing approach along with marketing automation technology to build brand recognition and our reputation as an industry leader in our targeted verticals.

We participate in and drive industry thought leadership and education with both online and offline activities. We attend, host and present at a number of industry events and support educational opportunities in the form of trade shows, conferences and webinars across the United States. We host informational lunches and networking opportunities in key cities in the form of "Connects" (formerly, "Meet Ups"), which bring together existing and prospective customers. Our online user forums facilitate discussions with other industry participants and serve as a resource for tips on using our platform and best practices. We also make a number of valuable educational resources available for free through our industry partners and on our industry websites, such as PropertyManager.com and our blogs.

We use a variety of in-bound marketing techniques to promote our software solutions, including content marketing, SEO, SEM, social media and advanced digital advertising tactics. Our sales development team acts in partnership with our in-bound marketing efforts to reach potential customers, generate additional sales opportunities and speed the time from evaluation to close. Our sales representatives then assist prospective property manager customers as they evaluate APM, while prospective law firm customers generally sign up for a 30-day free trial on a self-service basis (with additional support from a live sales development representative as needed).

Our sales team works closely with our marketing organization to find and acquire new customers as well as expand adoption and use by existing customers. We have a metrics-driven sales culture with a focus on early indicators that lead to strong pipeline creation. We leverage technology and specialization of resources along with an emphasis on continued training and development to maximize the productivity and speed the ramp time for each sales representative. Our interactive sales methodology allows the sales team to quickly build relationships, assess the customer's business challenges, and demonstrate the benefits of our core functionality and Value+ services.

Throughout the customer relationship, we continue to promote adoption and usage of our Value+ services in a variety of channels, including email, webinars, training, sales outreach and from within our software solution via in-app messaging. While APM and MyCase customers are using our core solutions, in-app messaging puts additional Value+ services directly in their workflow. This makes it easy for customers to find out about additional Value+ services in an

unobtrusive manner and begin to adopt those services that are useful to their business. Our Value+ sales team then works in tandem with our marketing organization to further increase adoption and usage of our Value+ services.

Customer Service

Our success is based on long-term customer retention, not a one-time sale, and we partner with our customers throughout the life of the customer relationship to help them navigate their digital transformation. We design our software solutions to be simple and easy to switch to, set up, use and manage. We offer unlimited training and support across our software solutions at no extra charge. We pride ourselves on being customer-centric and strive to educate our customers on the additional core functionality and Value+ services they can use to improve business efficiency and productivity.

Our on-boarding team strives to ensure that customers are prepared to run their businesses on our platform and provide the best on-boarding experience in the industry. Based on our assistance with data migration, we are able to provide valuable insights into data integrity and work diligently with our customers to help resolve any issues in their underlying business processes. We also assist our customers with the configuration of our platform for particular property types or cases. We provide a dedicated team throughout the on-boarding process and ongoing planning thereafter, including compliance with best practices. Our Value+ team also includes a number of employees focused on guiding our customers through the adoption of our Value+ services.

Our software solutions are designed to be intuitive; nevertheless, we provide a variety of training options to assist with implementation and adoption to help ensure maximum value for our customers. Our instructors offer several live-streamed training courses each week, and we also make available recorded training courses that can be accessed on demand. Our training is designed to provide product overviews for those in the process of converting to our software solutions, as well as in-depth, step-by-step instructions and ongoing education for those seeking to leverage greater functionality.

Our cloud-based platform allows us to fix issues quickly and to continuously improve our customers' experience through ongoing updates to our software solutions. However, when issues and questions do arise, we strive to ensure that a real person is available to respond to a customer's concerns quickly and intelligently.

Throughout the customer relationship, our customer loyalty team proactively engages with our customers to facilitate our customers' success. Similarly, our Value+ team includes employees focused exclusively on expanding Value+ service adoption and usage by new and existing customers and providing expertise with respect to related services.

Competition

The overall market for business management software is global, highly competitive and continually evolving in response to changes in technology, operational requirements, laws and regulations. While we focus on providing software solutions to SMBs in each of our targeted verticals, we compete with other vertical cloud-based solution providers that serve companies of all sizes and horizontal cloud-based solution providers that offer broad solutions across multiple verticals.

In the property management vertical, our competitors include established vertical software vendors, such as RealPage and Yardi, and we also compete with cloud-based solution providers whose services are geared toward individual landlords with smaller portfolios than those of our targeted customers. In the legal vertical, our competitors include established vertical software vendors, such as Thompson-Reuters and LexisNexis, each of whom offers software solutions to solo practitioners and small law firms, and Clio.

We also see competition from numerous cloud-based solution providers that focus almost exclusively on one or more point solutions. For example, in the property management vertical, we compete with listing services, tenant screening applications and specialists in lease forms. In the legal vertical, we compete with time tracking, legal billing and payment services. Continued consolidation among cloud-based solution providers could lead to significantly increased competition.

We believe the principal competitive factors in each of our vertical markets include the following:

- ease of deployment and use of software solutions and applications;
- total cost of ownership;
- data security and availability;
- breadth and depth of functionality in software solutions and applications;
- nature and extent of mobile interface;
- level of customer satisfaction;

size of customer base and level of user adoption and usage;
brand awareness and reputation;

- ability to innovate and respond to customer needs rapidly;
- domain expertise with respect to our targeted verticals; and
- ability to leverage a common technology platform and business strategy.

We believe that we compete favorably on the basis of these factors and that the domain expertise required for developing, marketing and selling successful software solutions in the property management and legal verticals may hinder new entrants that are unable to invest the necessary resources to develop and deploy software solutions with the same level of functionality as ours.

Intellectual Property

We rely on a combination of patents, copyrights, trademarks, trade secrets, confidentiality procedures and contractual restrictions to establish and protect our proprietary rights in our core solutions and Value+ services. As of January 31, 2017, we had eleven issued U.S. patents that directly relate to our technology and expire between 2026 and 2033, and another for which we recently received a Notice of Allowance from the United States Patent and Trademark Office. We intend to pursue additional patent protection to the extent we believe it would be beneficial and cost effective.

We registered “AppFolio,” "MyCase" and "RentLinx" and certain other marks as trademarks in the United States and several other jurisdictions. We also filed trademark applications and renewals in the United States and certain other jurisdictions and will pursue additional trademark registrations to the extent we believe it would be beneficial and cost effective. We are the registered holder of a variety of domestic and international domain names that include “appfolioinc.com,” “appfolio.com,” “mycase.com,” “propertymanager.com” and similar variations. We also license software from third parties for use in our solutions, including open source software and other software available on standard commercial terms.

We control access to our proprietary technology by entering into confidentiality and invention assignment agreements with our employees and contractors and confidentiality agreements with third parties. Despite our precautions, it may be possible for unauthorized third parties to copy our software solutions and use information that we regard as proprietary to create products and services that compete with ours.

Corporate Information

We were formed in 2006 as a Delaware limited liability company and converted to a Delaware corporation in 2007. Our principal executive offices are located at 50 Castilian Drive, Goleta, California 93117, and our telephone number is (805) 364-6093. Our corporate website is www.appfolioinc.com. The information contained on or accessed through our website does not constitute part of, and is not incorporated by reference into this Annual Report. References to our website address in this Annual Report are inactive textual references only.

“AppFolio,” “MyCase,” "RentLinx," the AppFolio logo, the MyCase logo, and other trademarks and trade names of AppFolio, MyCase and RentLinx appearing in this Annual Report are our property. All other trademarks or trade names appearing in this report are the property of their respective owners. Solely for convenience, the trademarks and trade names in this report are referred to without the ® and ™ symbols. We do not intend our use or display of the trademarks, trade names or service marks of other parties to imply a relationship with, or endorsement or sponsorship of us by, such other parties.

Available Information

We file annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, as well as amendments to those reports pursuant to Sections 13(a) and 15(d) of the Exchange Act. We also file proxy statements and information statements pursuant to Section 14 of the Exchange Act. The public may obtain these filings at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549 or by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website at www.sec.gov that contains the reports, proxy and information statements, and other information that we file with or furnish to the SEC electronically. Copies of the reports, proxy statements and other information may also be obtained, free of charge, electronically through our corporate website at www.appfolioinc.com as soon as reasonably practical after we file such material with, or furnish it to, the SEC.

ITEM 1A. RISK FACTORS

An investment in our Class A common stock involves risks. You should carefully consider the risks and uncertainties described below, together with all of the other information in this Annual Report, as well as in our other public filings with the SEC, before making an investment decision. If any of the following risks are realized, our business, financial condition, and operating results could be materially and adversely affected. In that case, the trading price of our Class A common stock may decline, and you could lose all or part of your investment. Furthermore, additional risks and uncertainties of which we are currently unaware, or which we currently consider to be immaterial, could have a material adverse effect on our business.

Please be advised that certain of the risks and uncertainties described below contain "forward-looking statements." See the section of this Annual Report entitled "Cautionary Note Regarding Forward-Looking Statements" for additional information.

Risks Related to Our Business and Our Industry

If we are unable to enter new verticals, or if our software solution for any new vertical fails to achieve market acceptance, our operating results could be adversely affected and we may be required to reconsider our growth strategy.

Our growth strategy is dependent, in part, on leveraging our AppFolio Business System, including our common technology platform, to expand into new verticals. However, we may be unable to identify new verticals that meet our criteria for selecting industries that cloud-based solutions are ideally suited to address. In addition, our market validation process may not support entry into selected verticals due to our perception of the overall market opportunity or of the willingness of market participants within those verticals to adopt our software solutions. Further, instead of pursuing new verticals, we may prefer for various reasons to pursue alternative growth strategies, such as entry into markets that are adjacent to the markets in which we currently participate within our existing verticals, or the development of additional products or services for our existing markets.

Even if we choose to enter new verticals, our market validation process does not guarantee our success in any particular vertical. We may be unable to develop a software solution for a new vertical or, in the event that we enter a new vertical by way of a strategic acquisition, we may be unable to leverage the acquired software solution in time to take advantage of the identified market opportunity, and any delay in our time-to-market could expose us to additional competition or other factors that could impede our success. In addition, any software solution we develop or acquire for a new vertical may not provide the functionality required by potential customers and, as a result, may not achieve widespread market acceptance within the new vertical. To the extent we choose to enter new verticals, whether organically or via strategic acquisition, we may invest significant resources to develop and expand the functionality of our software solutions to meet the needs of customers in those verticals, which investments will occur in advance of our realization of revenue from them. If we elect not to enter new verticals in the future, or if we choose to enter new verticals and do so without achieving market acceptance for our software solutions, our reputation could be harmed, our operating results could be adversely affected, and we may be required to reconsider our growth strategy.

In addition, while we expedited our entry into the legal vertical through the acquisition of MyCase in 2012, our practice and case management solution is in an earlier stage of development than APM, our property management solution, and we are at an earlier stage in the process of expanding the core functionality and Value+ services associated with our legal software. We face significant competition in the legal market from both vertical software vendors and cloud-based solution providers that offer one or more point solutions. There can be no assurance that we will be able to achieve market acceptance for our legal software at or near the levels achieved by our property management software. The success of our vertical market strategy depends, in part, on our ability to continue to significantly increase the number of our law firm customers and the revenue derived from them, and our failure to achieve these objectives could have an adverse impact on our operating results.

We have a limited operating history and have incurred significant operating losses. As a result of continuing investments across our organization to grow our business, we expect our financial results may fluctuate significantly for the foreseeable future.

We were formed in 2006 and launched our first product, APM, in 2008. We expedited our entry into the legal vertical through the acquisition of MyCase in 2012. As a result, we have a limited operating history and limited experience selling our software solutions in two continually evolving vertical markets, especially within the legal vertical. These and other factors combine to make it more difficult for us to accurately forecast our future operating results, which in turn makes it more difficult for us to prepare accurate budgets and implement strategic plans. We expect that this uncertainty will continue to exist in our business for the foreseeable future, and will be exacerbated to the extent we introduce new functionality, or enter adjacent markets or new verticals.

We have incurred net losses in each fiscal period since our formation. We incurred net losses of $8.3 million, $15.7 million

and $8.6 million for the years ended December 31, 2016, 2015 and 2014, respectively. These losses reflect the substantial investments we have made across our organization to develop our software solutions and capitalize on our market opportunity. In order to implement our business strategy, we intend to continue to make substantial investments in, among other things:

- our research and product development organization to enhance the ease of use and functionality of our software solutions by adding new core functionality, Value+ services and other improvements to address the evolving needs of our customers, as well as to develop new products for adjacent markets and new verticals;
- our customer service organization to deepen our relationships with our customers, assist our customers in achieving success through the use of our software solutions, and promote customer retention;
- our sales and marketing organization, including expansion of our direct sales organization and marketing programs, to increase the size of our customer base, increase adoption and utilization of new and existing Value+ services by our new and existing customers, and enter adjacent markets and new verticals;
- maintaining and expanding our technology infrastructure and operational support, including data center operations, to promote the security and availability of our software solutions, and support our growth;
- our general and administrative functions, including hiring additional finance, IT, human resources, legal and administrative personnel, to support our growth and assist us in achieving and maintaining compliance with public company reporting and compliance obligations;
- the expansion of our existing facilities, including leasing and building out additional office space, to support our growth and strategic expansion; and
- our continued strategic efforts to identify and expand into key adjacent and new vertical markets.

As a result of our continuing investments to grow our business in these and other areas, we expect our expenses to increase significantly, and we do not expect to be consistently profitable, if we are profitable at all, for the foreseeable future. Even if we are successful in growing our customer base and increasing revenue from new and existing customers, we may not be able to generate additional revenue in amounts that are sufficient to cover our expenses. We may incur significant losses in a particular period for a number of reasons, and may experience significant fluctuations in our operating results from period to period, including as a result of the other risks and uncertainties described elsewhere in this Annual Report. We cannot assure you that we will achieve profitability in the near term or that, if we do become profitable, we will sustain profitability over any particular period of time. Any additional operating losses will have a negative impact on our stockholders' equity.

We manage our business towards the achievement of long-term growth, which may not be consistent with the short-term expectations of some investors, and may cause significant fluctuations in our quarterly results.

We plan to continue to manage our business towards the achievement of long-term growth that we believe will positively impact long-term stockholder value, and not towards the realization of short-term financial or business metrics, or short-term stockholder value. If opportunities arise that might cause us to sacrifice our performance with respect to short-term financial or business metrics, but that we believe are in the best interests of our stockholders, we will take those opportunities.

We focus on growing our customer base by launching new and innovative core functionality and Value+ services to address our customers' evolving business needs, developing new products for adjacent markets and additional verticals, and improving the experience of our users across our targeted verticals. We prioritize product innovation and user experience over short-term financial or business metrics. We will make product decisions that reduce our short-term operating results if we believe that these decisions are consistent with our strategic objective to achieve long-term growth. These decisions may not be consistent with the short-term expectations of some investors, and may cause significant fluctuations in our operating results from period to period. In addition, notwithstanding our intention to make strategic decisions that positively impact long-term stockholder value, the decisions we make may not produce the long-term benefits we expect.

Our executive officers, directors and principal stockholders control a majority of the combined voting power of our outstanding capital stock. As a result, they are able to exercise significant influence and control over the establishment and implementation of our future business plans and strategic objectives, as well as control all matters submitted to our stockholders for approval. These persons may manage our business in ways with which you disagree and which

may be adverse to your interests.

Actual or perceived security vulnerabilities in our software solutions, breaches of our security controls or other unauthorized access to our customers' data could result in liability or reputational harm to us, or cause us to lose customers, any of which could harm our business and operating results.

In providing our software solutions, we store and transmit large amounts of our customers' data, including sensitive and proprietary data. Our software solutions are typically the system of record and system of engagement for all or a portion of our customers' businesses, and the data processed through our software solutions is critical to their businesses. Cyber-attacks and other malicious Internet-based activities continue on a regular basis, as evidenced by the recent targeting of a number of high profile companies and organizations. As our business grows, the number of users of our software solutions, as well as the amount of information we store, is increasing, and our brands are becoming more widely recognized. We believe these factors combine to make us an even greater target for this type of malicious activity. Techniques used to sabotage, or to obtain unauthorized access to, systems or networks change frequently and generally are not recognized until launched against a target. Therefore, despite our significant efforts to keep our systems and networks up to date, we may be unable to anticipate these techniques, react in a timely manner, or implement adequate preventive measures, any of which may expose us to a risk of loss, litigation and potential liability. In addition, some of our third-party partners also collect information from transactions with our customers, and these third parties are subject to similar threats of cyber-attacks and other malicious Internet-based activities.

If our security measures, or the security measures of our third-party partners, are breached as a result of negligence, wrongdoing or malicious activity on the part of our employees, our partners' employees, our customers' employees, or any third party, or as a result of any error, product defect or otherwise, and this results in the disruption of the confidentiality, availability or integrity of our customers' data, we could incur liability to our customers and to individuals or organizations whose information was being stored by our customers, as well as fines from payment processing networks and regulatory action by governmental bodies. If we experience a widespread security breach, we cannot be certain that our insurance coverage will be sufficient to compensate us for liabilities actually incurred or that insurance will continue to be available to us on reasonable terms, or at all. In addition, any breaches of our security controls or other unauthorized access to our customers' data could result in reputational damage, adversely affect our ability to attract new customers and cause existing customers to reduce or discontinue the use of our software solutions, any of which could harm our business and operating results. Furthermore, the perception by our current or potential customers that our software solutions could be vulnerable to security breaches, even in the absence of a particular problem or threat, could reduce market acceptance of our software solutions and cause us to lose customers.

Service outages and other performance problems associated with our technology infrastructure could harm our reputation, adversely affect our ability to attract new customers and cause us to lose existing customers.

We have experienced significant growth in the number of users and the amount of data that our technology infrastructure supports, and we expect this growth to continue. We seek to maintain sufficient excess capacity in our technology infrastructure to meet the needs of all of our customers, including to facilitate the expansion of existing customer deployments and the provisioning of new customer deployments. In addition, we need to properly manage our technology infrastructure in order to support version control, changes in hardware and software parameters, and the evolution of our software solutions. However, the provision of new hosting infrastructure requires significant lead-time.

We have experienced, and may in the future experience, website disruptions, service outages and other performance problems with our technology infrastructure. These problems may be caused by a variety of factors, including infrastructure changes, power or network outages, fire, flood or other natural disasters affecting our data centers, human or software errors, viruses, security breaches, fraud or other malicious activity, spikes in customer usage and distributed denial of service issues. In some instances, we may not be able to identify the cause or causes of these service outages and performance problems within an acceptable period of time. If our technology infrastructure fails to keep pace with the increased number of users and amount of data, or if we are unable to avoid service outages and performance problems, or to resolve them quickly, it could adversely affect our ability to attract new customers, result in the loss of existing customers and harm our reputation, any or all of which could adversely affect our business and operating results.

Evolution and expansion of our electronic payment services may subject us to additional risks and regulatory requirements.

The evolution and expansion of our electronic payment services may subject us to additional risks and regulatory requirements, including laws and regulations governing money transmission and anti-money laundering. These requirements vary throughout the markets in which we operate, and several jurisdictions lack clarity in the application and interpretation of these rules. Our efforts to comply with these rules could require significant management time and effort, as well as significant expenditures, and will not guarantee our compliance with all regulatory requirements, especially given that the applicable regulatory frameworks are constantly changing and subject to evolving interpretation. While we maintain a compliance program focused on applicable laws and regulations throughout our applicable industries, there is no guarantee that we will not be subject to fines, penalties or other regulatory actions in one or more jurisdictions, or be required to adjust our business practices to accommodate

future regulatory requirements.

We face a number of risks in our payment processing business that could adversely affect our business or operating results.

In connection with our electronic payment services, we process payments and subsequently submit these payments to our customers after varying clearing times established by us. These payments are settled through our sponsoring clearing bank and, in the case of electronic funds transfers, or EFTs, through our Originating Depository Financial Institutions, or ODFIs, pursuant to agreements with one or more national banking institutions that we may contract with from time to time. Our electronic payment services subject us to a number of risks, including, but not limited to:

- liability for customer costs related to disputed or fraudulent transactions if those costs exceed the amount of the customer reserves we have during the clearing period or after payments have been settled to our customers;
- electronic processing limits on the amounts that any single ODFI, or collectively all of our ODFIs, will underwrite;
- our reliance on sponsoring clearing banks, card payment processors and other electronic payment partners to process electronic transactions, especially where those partners are highly scrutinized and regulated themselves;
- failure by us, our partners or our customers to adhere to applicable laws, regulations and standards that may legally or contractually apply to the provision of electronic payment services;
- continually evolving and developing laws and regulations governing money transmission and anti-money laundering, the application or interpretation of which is not clear in some jurisdictions;
- incidences of fraud, security breaches, errors, defects, failures, vulnerabilities or bugs in our electronic payments platform, or our failure to comply with required external audit standards; and
- our inability to increase our fees at times when our electronic payment partners increase their transaction processing fees.

If any of these risks related to our electronic payment services were to materialize, our business or operating results could be negatively affected. Although we attempt to structure and adapt our electronic payment services to comply with complex and evolving laws, regulations and standards, our underwriting efforts do not guarantee compliance. In the event that we are found to be in violation of our legal, regulatory or contractual requirements, we may be subject to monetary fines or penalties, cease and desist orders, mandatory product changes, or other liabilities that could have an adverse effect on our operating results.

Additionally, with respect to the processing of EFTs, we are exposed to financial risk. EFTs between our customer and another user may be returned for various reasons such as insufficient funds or stop payment orders. These returns are charged back to the customer by us. However, if we or our sponsoring clearing bank is unable to collect such amounts from the customer’s account (such as if the customer is illegitimate, or if the customer refuses or is unable to reimburse us for the amounts charged back), we bear the risk of loss for the amount of the transfer. While we have not experienced material losses resulting from amounts charged back in the past, there can be no assurance that we will not experience these types of significant losses in the future.

In addition to the foregoing risks associated with our electronic payment services themselves, there is an overarching risk stemming from the potential widespread adoption of quickly evolving financial technology products, including, for example, blockchain or other distributed ledger technologies, that could materially impact the manner in which payments are processed. Such adoption of new disruptive financial technologies could significantly reduce the volume of payments processed by us and our third party partners or change the transaction costs associated with or potential revenue derived from those payments, thereby reducing our revenue and increasing our associated expenses, which could materially impact our business, financial condition, operating results and, ultimately, our stock price.

Errors, defects or other disruptions in our software solutions could harm our reputation, cause us to lose customers, and result in significant expenditures to correct the problem.

Our customers use our software solutions to manage critical aspects of their businesses, and any errors, defects or other disruptions in the performance of our software solutions may result in loss of or damage to our customers’ data and disruption to our customers’ businesses, which could harm our reputation. We provide continuous updates to our software solutions and, while our software updates undergo extensive testing prior to their release, these updates may contain undetected errors when first introduced. In the past, we have discovered errors, failures, vulnerabilities and bugs in our software updates after they have been released, and similar problems may arise in the future. Real or

perceived errors, failures, vulnerabilities or bugs in our software solutions could result in negative publicity, reputational harm, loss of customers, delay in market acceptance of our software solutions, loss of competitive position, withholding or delay of payment to us, claims by customers for losses sustained by them

and potential litigation. In any such event, we may be required to expend additional resources in order to help correct the problem or, in order to address customer service or reputational concerns, we may choose to expend additional resources to take corrective action even where not required. The costs incurred in correcting any material errors, defects or other disruptions could be substantial and there may not be any corresponding increase in revenue to offset these costs. In addition, we may not carry insurance sufficient to compensate us for any losses that may result from claims arising from errors, defects or other disruptions in our software solutions.

Our quarterly results may fluctuate significantly and period-to-period comparisons of our results may not be meaningful.

Our quarterly results, including the levels of our revenue, costs, operating expenses, and operating margins, may fluctuate significantly in the future, and period-to-period comparisons of our results may not be meaningful. Accordingly, the results of any one quarter should not be relied upon as an indication of our future performance. In addition, our quarterly results may not fully reflect the underlying performance of our business. Factors that may cause fluctuations in our quarterly results include, but are not limited to:

our ability to retain our existing customers, and to expand adoption and utilization of our core solutions and Value+ services by our existing customers;

our ability to attract new customers, the type of customers we are able to attract, the size and needs of their businesses, and the cost of acquiring these customers;

the mix of our core solutions and Value+ services sold during the period;

the timing and impact of security breaches, service outages or other performance problems with our technology infrastructure and software solutions;

variations in the timing of sales of our core solutions and Value+ services as a result of trends impacting the verticals in which we sell our software solutions;

the timing and market acceptance of new core functionality, Value+ services and other products introduced by us and our competitors;

changes in our pricing policies or those of our competitors;

the timing of our recognition of revenue;

our ability to convert customers who start their accounts on a free trial into paying subscribers;

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

the amount and timing of costs and operating expenses associated with assessing or entering adjacent markets or new verticals;

the amount and timing of costs and operating expenses related to the development or acquisition of businesses, services, technologies or intellectual property rights, and potential future charges for impairment of goodwill from these acquisitions;

the timing and costs associated with legal or regulatory actions;

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

loss of our executive officers or other key employees;

industry conditions and trends that are specific to the verticals in which we sell or intend to sell our software solutions; and

general economic and market conditions.

Fluctuations in quarterly results may negatively impact the value of our Class A common stock, regardless of whether they impact or reflect the overall performance of our business. If our quarterly results fall below the expectations of investors or any securities analysts who follow our stock, or below any guidance we may provide, the price of our Class A common stock could decline substantially.

Business management software for SMBs is a relatively new and developing market and, if the market is smaller than we estimate or develops more slowly than we expect, our operating results could be adversely affected.

We currently provide cloud-based business management software for SMBs in the property management and legal industries and, as part of our business strategy, we will assess entry into new verticals. While the overall market for cloud-based business management software is rapidly growing, it is not as mature as the market for legacy on-premise software applications. In addition, when compared to larger enterprises, SMBs have not historically purchased enterprise resource planning or other enterprise-wide software systems to manage their businesses due to the cost and complexity of implementing such systems, which generally did not address their industry-specific needs. Furthermore, a number of widely adopted cloud-based solutions have not traditionally targeted SMBs. As a result, many SMBs still run their businesses using manual processes and disparate software systems that are not web-optimized, while others may have invested substantial resources to integrate a variety of point solutions into their organizations to address one or more specific business needs and, therefore, may be reluctant to migrate to a vertical cloud-based solution designed to apply to their entire business. Because we derive, and expect to continue to derive, substantially all of our revenue from sales of our cloud-based business management software to SMBs in our targeted verticals, our success will depend, to a substantial extent, on the widespread adoption by SMBs in these verticals of cloud computing in general and of cloud-based business management software in particular.

The market for industry-specific, cloud-based business management software for SMBs, both generally, and specifically within the property management and legal industries, is evolving and, in comparison to the overall market for cloud-based solutions, is relatively small. The continued expansion of this market depends on numerous factors, including:

- the cost and perceived value associated with cloud-based business management software relative to on-premise software applications and disparate point solutions;
- the ability of cloud-based solution providers to offer SMBs the functionality they need to operate and grow their businesses;
- the willingness of SMBs to transition from their existing software systems, or otherwise alter their existing businesses practices, to migrate their businesses to a vertical cloud-based business management software solution; and
- the ability of cloud-based solution providers to address security, privacy, availability and other concerns.

If cloud-based business management software does not achieve widespread market acceptance among SMBs, our revenue may increase at a slower rate than we expect and may even decline, which could adversely affect our operating results. In addition, it is difficult to estimate the rate at which SMBs will be willing to transition to vertical cloud-based business management software in any particular period, which makes it difficult to estimate the overall size and growth rate of the market for cloud-based business management software for SMBs at any given point in time or to forecast growth in our revenue or market share.

Our estimates of market opportunity are subject to significant uncertainty and, even if the markets in which we compete meet or exceed our size estimates, we could fail to increase our revenue or market share.

Market opportunity estimates are subject to significant uncertainty and are based on assumptions and estimates, including our internal analysis and industry experience. Assessing the market for industry-specific, cloud-based business management software for SMBs is particularly difficult due to a number of factors, including limited available information and rapid evolution of the market. If we had made different assumptions or estimates, our estimates of market opportunity could be materially different.

In addition, even if the markets in which we compete meet or exceed our size estimates, our business could fail to grow in line with our forecasts, or at all, and we could fail to increase our revenue or market share. Our growth, and our ability to serve a significant portion of our target markets, will depend on many factors, including our success in executing our business strategy, which is subject to many risks and uncertainties, including the other risks and uncertainties described elsewhere in this Annual Report.

If we are unable to introduce successful enhancements, including new and innovative core functionality and Value+ services for our existing markets and verticals, or new products for adjacent markets or additional verticals, our operating results could be adversely affected.

The software industry in general, and our targeted verticals in particular, are characterized by rapid technological advances, changing industry standards, evolving customer requirements and intense competition. Our ability to attract new customers, increase revenue from our existing customers, and expand into adjacent markets or new verticals depends, in part, on our ability to enhance the functionality of our existing software solutions by introducing new and innovative core functionality and Value+ services that keep pace with technological developments, and provide functionality that addresses the evolving business needs of our customers. In addition, our growth over the long term depends, in part, on our ability to introduce new products for adjacent markets and additional verticals that we identify through our market validation process. Market acceptance of our current and future software solutions will depend on numerous factors, including:

- the unique functionality of our software solutions and the extent to which our software solutions meet the business needs of our customers;
- the perceived benefits and security of our cloud-based business management software solutions relative to on-premise software applications or other competitive products;
- the pricing of our software solutions relative to competitive products;
- perceptions about the security, privacy and availability of our software solutions relative to competitive products;
- time-to-market of the updates and enhancements to our core functionality, Value+ services and new products; and
- perceptions about the quality and responsiveness of our customer service organization.

If we are unable to successfully enhance the functionality of our existing software solutions, including our core solutions and Value+ services, and develop new products that gain market acceptance in adjacent markets and additional verticals, our revenue may increase at a slower rate than we expect and may even decline, which could adversely affect our operating results.

Our business depends substantially on existing customers renewing their subscriptions with us and expanding their use of our Value+ services, and a decline in customer renewal rates, or failure to convince existing customers to adopt and utilize our Value+ services, could adversely impact our operating results.

In order for us to maintain or increase our revenue and improve our operating results, it is important that our existing customers continue to pay subscription fees for the use of our core solutions, as well as increase their adoption and utilization of our Value+ services. Our customers have no obligation to renew their subscriptions with us upon expiration of their subscription periods, which typically range from one month to one year. We cannot assure you that our customers will renew their subscriptions with us. In addition, our customers that start their accounts using a 30-day free trial have no obligation to begin a paid subscription. Furthermore, although a significant portion of our revenue growth has historically resulted from the adoption and utilization of our Value+ services by our existing customers, we cannot assure you that our existing customers will continue to broaden their adoption and utilization of our Value+ services, or use our Value+ services at all. If our existing customers do not renew their subscriptions and increase their adoption and utilization of our existing or newly developed Value+ services, our revenue may increase at a slower rate than we expect and may even decline, which could adversely impact our operating results.

Word-of-mouth referrals represent a significant source of new customers for us and provide us with an opportunity to cost-effectively market and sell our software solutions. The loss of our existing customers could have a significant impact on our reputation in our targeted verticals and our ability to acquire new customers cost-effectively. A reduction in the number of our existing customers, even if offset by an increase in new customers, could have the impact of reducing our revenue and operating margins.

In an effort to retain our customers and to expand our customers' adoption and utilization of our Value+ services, we may choose to use increasingly costly sales and marketing efforts. In addition, we may make significant investments in research and product development to introduce Value+ services that ultimately are not broadly adopted by our customers. In either of those cases, we could incur significantly increased costs without a corresponding increase in revenue. Furthermore, we may fail to identify Value+ services that our customers need for their businesses,

in which case we could miss opportunities to increase our revenue.

We expect to continue to derive a significant portion of our revenue from our property manager customers, and factors resulting in a loss of these customers could adversely affect our operating results.

Historically, more than 90% of our revenue has been derived from APM, our property management solution, and we expect that our property manager customers will continue to account for a significant portion of our revenue for the foreseeable future. The businesses of our property manager customers are typically significantly larger than those of our law firm customers. In addition, our property management solution has been available for longer, is more established within its vertical with a larger customer base, and currently offers a greater number of Value+ services.

We could lose property manager customers as a result of numerous factors, including:

- the expiration or termination of subscription agreements;
- the introduction of competitive products or technologies;
- a failure or inability by us to continue to provide high quality, useful products and services to our customers;
- changes in pricing policies by us or our competitors;
- acquisitions or consolidations within the property management industry;
- bankruptcies or other financial difficulties facing our customers; and
- conditions or trends that are specific to the property management industry such as the economic factors that impact the rental market.

The loss of a significant number of our property manager customers, or the loss of even a small number of our larger property manager customers, could cause our revenue to increase at a slower rate than we expect or even decline. In addition, even if we are able to retain our property manager customers, we may be unable to grow revenue from these property manager customers by increasing their adoption and utilization of our Value+ services. Furthermore, even if we continue to experience significant growth in our customer base within the legal vertical, it may be insufficient to offset slower growth or a decline in the property management business. Any of these outcomes could adversely affect our operating results.

Our growth depends in part on the success of our strategic relationships with third parties, and if we are unsuccessful in establishing or maintaining these relationships, our ability to compete in the market place or grow our revenue could be impaired.

In order to grow our business, we anticipate that we will continue to depend on our relationships with third parties, including our data center operators, electronic payment partners and other third parties that support delivery of our software solutions. Identifying partners, negotiating agreements and maintaining relationships requires significant time and resources. Our competitors may be more effective than us in cost-effectively building relationships with third parties that enhance their products and services, allow them to provide more competitive pricing, or offer other benefits to their customers. In addition, acquisitions of our partners by our competitors could result in a decrease in the number of current and potential strategic partners willing to establish or maintain relationships with us, and could increase the price at which products or services are available to us. If we are unsuccessful in establishing or maintaining our relationships with third parties, our ability to compete in the marketplace or to grow our revenue could be impaired, which could negatively impact our operating results. Even if we are successful, we cannot assure you that these relationships will result in increased customer adoption and usage of our software solutions or improved operating results. Furthermore, if our partners fail to perform as expected, we may be subjected to litigation, our reputation may be harmed, and our business and operating results could be adversely affected.

We depend on data centers and computing infrastructure operated by third parties and any disruption in these operations could adversely affect our operating results.

We currently serve our customers through a combination of our own servers located in third-party data center facilities, and servers and data centers operated by Amazon and other third parties. While we control and have access to our own servers and the other components of our network that are located in our third-party data centers, we do not control the operation of any of these third-party data center facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, or if one of our third-party data center operators is acquired, we may be required to transfer our servers and other infrastructure to new data center facilities, and we may incur significant costs and possible service interruptions in connection with doing so.

Problems faced by our third-party data center operators, or with any of the service providers with whom we or they contract, could adversely affect the experience of our customers. Our third-party data center operators could decide to close their

facilities without adequate notice. In addition, any financial difficulties, such as bankruptcy, faced by our third-party data center operators, or any of the service providers with whom we or they contract, may have negative effects on our business. Additionally, if our data centers are unable to keep up with our growing needs for capacity or any spikes in customer demand, it could have an adverse effect on our business. Any changes in third-party service levels at our data centers could result in loss of or damage to our customers' stored information and service interruptions, which could hurt our reputation. These issues could also cause us to lose customers, harm our ability to attract new customers, and subject us to potential liability, any of which could adversely affect our operating results.

Our systems are not fully redundant, and we have not yet implemented a complete disaster recovery plan or business continuity plan. Although the redundancies we do have in place will permit us to respond, at least to some degree, to service outages, our third-party data centers are vulnerable in the event of failure. We do not yet have adequate structure or systems in place to recover from a data center's severe impairment or total destruction, and recovery from the total destruction or severe impairment of any of our third-party data centers could be difficult and may not be possible at all.

We use third-party service providers for important payment processing and reporting functions, and their failure to fulfill their contractual obligations could harm our reputation, disrupt our business and adversely affect our operating results.

We use payment processing organizations and other service providers to enable us to provide electronic payment services to our customers, including EFT, and access to various reporting tools, such as background and credit checks. As a result, we have significantly less control over these payment processing and reporting functions than if we were to maintain and operate them ourselves. In some cases, functions necessary to our business are performed on proprietary third-party systems and software to which we have no access. We also generally do not have long-term contracts with these organizations and service providers. In addition, some of these organizations and service providers compete with us by directly or indirectly selling payment processing or reporting services to customers. The failure of these organizations and service providers to renew their contracts with us or to fulfill their contractual obligations could harm our reputation, result in significant disruptions to our business, and adversely affect our operating results.

Our platform must integrate with a variety of devices, operating systems and browsers that are developed by others, and if we are unable to ensure that our software solutions interoperate with such devices, operating systems and browsers, our software solutions may become less competitive, and our operating results may be harmed.

We offer our software solutions across a variety of operating systems and through the Internet. We are dependent on the interoperability of our platform with third-party devices, desktop and mobile operating systems, as well as web browsers that we do not control. Any changes in such devices, systems or web browsers that degrade the functionality of our software solutions or give preferential treatment to competitive services could adversely affect adoption and usage of our software solutions. In addition, in order to deliver high quality software solutions, we will need to continuously enhance and modify our functionality to keep pace with changes in Internet-related hardware, mobile operating systems such as iOS and Android, browsers and other software, communication, network and database technologies. We may not be successful in developing enhancements and modifications that operate effectively with these devices, operating systems, web browsers and other technologies or in bringing them to market in a timely manner. Furthermore, uncertainties regarding the timing or nature of new network platforms or technologies, and modifications to existing platforms or technologies, could increase our research and product development expense. In the event that it is difficult for our customers to access and use our software solutions, our software solutions may become less competitive, and our operating results could be adversely affected.

The markets in which we participate are intensely competitive and, if we do not compete effectively, our business could be harmed.

The overall market for business management software is global, highly competitive and continually evolving in response to a number of factors, including changes in technology, operational requirements, and laws and regulations. Although relatively early in its development, the market for cloud-based business management software is also highly competitive and subject to similar market factors.

While we focus on providing industry-specific, cloud-based business management software solutions to SMBs in our targeted verticals, we compete with other vertical cloud-based solution providers that serve companies of all sizes, as well as with horizontal cloud-based solution providers that provide broad cloud-based solutions across multiple verticals. Our competitors include established vertical software vendors, as well as newer entrants in the market. We also face competition from numerous cloud-based solution providers that focus almost exclusively on one or more point solutions. Continued consolidation among cloud-based providers could lead to significantly increased competition.

Although the domain expertise required to successfully develop, market and sell cloud-based business management software solutions in the property management and legal verticals may hinder new entrants that are unable to invest the necessary

resources to develop and deploy cloud-based solutions with the same level of functionality as ours, many of our competitors and potential competitors are larger and have greater name recognition, longer operating histories, and significantly greater resources than we do. As a result, our competitors may be able to respond more quickly and effectively to new or changing opportunities, technologies, operational requirements and industry standards. Some of these competitors may have more established customer relationships or strategic partnerships with third parties that enhance their products and services. Other competitors may offer products or services that address one or a number of business functions on a standalone basis at lower prices or bundled as part of a broader product sale, or with greater depth than our software solutions. In addition, our current and potential competitors may develop, market and sell new technologies with comparable functionality to our software solutions, which could cause us to lose customers, slow the rate of growth of new customers and cause us to decrease our prices in order to remain competitive. For all of these reasons, we may not be able to compete effectively against our current and future competitors, which could harm our business.

Pricing pressure may cause us to change our pricing model, which could hurt our renewal rates and our ability to attract new customers, as well as our ability to increase adoption and usage of our Value+ services, which could adversely affect our operating results.

As the markets for our existing software solutions mature, or as current and future competitors introduce new products or services that compete with ours, we may experience pricing pressure and be unable to renew our subscription agreements with existing customers or increase adoption and usage of our Value+ services, or attract new customers at prices that are consistent with our current pricing model and operating budget. If this were to occur, it is possible that we would have to change our pricing model, offer pricing incentives, or generally reduce our prices. In addition, our customers are SMBs, which are typically more price sensitive than larger enterprises. Changes to our pricing model could harm our customer retention rates and our ability to attract new customers, whether in connection with our core solutions or our Value+ services, which could adversely affect our operating results.

If we lose key members of our management team, our business may be harmed.

Our success and future growth depend, in part, upon the continued services of our executive officers and other key employees. From time to time, there may be changes in our executive officers or other key employees resulting from the hiring or departure of these personnel, which may disrupt our business. Our executive officers and other key employees are generally employed on an at-will basis, which means that these personnel could terminate their employment with us at any time. Additionally, the equity awards held by many of our executive officers and other key employees are close to fully vested, and these employees may not have sufficient financial incentive to stay with us. The loss of one or more of our executive officers or other key employees, or the failure by our executive team to work effectively with our employees and lead our company, could have an adverse effect on our business.

Our corporate culture has contributed to our success and, if we cannot maintain this culture as we grow, we could lose the passion, creativity, teamwork, focus and innovation fostered by our culture.

We believe that our culture has been and will continue to be a key contributor to our success. If we do not continue to develop our corporate culture or maintain our core values as we grow and evolve, we may be unable to foster the passion, creativity, teamwork, focus and innovation we believe we need to support our growth. Any failure to preserve our culture could negatively affect our ability to recruit and retain personnel and to effectively focus on and pursue our strategic objectives. Moreover, liquidity available to our employee security holders could lead to disparities of wealth among our employees, which could adversely impact relations among employees and our culture in general. As we grow and mature as a public company, we may find it difficult to maintain our corporate culture.

We expect to experience rapid growth and, if we fail to manage our growth effectively, it could adversely affect our operating results and preclude us from achieving our strategic objectives.

We have experienced significant growth since our formation in 2006, and we anticipate that we will continue to experience growth and expansion of our operations. For example, since our incorporation, we have significantly increased the number of employees across our organization, expanded the footprint of our business geographically, introduced a number of new Value+ services, and entered a new vertical with the acquisition of MyCase. This growth in the size, complexity and diversity of our business has placed, and we expect that our growth will continue to place, a significant strain on our management, administrative, operational and financial resources, as well as our company

culture. Our future success will depend, in part, on our ability to manage this growth effectively. To manage the expected growth of our operations and personnel, we will need to continue to develop and improve our operational and financial controls and our reporting systems and procedures, and to nurture and build on our company culture. Failure to effectively manage growth could adversely impact our business, including by resulting in errors or delays in deploying new core functionality to our customers, delays or difficulties in introducing new Value+ services or other

products, declines in the quality or responsiveness of our customer service organization, increases in costs and operating expenses, and other operational difficulties. If any of these risks actually occur, it could harm our reputation, adversely affect our operating results, and preclude us from achieving our strategic objectives.

We depend on highly skilled personnel and, if we are unable to retain or hire additional qualified personnel, we may not be able to achieve our strategic objectives.

To execute our growth plan and achieve our strategic objectives, we must continue to attract and retain highly qualified and motivated personnel across our organization. In particular, in order to continue to enhance our software solutions, add new and innovative core functionality and Value+ services, as well as develop new products, it will be critical for us to increase the size of our research and product development organization, including hiring highly skilled engineers with experience in designing, developing and testing cloud-based software solutions. Competition for software engineers is intense within our industry and there continues to be upward pressure on the compensation paid to these professionals. In addition, in order for us to achieve broader market acceptance of our software solutions, grow our customer base, and pursue adjacent markets and new verticals, we will need to continue to significantly increase the size of our sales and marketing organization. Identifying and recruiting qualified sales personnel and training them in the use of our platform requires significant time and expense, and it can be particularly difficult to retain these personnel.

Many of the companies with which we compete for experienced personnel have greater name recognition and financial resources than we have. If we hire employees from competitors or other companies, their former employers may attempt to assert that we or these employees have breached their legal obligations, resulting in a diversion of our time and resources. In addition, our headquarters are located in Santa Barbara, California, which is not generally recognized as a prominent commercial center, and it is challenging to attract qualified professionals due to our geographic location. As a result, we may have difficulty hiring and retaining suitably skilled personnel with the qualifications and motivation to expand our business. If we are unable to attract and retain the personnel necessary to execute our growth plan, we may be unable to achieve our strategic objectives and our operating results may suffer.

In addition, prospective and existing employees often consider the value of the equity awards they receive in connection with their employment. If the perceived value of our equity awards declines, or if the price of our Class A common stock experiences significant volatility, it may adversely affect our ability to recruit and retain highly skilled employees. If we fail to attract new personnel or to retain and motivate our current personnel, we may not be able to achieve our strategic objectives.

We have acquired, and may in the future acquire, other companies or technologies, which could divert our management's attention, result in additional dilution to our stockholders and otherwise disrupt our operations.

We have acquired, and may in the future acquire, other companies or technologies to complement or expand our software solutions, optimize our technical capabilities, enhance our ability to compete in our targeted verticals, provide an opportunity to expand into an adjacent market or new vertical, or otherwise offer growth or strategic opportunities. For example, in 2012, we acquired MyCase and, in April 2015, we acquired RentLinx. The pursuit of acquisitions may divert the attention of management and cause us to incur various expenses in identifying, investigating and pursuing suitable acquisitions, whether or not they are consummated.

We have limited experience acquiring other businesses. We may not be able to integrate acquired assets, technologies, personnel and operations successfully or achieve the anticipated synergies or other benefits from the acquired business due to a number of risks associated with acquisitions, including:

- incurrence of acquisition-related costs;
- difficulties integrating the assets, technologies, personnel or operations of the acquired business in a cost-effective manner, or inability to do so;
- difficulties and additional expenses associated with supporting legacy products and services of the acquired business;
- difficulties converting the customers of the acquired business to our software solutions and contract terms;
- diversion of management's attention from our business to address acquisition and integration challenges;
- adverse effects on our existing business relationships with customers and strategic partners as a result of the acquisition;
- cultural challenges associated with integrating employees from the acquired organization into our company;

the loss of key employees;

- use of resources that are needed in other parts of our business;
- use of substantial portions of our available cash to consummate the acquisition; and
- unanticipated costs or liabilities associated with the acquisition.

If an acquired business fails to meet our expectations in terms of its contribution to our overall business strategy, or if the costs of acquiring or integrating the acquired business exceed our estimates, our business, operating results and financial condition may suffer. In addition, acquisitions could also result in dilutive issuances of equity securities or the incurrence of debt, which could impose restrictions on our ability to operate our business and adversely affect our operating results. Furthermore, a significant portion of the purchase price of companies we may acquire could be allocated to goodwill and other intangible assets, which must be assessed for impairment. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could adversely affect our operating results.

If our property manager customers stop requiring residents to provide proof of tenant liability insurance, if insurance premiums decline or if insureds experience greater than expected losses, our operating results could be harmed.

We generate revenue by offering tenant liability insurance through a wholly owned subsidiary. Some of our property manager customers require residents to provide proof of tenant liability insurance and offer to enroll residents in their tenant liability insurance policy as additional insureds. If demand for rental housing declines, or if our property manager customers believe that it may decline, these customers may reduce their rental rates and stop requiring residents to provide proof of tenant liability insurance in order to reduce the overall cost of renting and make their rental offerings more competitive. If our property manager customers stop requiring residents to provide proof of tenant liability insurance or elect to enroll residents in insurance programs offered by competing providers, or if insurance premiums otherwise decline, our revenues from insurance services could be adversely affected.

Additionally, our tenant liability insurance policies are underwritten by us, and we are required by our insurance partner to maintain a reserve to cover potential claims under the policies. While our policies have a limit of $100,000 per occurrence, there is no limit on the dollar amount of claims that could be made against us in any particular period or in the aggregate. In the event that claims by the insureds increase unexpectedly, our reserve may not be sufficient to cover our resultant liability under the policies. To the extent we are required to pay out amounts to insureds that are significantly higher than our current reserves, it could have a material adverse effect on our operating results.

Our tenant liability insurance business is subject to state governmental regulation, which could limit the growth of our insurance business and impose additional costs on us.

Our wholly owned subsidiary holds a license from the State of Hawaii Insurance Division of the Department of Commerce and Consumer Affairs and our third-party service providers maintain licenses with a number of other individual state departments of insurance. Collectively, we are subject to state governmental regulation and supervision in connection with the operation of our tenant liability insurance business. This state governmental supervision could limit the growth of our insurance business by increasing the costs of regulatory compliance, limiting or restricting the products or services we provide or the methods by which we provide them, and subjecting us to the possibility of regulatory actions or proceedings. Our continued ability to maintain these insurance licenses in the jurisdictions in which we are licensed depends on our compliance with the rules and regulations promulgated from time to time by the regulatory authorities in each of these jurisdictions. Furthermore, state insurance departments conduct periodic examinations, audits and investigations of the affairs of insurance companies, any of which could result in the expenditure of significant management time or financial resources.

In all jurisdictions, the applicable laws and regulations are subject to amendment or interpretation by regulatory authorities. Generally, such authorities are vested with relatively broad discretion to grant, renew and revoke licenses and approvals and to implement and interpret rules and regulations. Accordingly, we may be precluded or temporarily suspended from carrying on some or all of the activities of our insurance business or otherwise be fined or penalized in a given jurisdiction. No assurances can be given that our insurance business can continue to be conducted in any given jurisdiction as it has been conducted in the past or that we will be able to expand our insurance business in the future.

All of our revenues are generated by sales to customers in our targeted verticals, and factors that adversely affect the applicable industry could also adversely affect us.

Currently, all of our sales are to customers in the property management and legal industries. Demand for our software solutions could be affected by factors that are unique to and adversely affect our targeted verticals. In particular, the property management and legal industries are highly regulated, subject to intense competition and impacted by changes in general economic and market conditions. For example, changes in applicable laws and regulations could significantly impact the software functionality demanded by our customers and require us to expend significant resources to ensure our software solutions continue to meet their evolving needs. In addition, other industry-specific factors, such as industry consolidation or the introduction of competing or disruptive technology, could lead to a significant reduction in the number of customers that use our software solutions within a particular vertical or the Value+ services demanded by these customers. Further, if the rental housing or legal markets decline, our customers may decide not to renew their subscriptions or they may cease using our Value+ services in order to reduce costs to remain competitive. As a result, our ability to generate revenue from our property manager and law firm customers could be adversely affected by specific factors that affect the property management or legal industries.

In addition to the foregoing risks associated with our targeted verticals themselves, there is an overarching risk stemming from potential widespread adoption of quickly evolving financial or other disruptive technology products that could significantly impact our targeted verticals, even if that technology is not specifically designed to apply directly to our targeted verticals. The adoption of these new technologies could significantly reduce the volume or demand of customers in our targeted verticals, thereby reducing our revenue, which could materially impact our business, financial condition, operating results and, ultimately, our stock price.

Our software solutions address functions within the heavily regulated property management and legal industries, and our customers' failure to comply with applicable laws and regulations could subject us to litigation.

We sell our software solutions to customers within the property management and legal industries. Our customers use our software solutions for business activities that are subject to a number of laws and regulations, including without limitation state and local real property laws and legal ethics rules. Any failure by our customers to comply with laws and regulations applicable to their businesses could result in fines, penalties or claims for substantial damages against our customers. To the extent our customers believe that our software solutions or our customer service organization caused or contributed to such failures, our customers may make claims for damages against us, regardless of whether we are responsible for the failure. As a result, we may be subject to lawsuits that, even if unsuccessful, could divert our resources and our management's attention and adversely affect our business, and our insurance coverage may not be sufficient to cover such claims against us.

If we are unable to deliver effective customer service, it could harm our relationships with our existing customers and adversely affect our ability to attract new customers.

Our business depends, in part, on our ability to satisfy our customers, both by providing software solutions that address their business needs, and by providing on-boarding services and ongoing customer service, which contributes to retaining customers and increasing adoption and utilization of our Value+ services by our existing customers. Once our software solutions are deployed, our customers depend on our customer service organization to resolve technical issues relating to their use of our solutions. We may be unable to respond quickly to accommodate short-term increases in customer demand for support services or may otherwise encounter a customer issue that is difficult to resolve. If a customer is not satisfied with the quality or responsiveness of our customer service, we could incur additional costs to address the situation. As we do not separately charge our customers for support services, increased demand for our support services would increase costs without corresponding revenue, which could adversely affect our operating results. In addition, regardless of the quality or responsiveness of our customer service efforts, a customer that is not satisfied with an outcome may choose to terminate, or to not renew, their relationship with us.

Our sales process is highly dependent on the ease of use of our software solutions, our reputation and positive recommendations from our existing customers. Any failure to maintain high-quality or responsive customer service, or a market perception that we do not maintain high-quality or responsive customer service, could harm our reputation, cause us to lose customers and adversely impact our ability to sell our software solutions to prospective customers.

If we are unable to maintain and promote our brands, or to do so in a cost-effective manner, our ability to maintain and expand our customer base will be impaired, and our operating results could be adversely affected.

We believe that maintaining and promoting our brands is critical to achieving widespread awareness and acceptance of our software solutions, and maintaining and expanding our customer base. We also believe that the importance of brand recognition will increase as competition in our targeted verticals increases. If we do not continue to build awareness of our brands, we could be placed at a competitive disadvantage as compared to companies whose brands are, or become, more recognizable than ours. Maintaining and promoting our brands will depend, in part, on our ability to continue to provide new and innovative core

functionality and Value+ services and best-in-class customer service, as well as the effectiveness of our sales and marketing efforts. If we fail to deliver products and functionality that address our customers' business needs, or if we fail to meet our customers' expectations for customer service, it could weaken our brands and harm our reputation. Additionally, the actions of third parties may affect our brands and reputation if customers do not have a positive experience using the services of our third-party partners that support our software solutions. Maintaining and enhancing our brands may require us to make substantial investments, and these investments may not result in commensurate increases in our revenue. If we fail to successfully maintain and promote our brands, or if make investments that are not offset by increased revenue, our operating results could be adversely affected.

If we are unable to increase sales of our software solutions to larger customers while mitigating the risks associated with serving such customers, our business and operating results may suffer.

While we plan to continue to market and sell our software solutions to SMBs, our growth strategy is dependent, in part, upon increasing sales of our software solutions to larger customers within the SMB market. Sales to larger customers may involve risks that are not present, or are present to a lesser extent, in sales to smaller businesses. As we seek to increase our sales to larger customers, we may invest considerably greater amounts of time and financial resources in our sales and marketing efforts. In addition, we may face longer sales cycles and experience less predictability and greater competition in completing some of our sales than we have in selling our software solutions to smaller businesses. Although we generally have not configured our software solutions or negotiated our pricing for specific customers, which has historically resulted in reduced upfront selling costs, our ability to successfully sell our software solutions to larger customers may be dependent, in part, on our ability to develop functionality, or to implement pricing policies, that are unique to particular customers. It may also be dependent on our ability to attract and retain sales personnel with experience selling to larger organizations. Also, because security breaches or other performance problems with respect to larger customers may result in greater economic harm to these customers and more adverse publicity, there is increased financial and reputational risk associated with serving such customers. If we are unable to increase sales of our software solutions to larger customers, while mitigating the risks associated with serving such customers, our business and operating results may suffer.

Because we recognize revenue from subscriptions for our software solutions over the terms of the subscription agreements, downturns or upturns in new business may not be immediately reflected in our operating results.

We recognize revenue from customers ratably over the terms of their subscription agreements, which typically range from one month to one year. As a result, some of the revenue we report in each period is derived from the recognition of deferred revenue relating to subscription agreements entered into during previous periods. Consequently, a decline in new or renewed subscriptions in any one period may not be reflected in our revenue results for that period. However, any such decline will negatively affect our revenue in future quarters. Our subscription model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription period. Accordingly, the effect of downturns or upturns in our sales and the market acceptance of our software solutions, and potential changes in our customer retention rates, may not be apparent in our operating results until future periods.

Because our invoicing is generally for periods less than one year, our revenue growth is heavily dependent on new subscription sales, consumption of our usage-based Value+ services and renewals of our subscription services in the current year.

Our growth is heavily dependent on subscription sales, adoption and consumption of our usage-based Value+ services and renewals of our subscription services in the current year. We offer our core solutions and Value+ subscription services to customers pursuant to subscription agreements with relatively short terms, typically ranging from one month to one year. We generally invoice our customers for subscription services in monthly, quarterly or annual installments, typically in advance of the subscription period. We do not currently intend to extend the typical terms of our subscription agreements with any regularity, or to invoice our customers less frequently, and we expect that we will continue to depend on current-year sales and renewals to drive our growth.

Failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brands which could harm our business.

We currently rely on patent, trademark, copyright and trade secret laws, trade secret protection and confidentiality or license agreements with our employees, customers, partners and others to protect our intellectual property rights. Our success and ability to compete depend, in part, on our ability to protect our intellectual property, including our proprietary technology and our brands. If we are unable to protect our proprietary rights adequately, our competitors could use the intellectual property we have developed to enhance their own products and services, which could harm our business.

In order to monitor and protect our intellectual property rights, we may be required to spend significant resources. Litigation brought to protect and enforce our intellectual property rights could be costly, time-consuming and distracting to management, and could result in the impairment or loss of portions of our intellectual property or require us to pay costly royalties.

Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights. Accordingly, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property. Our failure to secure, protect and enforce our intellectual property rights could adversely affect our business and operating results.

We may be sued by third parties for alleged infringement of their proprietary rights, which could cause us to incur significant expenses and require us to pay substantial damages.

There is considerable patent, trademark, copyright, trade secret and other intellectual property development activity in our industry. Our success depends, in part, on our not infringing upon the intellectual property rights of others. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our technology or software solutions. From time to time, our competitors or other third parties may claim that we are infringing upon their intellectual property rights. However, we may be unaware of the intellectual property rights that others may claim cover some or all of our technology or software solutions. Any claims or litigation, regardless of merit, could cause us to incur significant expenses and, if successfully asserted against us, could require that we pay substantial damages, settlement costs or ongoing royalty payments, require that we comply with other unfavorable license and other terms, or prevent us from offering our software solutions in their current form. Even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the attention of our management and key personnel from our business operations and harm our operating results.

Our software solutions contain open source software, which may pose particular risks to our proprietary source code, and could have a negative impact on our business and operating results.

We use open source software in our software solutions and expect to continue to do so in the future. The terms of many open source licenses to which we are subject have not been interpreted by U.S. or foreign courts, and there is a risk that open source licenses could be construed in a manner that imposes unanticipated conditions, restrictions or costs on our ability to provide or distribute our software solutions. Additionally, we may from time to time face claims from third parties alleging ownership of, or demanding release of, the open source software or derivative works that we developed using such software, which could include our proprietary source code, or otherwise seeking to enforce the terms of the applicable open source license. These claims could result in litigation, which could be costly for us to defend, and could require us to make our source code freely available, purchase a costly license or cease offering the implicated core functionality and Value+ services unless and until we can re-engineer them to avoid infringement. This re-engineering process could require significant additional research and product development resources, and we may not be able to complete it successfully or in a timely manner. In addition to risks related to license requirements, usage of certain open source software can lead to greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of software. These risks could be difficult to eliminate or manage, and could have a negative impact on our business and operating results.

Changes in laws and regulations related to the Internet or changes in the Internet infrastructure itself may diminish the demand for our software solutions, and could have a negative impact on our business.

The future success of our business depends upon the continued use of the Internet as a primary medium for commerce, communication and business services. Federal, state or foreign government bodies or agencies have in the past adopted, and may in the future adopt, laws or regulations affecting the use of the Internet as a commercial medium. Changes in these laws or regulations could require us to modify our software solutions in order to comply with these changes. In addition, government agencies or private organizations may begin to impose taxes, fees or other charges for accessing the Internet, or for the commerce conducted via the Internet. These laws or charges could limit the growth of Internet-related commerce or communications generally, result in reductions in the demand for Internet-based business services such as ours, and cause us to incur significant expenses.

The use of the Internet in general could be adversely affected by delays in the development or adoption of new standards and protocols to handle increased demands of Internet activity, accessibility, reliability, security, cost, ease of use and quality of service. In addition, the use of the Internet as a medium for commerce, communication and business services may have been, and may continue to be, adversely affected by concerns regarding network outages, software errors, viruses, security breaches, fraud or other malicious activity. If the use of the Internet is adversely

affected by these issues, demand for our software solutions could suffer.

Privacy and data security laws and regulations could impose additional costs on us and reduce the demand for our software solutions.

Our customers store and transmit a significant amount of personal or identifying information through our technology platform. Privacy and data security have become significant issues in the United States and in other jurisdictions where we may offer our software solutions. The regulatory framework relating to privacy and data security issues worldwide is rapidly evolving

and is likely to remain uncertain for the foreseeable future. Federal, state and foreign government bodies and agencies have in the past adopted, or may in the future adopt, laws and regulations regarding the collection, use, processing, storage and disclosure of personal or identifying information obtained from customers and other individuals. In addition to government regulation, privacy advocates and industry groups may propose various self-regulatory standards that may legally or contractually apply to our business. Because the interpretation and application of many privacy and data security laws, regulations and applicable industry standards are uncertain, it is possible that these laws, regulations and standards may be interpreted and applied in a manner inconsistent with our existing privacy and data management practices. As we expand into new jurisdictions or verticals, we will need to understand and comply with various new requirements applicable in those jurisdictions or verticals.

To the extent applicable to our business or the businesses of our customers, these laws, regulations and industry standards could have negative effects on our business, including by increasing our costs and operating expenses, and delaying or impeding our deployment of new core functionality or Value+ services. Compliance with these laws, regulations and industry standards requires significant management time and attention, and failure to comply could result in negative publicity, subject us to fines or penalties, or result in demands that we modify or cease existing business practices. In addition, the costs of compliance with, and other burdens imposed by, such laws, regulations and industry standards may adversely affect our customers' ability or desire to collect, use, process and store personal information using our software solutions, which could reduce overall demand for them. Even the perception of privacy and data security concerns, whether or not valid, may inhibit market acceptance of our software solutions in certain verticals. Furthermore, privacy and data security concerns may cause our customers' clients, vendors, employees and other industry participants to resist providing the personal information necessary to allow our customers to use our applications effectively. Any of these outcomes could adversely affect our business and operating results.

We may require additional capital to support our operations or the growth of our business, and we cannot be certain that this capital will be available on favorable terms when required, or at all.

We may need additional capital to grow our business and meet our strategic objectives. Our ability to obtain additional capital, if and when required, will depend on numerous factors, including investor and lender demand, our historical and forecasted financial and operating performance, our market position, and the overall condition of the capital markets. We cannot guarantee that additional financing will be available to us on favorable terms when required, or at all. In addition, if we raise additional funds through the issuance of equity securities, those securities may have powers, preferences or rights senior to the rights of our Class A common stock, and our existing stockholders may experience dilution. If we raise additional funds through the issuance of debt securities, we may incur interest expense or other costs to service the indebtedness, or we may be required to encumber certain assets, which could negatively impact our operating results. Furthermore, if we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support the growth of our business and the achievement of our strategic objectives could be significantly impaired and our operating results may be harmed.

Financing agreements we are party to or may become party to may contain operating and financial covenants that restrict our business and financing activities. Failure to comply with these covenants, or other restrictions, could result in default under these agreements.

Our existing credit agreement, with Wells Fargo, which we refer to as the Credit Agreement, contains certain operating and financial restrictions and covenants, including limitations on dividends, dispositions, mergers or consolidations, incurrence of indebtedness and liens, and other corporate activities. These restrictions and covenants, as well as those contained in any future financing agreements that we may enter into, may restrict our ability to finance our operations, and to engage in, expand or otherwise pursue our business activities and strategic objectives. Our ability to comply with these covenants may be affected by events beyond our control, and breaches of these covenants could result in a default under our existing Credit Agreement and any future financial agreements that we may enter into. If not waived, defaults could cause any outstanding indebtedness under the Credit Agreement and any future financing agreements that we may enter into to become immediately due and payable.

Because our long-term growth strategy involves expansion of our sales to customers outside the United States, our business will be susceptible to the risks associated with international operations.

A component of our growth strategy involves the expansion of our international operations and worldwide customer base. To date, we have realized an immaterial amount of revenue from customers outside the United States. Operating in international markets will require significant resources and management attention and will subject us to regulatory, economic, geographic and political risks that are different from those in the United States. Because of our limited experience with international operations and significant differences between the United States and international markets, our international expansion efforts may not be successful in creating demand for our software solutions outside of the United States or in effectively selling our software solutions in any international markets we may enter. If we invest substantial time and resources to expand our international operations and are unable to do so successfully, our business and operating results could suffer.

If we fail to maintain an effective system of internal control over financial reporting, our ability to produce timely and accurate financial statements or comply with applicable regulations could be impaired.

In connection with the audit of our consolidated financial statements for fiscal year 2014, our independent registered public accounting firm identified material weaknesses in our internal control over financial reporting. As of December 31, 2015, we completed remediation of these material weaknesses. However, the completion of remediation does not provide assurance that our controls will continue to operate properly or that our financial statements will not contain any material errors. There may be future material weaknesses in our internal control over financial reporting, and as a result we may not detect financial statement errors on a timely basis. Moreover, in the future we may engage in business transactions, such as acquisitions or reorganizations, or implement new accounting standards, or adopt other changes to our business processes, any of which could require us to develop and implement new controls or to modify existing controls, which could negatively affect our internal control over financial reporting and result in material weaknesses.

In the event we experience a material weakness in our internal control over financial reporting in the future, we may not detect errors on a timely basis and our financial statements may be materially misstated. Ineffective internal control over financial reporting, failure to comply with the requirements of Section 404 of the Sarbanes-Oxley Act in a timely manner and the inability to express an opinion as to the effectiveness of our internal control over financial reporting could cause investors to lose confidence in our reported financial statements and other information, which could have a negative effect on the market price of our Class A common stock. Additionally, it could lead to an investigation by the SEC, NASDAQ or other regulatory authorities, which could require the expenditure of additional financial and management resources.

We are an emerging growth company and our decision to comply with certain reduced reporting and disclosure requirements could make our Class A common stock less attractive to investors.

We qualify as an emerging growth company under the JOBS Act. An emerging growth company may take advantage of specified reduced reporting requirements and may be relieved of other significant requirements that are otherwise generally applicable to public companies. These provisions include:

- an exemption from compliance with the auditor attestation requirement on the effectiveness of our internal control over financial reporting;
- an exemption from compliance with any requirement that the Public Company Accounting Oversight Board may adopt regarding mandatory audit firm rotation or a supplement to the auditor's report providing additional information about the audit and the financial statements;
- reduced disclosure about our executive compensation arrangements; and
- exemptions from the requirements to obtain a non-binding advisory vote on executive compensation or stockholder approval of any golden parachute arrangements.

We have irrevocably elected to opt out of the extended transition period for complying with new or revised accounting standards pursuant to Section 107(b) of the JOBS Act. However, in this Annual Report, we are taking advantage of the other exemptions discussed above. Accordingly, the information that we provide to our stockholders may be different from the information you receive from other public companies in which you have invested. If some investors find our Class A common stock less attractive as a result of our reliance on these exemptions, there may be a less active trading market for our Class A common stock, the market price of our Class A common stock may be more volatile, and the trading price of our Class A common stock may be lower than that of comparable companies.

Our ability to use our net operating loss carryforwards and certain other tax attributes may be limited.

As of December 31, 2016, we had U.S. federal net operating loss carryforwards of approximately $80.7 million and state net operating loss carryforwards of approximately $50.5 million, which begin to expire in 2027 and 2017, respectively. As of December 31, 2016 we also had federal and state research and development credit carryforwards of $3.9 million and $4.1 million, respectively. The federal credits carryforwards will begin to expire in 2027, while the state credit carryforwards indefinitely. Under Section 382 of the Internal Revenue Code of 1986, as amended, or the

Code, if a corporation undergoes an "ownership change," the corporation's ability to use its pre-change net operating loss carryforwards and other pre-change tax attributes, such as research tax credits, to offset its post-change income and taxes may be limited. In general, an "ownership change" occurs if there is a cumulative change in our ownership by "5% shareholders" that exceeds 50 percentage points over a rolling three-year period. Similar rules may apply under state tax laws. It is possible that our existing net operating loss and/or credit carryforwards may be subject to limitations arising from previous ownership changes, and future issuances of our stock could cause an ownership change.

Furthermore, our ability to utilize net operating loss and/or credit carryforwards of companies that we have acquired or may acquire in the future may be subject to limitations. Any such limitations on our ability to use our net operating loss carryforwards and other tax assets could adversely impact our business, financial condition and operating results.
Tax laws or regulations could be enacted or changed and existing tax laws or regulations could be applied to us or to our customers in a manner that could increase the costs of our software solutions and adversely impact our operating results.

The application of federal, state, local and foreign tax laws to services provided electronically is continuously evolving. New income, sales, use or other tax laws, statutes, rules, regulations or ordinances could be enacted or amended at any time, possibly with retroactive effect, and could be applied solely or disproportionately to services provided over the Internet. These enactments or amendments could adversely affect our sales activity due to the inherent cost increase the taxes would represent and ultimately result in a negative impact on our operating results.

In addition, existing tax laws, statutes, rules, regulations or ordinances could be interpreted, modified or applied adversely to us, possibly with retroactive effect, which could require us or our customers to pay additional tax amounts, as well as require us or our customers to pay fines or penalties, as well as interest on past amounts. If we are unsuccessful in collecting such taxes due from our customers, we could be held liable for such costs, thereby adversely impacting our operating results.
We may be subject to additional tax liabilities.

We are subject to income, sales, use, value added and other taxes in the United States and other jurisdictions in which we conduct business, and such laws and rates vary by jurisdiction. Certain jurisdictions in which we do not collect sales, use, value added or other taxes on our sales may assert that such taxes are applicable, which could result in tax assessments, penalties and interest, and we may be required to pay or collect such taxes in the future. If we receive an adverse determination as a result of an audit or related litigation, or we unilaterally determine that we have misinterpreted provisions of the tax regulations to which we are subject, there could be a material effect on our tax provision, net income or cash flows in the period or periods for which that determination is made.
Our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.

Generally accepted accounting principles in the United States, or GAAP, are subject to interpretation by the Financial Accounting Standards Board, or FASB, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant impact on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change.
Risks Related to Our Class A Common Stock
The market price of our Class A common stock may be volatile or may decline regardless of our operating performance, which could result in substantial losses for our stockholders.

Prior to the completion of our initial public offering in June 2015, there was no public market for shares of our Class A common stock. We cannot assure you that an active trading market for our Class A common stock will develop, or if developed, that any market will be sustained. The market price of our Class A common stock has been, and is likely to continue to be, highly volatile, and fluctuations in the price of our Class A common stock could cause you to lose all or part of your investment. For example, during 2016, the share price of our Class A common stock on the NASDAQ Global Market fluctuated between $11.07 and $24.50.
There are numerous factors that could cause fluctuations in the market price of our Class A common stock, including:
- price and volume fluctuations in the overall stock market from time to time;
- volatility in the market prices and trading volumes of securities issued by software companies;
- changes in operating performance and stock market valuations of other software companies generally, and of companies that sell cloud-based solutions within our targeted verticals in particular;

sales of shares of our Class A common stock by us or our stockholders, or perceptions that such sales may occur; failure of securities analysts to maintain coverage of us, changes in financial estimates by securities analysts who

follow us, or our failure to meet these estimates or the expectations of investors;
the guidance we may provide to the public, any changes in that guidance, and our performance relative to that guidance;
announcements by us or our competitors of new products or services;
the public's reaction to our press releases, filings with the SEC and other public announcements;
rumors and market speculation involving us or other software companies;
actual or anticipated changes in our operating results or fluctuations in our operating results;
actual or anticipated developments in our business, our competitors' businesses or the competitive landscape generally;
litigation involving us, our industry or both, or investigations by regulators into our operations or those of our competitors;
developments or disputes concerning our intellectual property or other proprietary rights;
announced or completed acquisitions of businesses or technologies by us or our competitors;
new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
changes in accounting standards, policies, guidelines, interpretations or principles;
changes in our management; and
general economic conditions and trends, including slow or negative growth of our markets.

In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. If instituted against us, any such litigation, regardless of its merit or final outcome, could result in substantial costs and a diversion of our management's attention, thereby adversely affecting our operating results and, potentially, the price of our Class A common stock.

The dual class structure of our common stock has the effect of concentrating voting control with a limited number of stockholders, including our executive officers, directors and principal stockholders, which will limit your ability to influence corporate matters.

Our Class B common stock has 10 votes per share, and our Class A common stock has one vote per share. As of December 31, 2016, the holders of the outstanding shares of our Class B common stock, including our executive officers, directors, and principal stockholders, collectively hold approximately 95% of the combined voting power of our outstanding capital stock. Because of the 10-to-1 voting ratio between our Class B common stock and Class A common stock, the holders of our Class B common stock collectively control a majority of the combined voting power of our outstanding capital stock and therefore are able to exercise significant influence and control over the establishment and implementation of our future business plans and strategic objectives, as well as to control all matters submitted to our stockholders for approval. These persons may manage our business in ways with which you disagree and which may be adverse to your interests. This concentrated control may also have the effect of delaying, deterring or preventing a change-in-control transaction, depriving our stockholders of an opportunity to receive a premium for their capital stock or negatively affecting the market price of our Class A common stock.

Transfers by holders of our Class B common stock will generally result in those shares converting to Class A common stock, subject to limited exceptions. The conversion of our Class B common stock to Class A common stock will have the effect, over time, of increasing the relative voting power of the holders of our Class B common stock who retain their shares over the long term.

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

Our amended and restated certificate of incorporation and our amended and restated bylaws contain provisions that could have the effect of rendering more difficult hostile takeovers, change-in-control transactions or changes in our board of directors or management. Among other things, these provisions:

- authorize the issuance of preferred stock with powers, preferences and rights that may be senior to our common stock, which can be created and issued by our board of directors without prior stockholder approval;
- provide for the adoption of a staggered board of directors whereby the board is divided into three classes, each of which has a different three-year term;
- provide that the number of directors will be fixed by the board;
- prohibit our stockholders from filling board vacancies;
- provide for the removal of a director only for cause and then only by the affirmative vote of the holders of a majority of the combined voting power of our outstanding capital stock;
- prohibit stockholders from calling special stockholder meetings;
- prohibit stockholders from acting by written consent without holding a meeting of stockholders;
- require the vote of at least two-thirds of the combined voting power of our outstanding capital stock to approve amendments to our certificate of incorporation or bylaws;
- require advance written notice of stockholder proposals and director nominations;
- provide for a dual-class common stock structure, as discussed above; and
- require the approval of the holders of at least a majority of the outstanding shares of our Class B common stock, voting as a separate class, prior to consummating a change-in-control transaction.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, or DGCL, which may delay, deter or prevent a change-in-control transaction. Section 203 imposes certain restrictions on mergers, business combinations and other transactions between us and holders of 15% or more of our common stock.

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

Future sales of shares of our Class A common stock, or the perception that these sales could occur, could depress the market price of our Class A common stock.

Sales of a substantial number of shares of our Class A common stock in the public market, or the perception that these sales might occur, could cause the market price of our Class A common stock to decline or make it more difficult for you to sell your Class A common stock at a time and price that you deem appropriate, and could impair our ability to raise capital through the sale of additional equity securities. We are unable to predict the effect that sales, or the perception that our shares may be available for sale, will have on the prevailing market price of our Class A common stock.

As of December 31, 2016, we had an aggregate of 1.7 million options outstanding that, if fully exercised, would result in the issuance of additional shares of Class A common stock or Class B common stock, as applicable. Our Class B common stock converts into Class A common stock on a one-for-one basis. In addition, as of December 31, 2016, we had 0.5 million restricted stock units outstanding which, if fully vested and settled in shares, would result in the issuance of additional shares of Class A common stock. All of the shares of Class A common stock issuable upon the exercise of options (or upon conversion of shares of Class B common stock issued upon the exercise of options), or upon the vesting and settlement of restricted stock units, have been registered for public resale under the Securities Act. Accordingly, these shares will be able to be freely sold in the public market upon issuance.

Certain holders of our Class A common stock and Class B common stock have rights, subject to certain conditions, to require us to file registration statements for the public resale of such shares (in the case of Class B common stock, the Class A common stock issuable upon conversion of such shares) or to include such shares in registration statements that we may file for us or other stockholders. Any sales of securities by these stockholders could have a material adverse effect on the market price of our Class A common stock.

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

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

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

We have never declared or paid any cash dividends on our existing common stock. We do not anticipate declaring or paying any cash dividends to holders of our Class A common stock in the foreseeable future and intend to retain all future earnings for the growth of our business. In addition, the terms of our Credit Agreement restrict our ability to pay dividends. Consequently, investors may need to rely on sales of our Class A common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investment. Investors should not purchase our Class A common stock with the expectation of receiving cash dividends.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our corporate headquarters is located in two adjacent buildings in Santa Barbara, California. The lease on the first building covers approximately 43,300 square feet and expires in December 2021. The lease on the second building covers approximately 35,900 square feet and expires in November 2020.

We also lease space in San Diego, California, and Richardson, Texas under leases that expire at various times between 2021 and 2022.

We intend to procure additional space as we add employees and expand our operations geographically. We believe our current facilities are adequate for our current needs and that, should it be needed, suitable additional or alternative space will be available to us to accommodate any such expansion of our operations.

We lease all of our facilities and do not own any real property.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we are involved in various legal proceedings arising from or related to claims incident to the normal course of our business activities. Although the results of such legal proceedings and claims cannot be predicted with certainty, we believe we are not currently a party to any legal proceeding(s) which, if determined adversely to us, would, individually or taken together, have a material adverse effect on our business, operating results, financial condition or cash flows. However, regardless of the merit of any claims raised or the ultimate outcome, legal proceedings may generally have an adverse impact on us as a result of defense and settlement costs, diversion of management resources and other factors.

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

Market Information for our Class A Common Stock

Our Class A common stock began trading publicly on the Nasdaq Global Market under the symbol "APPF" on June 26, 2015. Prior to that date, there was no public trading market for our Class A common stock. The following table sets forth the high and low sales price per share of our Class A common stock as reported on the Nasdaq Global Market for the periods indicated:

	High	Low
Year ended December 31, 2016:		
First quarter	$15.19	$11.07
Second quarter	$15.57	$12.07
Third quarter	$19.98	$14.12
Fourth quarter	$24.50	$18.27

	High	Low
Year ended December 31, 2015:		
Second quarter (from June 26, 2015)	$14.87	$12.11
Third quarter	$18.48	$13.50
Fourth quarter	$19.93	$14.51

Holders of Record

As of February 1, 2017, there were 39 holders of record of our Class A common stock and 172 holders of record of our Class B common stock. Because many of our shares of Class A common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders.

Dividend Policy

We have never declared or paid any cash dividends on our capital stock. We have no plans to declare or pay any dividends on our capital stock in the foreseeable future and intend to retain all future earnings, if any, generated by our operations for the growth of our business. Any future decision to declare or pay dividends will be made by our board of directors in its sole discretion and will depend upon our financial condition, results of operations, capital requirements, general economic conditions and other factors that our board of directors deems relevant at the time of its decision. Investors should not purchase our Class A common stock with the expectation of receiving cash dividends. In addition, the terms of our Credit Agreement may restrict our ability to pay dividends.

Stock Performance Graph

The following performance graph compares the cumulative total return on our Class A common stock with that of the S&P 500 Index, the S&P Information Technology Index and the NASDAQ Computer Index. This chart assumes $100 was invested at the close of market on June 26, 2015, which was our initial trading day, in our Class A common stock, the S&P 500 Index, the S&P Information Technology Index and the NASDAQ Computer Index, and assumes the reinvestment of any dividends. The stock price performance reflected in the performance graph is not necessarily indicative of future stock performance.

The NASDAQ Computer Index replaces the S&P Information Technology Index, which was used in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. We believe that the NASDAQ Computer Index, which is designed to measure the financial health of the overall computer industry, including software and hardware companies, is a more appropriate comparative market index because it is more widely used by our publicly traded industry peers.

This performance graph shall not be deemed “filed” for purposes of Section 18 of the Exchange Act or incorporated by reference into any of our other filings under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

Unregistered Sales of Equity Securities
None.

Use of Proceeds
None.

ITEM 6. SELECTED FINANCIAL DATA

The following tables provide our historical selected consolidated financial data for the periods indicated. We have derived the selected Consolidated Statements of Operations data for the fiscal years ended December 31, 2016, 2015 and 2014 and the selected Consolidated Balance Sheet data as of December 31, 2016 and 2015 from our audited Consolidated Financial Statements included elsewhere in this Annual Report. We have derived the selected Consolidated Statements of Operations data for the fiscal year ended December 31, 2013 and 2012 and the selected Consolidated Balance Sheet data as of December 31, 2014, 2013 and 2012 from our audited Consolidated Financial Statements, which are not included in this Annual Report. Our historical results are not necessarily indicative of the results we expect in the future.

The following historical selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements and the related notes included elsewhere in this Annual Report.

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands, except per share data)				
Consolidated Statements of Operations Data:					
Revenue	$105,586	$74,977	$47,671	$26,542	$12,706
Costs and operating expenses:					
Cost of revenue (exclusive of depreciation and amortization)(1)	44,630	33,903	22,555	13,616	8,211
Sales and marketing(1)	28,827	26,076	16,876	10,337	8,001
Research and product development(1)	12,638	9,554	6,505	5,057	4,067
General and administrative(1)	17,979	14,343	6,489	2,286	2,736
Depreciation and amortization	9,935	6,104	3,805	2,850	2,079
Total costs and operating expenses	114,009	89,980	56,230	34,146	25,094
Loss from operations	(8,423)	(15,003)	(8,559)	(7,604)	(12,388)
Other income (expense), net	(37)	5	(121)	287	—
Interest income (expense), net	246	(595)	59	12	72
Loss before income taxes	(8,214)	(15,593)	(8,621)	(7,305)	(12,316)
Provision for income taxes	67	75	—	—	—
Net loss	$(8,281)	$(15,668)	$(8,621)	$(7,305)	$(12,316)
Net loss per share, basic and diluted	(0.25)	(0.73)	(0.98)	(0.87)	(1.52)
Weighted average common shares outstanding, basic and diluted	33,561	21,336	8,757	8,437	8,104

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

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Costs and operating expenses:					
Cost of revenue (exclusive of depreciation and amortization)	$471	$124	$68	$63	$49
Sales and marketing	442	115	48	39	41

Research and product development	382	41	19	49	48
General and administrative	3,006	727	757	96	110
Total stock-based compensation expense	$4,301	$1,007	$892	$247	$248

	December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Consolidated Balance Sheet Data:					
Cash and cash equivalents and investment securities [(1)]	$52,860	$56,715	$5,412	$11,269	$3,943
Total assets	92,583	90,481	25,434	27,707	22,109
Deferred revenue	7,638	4,953	3,780	2,943	2,289
Convertible preferred stock	—	—	63,166	63,166	51,288
Total stockholders' equity (deficit)	69,682	72,697	(51,467)	(43,959)	(36,984)

[(1)] Amounts for the years ended December 31, 2016 and 2015 include cash and cash equivalents, investment securities-current and investment securities-noncurrent. We held no investment securities during the years ended December 31, 2014, 2013 and 2012.

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 together with our Consolidated Financial Statements and the related notes included elsewhere in this Annual Report. This discussion and analysis contains forward-looking statements that are based on our current expectations and reflect our plans, estimates and anticipated future financial performance. See the section of this Annual Report entitled “Cautionary Note Regarding Forward-Looking Statements” for additional information. These statements involve numerous risks and uncertainties. Our actual results may differ materially from those expressed or implied by these forward-looking statements as a result of many factors, including those set forth in the section of this Annual Report entitled “Risk Factors.”

Overview

AppFolio is a provider of industry-specific, cloud-based software solutions for SMBs in the property management and legal industries. We were formed in 2006 with a vision to revolutionize the way that small and medium-sized businesses grow and compete.

Our platform is designed to be the system of record to automate essential business processes and the system of engagement to enhance business interactions between our customers and their clients and vendors. Our mobile-optimized software solutions have a user-friendly interface designed for use across multiple devices, enabling our customers to work at any time and from anywhere. Our property management software provides small and medium-sized property managers with an end-to-end solution to their business needs, enabling them to manage their portfolio of properties quickly and easily in a single, integrated environment. Our legal software provides solo practitioners and small law firms with a streamlined practice and case management solution, allowing them to manage their practices and case load within a single system. We also offer optional, but often mission-critical, Value+ services, such as our professionally designed websites and electronic payment services, which are seamlessly built into our core solutions.

We launched our first product, APM, a property management solution, in 2008. Recognizing that our customers would benefit from additional mission-critical services that they can purchase as needed, we launched our first Value+ service in 2009 by offering website design and hosting services to our property manager customers. Our websites give our customers a professional online presence and serve as the hub for our system of engagement. In 2010, we commenced the roll out of our electronic payments platform with the introduction of ACH payment processing and, in 2011, we launched resident screening as additional Value+ services. In 2012, we introduced our tenant liability insurance program as a further Value+ service. Also in 2012, after completing our market validation process, we decided to enter the legal market. We expedited our time-to-market by acquiring MyCase, a legal practice and case management solution, and we leveraged our AppFolio Business System, including our experience gained in the property management vertical, to advance our software solution in the legal vertical. In 2013, we extended our website design and hosting services to our law firm customers and expanded our electronic payments platform for property managers by allowing residents to pay rent by Electronic Cash Payment and credit or debit card. In 2014, we launched an additional Value+ service for our property manager customers with our contact center to resolve or route incoming maintenance requests. In 2016, we launched Premium Leads and Debt Collection Services as additional Value+ services to our property manager customers to assist with filling vacancies and collecting their tenant's unpaid rent. In 2016, we also expanded our electronic payments platform in the legal vertical by allowing clients of our legal customers to pay their legal bills by credit card, debit card, or ACH. Through our disciplined market validation approach and ongoing investment in product development, we continuously update our software solutions through new and innovative core functionality and Value+ services, as well as assess opportunities in adjacent markets and new verticals.

We have focused on growing our revenue by increasing the size of our customer base in the markets we serve, increasing the number of units under management, introducing new or expanded Value+ services, retaining customers, and increasing the adoption and utilization of our Value+ services by new and existing customers. We define our

customer base as the number of customers subscribing to our core solutions, exclusive of free trials. We intend to continue to invest in revenue growth opportunities over time in our current markets, adjacent markets, and new verticals.

Customer count and property manager units under management is summarized in the table below:

	As of December 31,			2015 to 2016	2014 to 2015
	2016	2015	2014	% Change	% Change
Property manager customers	10,038	8,218	5,885	22 %	40 %
Property manager units under management (in millions)	2.68	2.15	1.68	25 %	28 %
Law firm customers	8,135	6,145	3,663	32 %	68 %

We have invested in growth in a disciplined manner across our organization, and intend to continue to do so. These investments to grow our business will continue to increase our costs and operating expenses on an absolute basis. Many of these investments will occur in advance of our realization of revenue or any other benefit and will make it difficult to determine if we are allocating our resources efficiently. We expect cost of revenue, research and product development expense, sales and marketing expense, and general and administrative expense to decrease as a percentage of revenue over the long term as revenue increases and we gain additional operating leverage in our business. As a result of this increased operating leverage, we expect our operating margins will improve over the long term.

To date, we have experienced rapid revenue growth due to our investments in research and product development, sales and marketing, customer service and support, and infrastructure. During the fiscal year ended December 31, 2016, we have derived more than 90% of our revenue from our property management solution, as it has been available for a longer period of time, is more established within its vertical with a larger customer base, and currently offers a greater number of Value+ services.

We have managed, and plan to continue to manage, our business towards the achievement of long-term growth that we believe will positively impact long-term stockholder value, and not towards the realization of short-term financial or business metrics, or short-term stockholder value.

Key Components of Results of Operations

Revenue

We charge our customers on a subscription basis for our core solutions and many of our Value+ services. Our subscription fees are designed to scale to the size of our customers' businesses. We recognize subscription revenue ratably over the terms of the subscription agreements, which typically range from one month to one year. We generally invoice our customers for subscription services in monthly, quarterly or annual installments, typically in advance of the subscription period. Revenue from subscription services is impacted by the change in the number and type of our customers, the size and needs of our customers' businesses, our customer renewal rates, and the level of adoption of our Value+ subscription services by new and existing customers.

We also charge our customers usage-based fees for using certain Value+ services, although fees for electronic payment processing are generally paid by the clients of our customers. Usage-based fees are charged on a flat fee per transaction basis with no minimum usage commitments. We recognize revenue for usage-based services in the period the service is rendered. We generally invoice our customers for usage-based services on a monthly basis for services rendered in the preceding month. Revenue from usage-based services is impacted by the change in the number and type of our customers, the size and needs of our customers' businesses, and the level of adoption and utilization of our Value+ usage-based services by new and existing customers and clients of our customers.

We also offer our customers assistance with on-boarding our core solutions, as well as website design services. These services are generally purchased as part of a subscription agreement, and are typically performed within the first several months of the arrangement. We generally invoice our customers for other services in advance of the services being completed. We recognize revenue for these other services upon completion of the related service. We also generate revenue from legacy RentLinx customers by providing services that allow these customers to advertise rental houses and apartments online. Revenue derived from customers using the RentLinx services outside of our property manager core solution platform is being recorded under other services.

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Costs and Operating Expenses

Cost of Revenue. Cost of revenue consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on customer service and the support of our operations, platform infrastructure costs (such as data center operations and hosting-related costs), fees paid to third-party service providers, payment processing fees, and allocated shared costs. We typically allocate shared costs across our organization based on headcount within the applicable part of our organization. Cost of revenue excludes amortization of capitalized software development costs and acquired technology. We intend to continue to invest in customer service and support, and the expansion of our technology infrastructure as we grow the number of our customers and roll out additional Value+ services. We also intend to expand our Value + offerings over time which will impact cost of revenue both in absolute dollars and overall percentage of revenue.

Sales and Marketing. Sales and marketing expense consists of personnel-related costs (including salaries, sales commissions, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on sales and marketing, costs associated with sales and marketing activities, and allocated shared costs. Marketing activities include advertising, online lead generation, lead nurturing, customer and industry events, industry-related content creation and collateral creation. Sales commissions and other incremental costs to acquire customers and grow adoption and utilization of our Value+ services by new and existing customers are expensed as incurred. We focus our sales and marketing efforts on generating awareness of our software solutions, creating sales leads, establishing and promoting our brands, and cultivating an educated community of successful and vocal customers. We intend to continue to invest in sales and marketing to increase the size of our customer base and increase the adoption and utilization of Value+ services by our new and existing customers.

Research and Product Development. Research and product development expense consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on research and product development, fees for third-party development resources, and allocated shared costs. Our research and product development efforts are focused on enhancing the ease of use and functionality of our existing software solutions by adding new core functionality, Value+ services and other improvements, as well as developing new products. We capitalize the portion of our software development costs that meets the criteria for capitalization. Amortization of capitalized software development costs is included in depreciation and amortization expense. We intend to continue to invest in research and product development as we continue to introduce new core functionality, roll out new Value+ services, develop new products, and expand into adjacent markets and new verticals.

General and Administrative. General and administrative expense consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for employees in our executive, finance, information technology, or IT, human resources, corporate development, legal and administrative organizations. In addition, general and administrative expense includes fees for third-party professional services (including consulting, legal and audit services), other corporate expenses, and allocated shared costs. We intend to incur incremental costs associated with supporting the growth of our business, both in terms of increased headcount and to meet the increased reporting requirements and compliance obligations associated with our operation as a public company.

Depreciation and Amortization. Depreciation and amortization expense includes depreciation of property and equipment, amortization of capitalized software development costs and amortization of intangible assets. We depreciate or amortize property and equipment, software development costs and intangible assets over their expected useful lives on a straight-line basis, which approximates the pattern in which the economic benefits of the assets are consumed. Accounting guidance for internal-use software costs requires that we capitalize and then amortize qualifying internal-use software costs, rather than expense costs as incurred, which has the impact of shifting these expenses to a future period and reducing the impact of these costs on our financial results in the current period. As we continue to invest in our research and product development organization and the development or acquisition of new technology, we expect to have increased capitalized software development costs and incremental amortization.

Interest Income (Expense). Interest expense includes interest paid on outstanding borrowings under our Credit Agreement. Interest income includes interest earned on investment securities, amortization and accretion of the

premium and discounts paid from the purchase of investment securities, interest earned on notes receivable and on cash deposited within our bank accounts.

Results of Operations for the Years Ended December 31, 2016, 2015, and 2014

The following table sets forth our results of operations for the periods presented in dollars (in thousands) and as a percentage of revenue:

	Year Ended December 31,					
	2016		2015		2014	
	Amount	%	Amount	%	Amount	%
Consolidated Statements of Operations Data:						
Revenue	$105,586	100.0 %	$74,977	100.0 %	$47,671	100.0 %
Costs and operating expenses:						
Cost of revenue (exclusive of depreciation and amortization) [1]	44,630	42.3	33,903	45.2	22,555	47.3
Sales and marketing[1]	28,827	27.3	26,076	34.8	16,876	35.4
Research and product development[1]	12,638	12.0	9,554	12.7	6,505	13.6
General and administrative[1]	17,979	17.0	14,343	19.1	6,489	13.6
Depreciation and amortization	9,935	9.4	6,104	8.1	3,805	8.0
Total costs and operating expenses	114,009	108.0	89,980	120.0	56,230	118.0
Loss from operations	(8,423)	(8.0)	(15,003)	(20.0)	(8,559)	(18.0)
Other income (expense), net	(37)	—	5	—	(121)	(0.3)
Interest income (expense), net	246	0.2	(595)	(0.8)	59	0.1
Loss before provision for income taxes	(8,214)	(7.8)	(15,593)	(20.8)	(8,621)	(18.1)
Provision for income taxes	67	0.1	75	0.1	—	—
Net loss	$(8,281)	(7.8)%	$(15,668)	(20.9)%	$(8,621)	(18.1)%

[1] Includes stock-based compensation expense as follows (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Costs and operating expenses:			
Cost of revenue (exclusive of depreciation and amortization)	$471	$124	$68
Sales and marketing	442	115	48
Research and product development	382	41	19
General and administrative	3,006	727	757
Total stock-based compensation expense	$4,301	$1,007	$892

Revenue

	Year Ended December 31,			2015 to 2016 % Change		2014 to 2015 % Change	
	2016	2015	2014				
	(dollars in thousands)						
Core solutions	$43,775	$32,119	$22,406	36	%	43	%
Value+ services	56,965	37,998	22,525	50	%	69	%
Other	4,846	4,860	2,740	—	%	77	%
Total revenues	$105,586	$74,977	$47,671	41	%	57	%

Fiscal 2016 Compared to Fiscal 2015

Revenue increased $30.6 million, or 41%, in 2016 compared to 2015, mainly reflecting increased revenue from a 22% year over year increase in the number of our property manager customers. The overall increase in revenue was mostly attributable to revenue from Value+ services which increased by $19.0 million, or 50% when compared to last year. The increase in Value+ services was mainly driven by increased usage of our electronic payments platform and screening services by a larger property manager customer base, and the increase in property manager units under management of 25% year over year. We also had strong growth in our tenant liability insurance programs, customer contact center and website hosting services offered within our Value+ services. In addition, during 2016 we launched Premium Leads as a Value+ services for our property manager customers. The overall increase in revenue was also the result of an increase in revenue from our Core solutions of $11.7 million, or 36%, driven by the growth in the number of our customers, units under management, and strong customer renewal rates.

In each of 2016, 2015 and 2014, we derived more than 90% of our revenue from our property manager customers.

Fiscal 2015 Compared to Fiscal 2014

Revenue increased $27.3 million, or 57%, in 2015 compared to 2014, mainly reflecting increased revenue from a 40% year over year increase in the number of our property manager customers. The overall increase was mostly attributable to revenue from Value+ services which increased by $15.5 million, or 69%, when compared to last year. The increase in Value+ services revenue was mainly driven by increased usage of our electronic payments platform, screening services and tenant liability insurance programs resulting from a larger property manager customer base and an increase in property manager units under management of 28% year over year. The overall increase in revenue was also the result of an increase in revenue from our core solutions of $9.7 million, or 43%, driven by growth in the number of our customers, units under management and strong customer renewal rates. The increase in other revenue of $2.1 million, or 77% was primarily the result of an increase in fees for website design fees and incremental revenue gained from the acquisition of RentLinx.

Cost of Revenue (Exclusive of Depreciation and Amortization)

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Cost of revenue (exclusive of depreciation and amortization)	$44,630	$33,903	$22,555	32 %	50 %
Percentage of revenue	42.3 %	45.2 %	47.3 %		

Fiscal 2016 Compared to Fiscal 2015

Cost of revenue (exclusive of depreciation and amortization) increased $10.7 million, or 32%, in 2016 compared to 2015. The increase was primarily due to increased third-party costs of $5.0 million driven by increased Value+ services, increased personnel-related costs of $3.9 million due to our headcount growth, as well as increased allocated and other costs of $1.8 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

As a percentage of revenue, cost of revenue (exclusive of depreciation and amortization) improved 2.9 percentage points in 2016 compared to 2015. The improvement was primarily driven by a decrease in personnel-related costs due to our ability to increase revenue with a more moderate increase in headcount, and a decrease in third-party costs due to improved pricing with our third-party service providers as we continue to grow.

Fiscal 2015 Compared to Fiscal 2014

Cost of revenue (exclusive of depreciation and amortization) increased $11.3 million, or 50%, in 2015 compared to 2014. The increase was primarily due to increased third-party costs of $5.4 million driven by increased Value+ services, increased personnel-related costs of $4.5 million due to our headcount growth, as well as increased allocated and other costs of $1.4 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

As a percentage of revenue, cost of revenue (exclusive of depreciation and amortization) improved 2.1 percentage points in 2015 compared to 2014. The improvement was primarily driven by a decrease in personnel-related costs and other costs due to our ability to increase revenue with a more moderate increase in headcount and supporting infrastructure.

Sales and Marketing

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Sales and marketing	$28,827	$26,076	$16,876	11 %	55 %
Percentage of revenue	27.3 %	34.8 %	35.4 %		

Fiscal 2016 Compared to Fiscal 2015

Sales and marketing expense increased $2.8 million, or 11%, in 2016 compared to 2015. The increase was primarily due to increased personnel-related costs of $2.6 million due to our headcount growth and related commission based compensation, and increased allocated and other costs of $0.2 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

Fiscal 2015 Compared to Fiscal 2014

Sales and marketing expense increased $9.2 million, or 55%, in 2015 compared to 2014. The increase was primarily due to increased personnel-related costs of $5.6 million due to our headcount growth and related commission based compensation, increased marketing program costs of $2.5 million incurred to support incremental revenue growth, and increased allocated and other costs of $1.0 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

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Research and Product Development

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Research and product development	$12,638	$9,554	$6,505	32 %	47 %
Percentage of revenue	12.0%	12.7%	13.6%		

Fiscal 2016 Compared to Fiscal 2015

Research and product development expense increased $3.1 million, or 32%, in 2016 compared to 2015. The increase was primarily due to increased personnel-related costs, net of capitalized software development costs of $1.9 million, due to our headcount growth and rate of innovation and increased allocated and other costs of $1.1 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

Fiscal 2015 Compared to Fiscal 2014

Research and product development expense increased $3.0 million, or 47%, in 2015 compared to 2014. The increase was primarily due to increased personnel-related costs, net of capitalized software development costs of $2.1 million, due to our headcount growth and rate of innovation and increased allocated and other costs of $1.0 million driven by expanded facilities, information technology and other shared expenses supporting our growth.

General and Administrative

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
General and administrative	$17,979	$14,343	$6,489	25 %	121 %
Percentage of revenue	17.0%	19.1 %	13.6%		

Fiscal 2016 Compared to Fiscal 2015

General and administrative expense increased $3.6 million, or 25%, in 2016 compared to 2015. The increase was primarily due to increased personnel-related costs of $4.4 million due to headcount growth and incentive-based compensation programs partially off-set by decreased allocated and other costs of $0.7 million related to certain costs incurred in 2015 for our initial public offering, or IPO, and incremental compensation paid to certain RentLinx personnel related to the acquisition that did not reoccur in 2016.

Fiscal 2015 Compared to Fiscal 2014

General and administrative expense increased $7.9 million, or 121%, in 2015 compared to 2014. The increase was primarily due to increased allocated and other costs of $4.6 million and increased personnel-related costs of $3.2 million due to our headcount growth. The increase in allocated and other costs included increased professional fees of $3.1 million in connection with our IPO, a $0.6 million payment to a third-party service provider to expedite our transition to a new partner, $0.3 million of legal fees associated with the acquisition of RentLinx, and increased allocated and other costs driven by expanded facilities, information technology and other shared expenses supporting our growth.

Depreciation and Amortization

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Depreciation and amortization	$9,935	$6,104	$3,805	63 %	60 %
Percentage of revenue	9.4%	8.1 %	8.0 %		

Fiscal 2016 Compared to Fiscal 2015

Depreciation and amortization expense increased $3.8 million, or 63%, in 2016 compared to 2015. The increase was primarily due to increased amortization expense of $2.8 million related to increased capitalized software development balances and increased depreciation expense of $0.9 million from capital purchases and building improvements made during 2016.

Fiscal 2015 Compared to Fiscal 2014

Depreciation and amortization expense increased $2.3 million, or 60%, in 2015 compared to 2014. The increase was primarily due to increased amortization expense of $1.5 million related to increased capitalized software development balances, increased depreciation expense of $0.4 million from capital purchases made during 2015, and increased amortization of intangible assets of $0.4 million from the acquisition of RentLinx.

Interest Income (Expense), net

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Interest income (expense)	$246	$(595)	$59	N/A	N/A
Percentage of revenue	0.2 %	(0.8)%	0.1 %		

Fiscal 2016 Compared to Fiscal 2015

Interest income, net increased by $0.8 million in 2016 compared to 2015. The increase is primarily due to holding investment securities for a full year in 2016 versus a few months in 2015 resulting in increased interest income of $0.2 million. In addition, interest expense decreased $0.6 million related to our term loan repaid in 2015 and the associated write-off of deferred financing costs.

Fiscal 2015 Compared to Fiscal 2014

Interest expense, net increased by $0.7 million in 2015 compared to 2014. The increase is primarily due to the interest expense recognized from the write-off of deferred financing costs associated with the repayment of our term loan in 2015 and interest expense incurred pursuant to the Original Credit Agreement of $0.8 million. The interest expense was offset by $0.2 million of interest income from our investment securities. For additional information regarding our Original Credit Agreement refer to Note 8, Long-term Debt, of our Consolidated Financial Statements.

Provision for Income Taxes

	Year Ended December 31,			2015 to 2016 % Change	2014 to 2015 % Change
	2016	2015	2014		
	(dollars in thousands)				
Provision for income taxes	$67	$75	$ —	(11)%	—%
Percentage of revenue	0.1 %	0.1 %	—%		

The provision for income taxes for the years ended December 31, 2016 and 2015, of $67,000 and $75,000, respectively is related to minimum state taxes and the amortization of tax deductible goodwill from the purchase of RentLinx in 2015 that is not an available source of income to realize the deferred tax asset.

Quarterly Results of Operations

The following table sets forth selected unaudited quarterly consolidated statements of operations data for each of the eight quarters in the period ended December 31, 2016. We have prepared the unaudited quarterly consolidated statements of operations data on a basis consistent with the audited annual Consolidated Financial Statements included elsewhere in this Annual Report. In the opinion of management, the financial information in this table reflects all adjustments, consisting of normal and recurring adjustments, necessary for the fair statement of this data. This information should be read in conjunction with the Consolidated Financial Statements and related notes included elsewhere in this Annual Report. The results of historical periods are not necessarily indicative of the results for any future period.

	Quarter Ended							
	2016				2015			
	December 31,	September 30,	June 30,	March 31,	December 31,	September 30,	June 30,	March 31,
	(in thousands, except per share data)							
Consolidated Statements of Operations Data:								
Revenue	$28,010	$28,162	$26,203	$23,211	$20,399	$20,305	$18,425	$15,848
Costs and operating expenses:								
Cost of revenue (exclusive of depreciation and amortization)(1)	11,243	11,645	11,212	10,530	9,465	9,264	8,109	7,065
Sales and marketing(1)	6,730	6,979	7,567	7,551	7,100	7,028	6,239	5,709
Research and product development(1)	3,107	3,464	3,024	3,043	2,594	2,797	2,154	2,009
General and administrative(1)	5,399	4,642	4,389	3,549	3,356	3,888	3,707	3,392
Depreciation and amortization	2,823	2,636	2,359	2,117	1,852	1,638	1,431	1,183
Total costs and operating expenses	29,302	29,366	28,551	26,790	24,367	24,615	21,640	19,358
Operating loss	(1,292)	(1,204)	(2,348)	(3,579)	(3,968)	(4,310)	(3,215)	(3,510)
Other income (expense), net	(3)	(12)	2	(24)	13	(1)	(5)	(2)
Interest income (expense), net	25	102	95	24	106	(426)	(243)	(32)
Loss before income taxes	(1,270)	(1,114)	(2,251)	(3,579)	(3,849)	(4,737)	(3,463)	(3,544)
Provision for income taxes	19	11	13	24	41	23	(63)	74
Net loss	$(1,289)	$(1,125)	$(2,264)	$(3,603)	$(3,890)	$(4,760)	$(3,400)	$(3,618)
Net loss per share, basic and diluted	$(0.04)	$(0.03)	$(0.07)	$(0.11)	$(0.12)	$(0.14)	$(0.36)	$(0.41)

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

	Quarter Ended							
	2016				2015			
	December 31,	September 30,	June 30,	March 31,	December 31,	September 30,	June 30,	March 31,
	(in thousands)							
Cost of revenue (exclusive of depreciation and amortization)	$150	$ 138	$138	$ 45	$38	$ 35	$27	$ 24
Sales and marketing	146	124	130	42	31	33	28	23
Research and product development	118	109	104	51	19	10	7	5
General and administrative	1,043	918	720	325	296	200	150	81

Total stock-based compensation expense	$1,457	$ 1,289	$1,092	$463	$384	$ 278	$212	$133

The following table sets forth selected consolidated statements of operations data for the specified periods as a percentage of our revenue for those periods.

	Quarter Ended							
	2016				2015			
	December 31,	September 30,	June 30,	March 31,	December 31,	September 30,	June 30,	March 31,
Consolidated Statements of Operations Data:								
Revenue	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %
Costs and operating expenses:								
Cost of revenue (exclusive of depreciation and amortization)	40.1 %	41.4 %	42.8 %	45.4 %	46.4 %	45.6 %	44.0 %	44.6 %
Sales and marketing	24.0 %	24.8 %	28.9 %	32.5 %	34.8 %	34.6 %	33.9 %	36.0 %
Research and product development	11.1 %	12.3 %	11.5 %	13.1 %	12.7 %	13.8 %	11.7 %	12.7 %
General and administrative	19.3 %	16.5 %	16.7 %	15.3 %	16.5 %	19.1 %	20.1 %	21.4 %
Depreciation and amortization	10.1 %	9.4 %	9.0 %	9.1 %	9.1 %	8.1 %	7.8 %	7.5 %
Total costs and operating expenses	104.6 %	104.3 %	109.0 %	115.4 %	119.5 %	121.2 %	117.4 %	122.1 %
Operating loss	(4.6)%	(4.3)%	(9.0)%	(15.4)%	(19.5)%	(21.2)%	(17.4)%	(22.1)%
Other expense, net	— %	— %	— %	(0.1)%	0.1 %	— %	— %	— %
Interest income (expense), net	0.1 %	0.4 %	0.4 %	0.1 %	0.5 %	(2.1)%	(1.3)%	(0.2)%
Loss before income taxes	(4.5)%	(4.0)%	(8.6)%	(15.4)%	(18.9)%	(23.3)%	(18.8)%	(22.4)%
Provision for income taxes	0.1 %	— %	— %	0.1 %	0.2 %	0.1 %	(0.3)%	0.5 %
Net loss	(4.6)%	(4.0)%	(8.6)%	(15.5)%	(19.1)%	(23.4)%	(18.5)%	(22.8)%

Quarterly Revenue and Cost Trends

Our quarterly revenue trends generally reflect increased revenue from our property manager customers. The overall increase was primarily a result of a quarter-over-quarter increase in the number of our customers, property manager units under management, as well as strong customer renewal rates, and an increase in Value+ services revenue primarily attributable to the expansion of our electronic payments platform and screening services. We experience some seasonality in our revenue, primarily with respect to the screening services we provide to our property manager customers. These customers historically have processed fewer applications for new tenants during the fourth quarter holiday season; therefore, revenue associated with our screening services and new tenant applications typically declines in the fourth quarter of the year. As a result of this seasonal decline in revenue, we have typically experienced slower revenue growth in the fourth quarter of each year (and a slight decline in revenue in the fourth quarter of 2016) than we have experienced in other quarters.

Our quarter-over-quarter total costs and operating expenses as a percentage of revenue for each quarter during 2016 improved, with the exception of general and administrative expenses and depreciation and amortization, as we continue to realize operating leverage. General and administrative expenses fluctuated each quarter during 2016 primarily due to the impact of increased compensation due to an increase in headcount.

Our quarter-over-quarter total costs and operating expenses as a percentage of revenue for each quarter during 2015 remained consistent and scaled with the growth in our business.

Liquidity and Capital Resources

Cash and Cash Equivalents

As of December 31, 2016, and 2015, our principal sources of liquidity were cash and cash equivalents and investment securities, which had an aggregate balance of $52.9 million and $56.7 million, respectively.

Working Capital

As of December 31, 2016, we had working capital of $10.9 million, compared to working capital of $10.6 million as of December 31, 2015. The increase in our working capital was primarily due to an increase in the current portion of investment securities, accounts receivable and prepaid expenses and a decline in accounts payable, offset by increases in our accrued employee expenses, accrued expenses and deferred revenue from the continued growth of our business

and a decline in our cash and cash equivalents.

Revolving Facility

As of December 31, 2016, we had a $25.0 million revolving line of credit, which we refer to as the Revolving Facility, under the terms of the Credit Agreement with Wells Fargo, as administrative agent, and the lenders and parties thereto. As of December 31, 2016, we had no outstanding balance under the Revolving Facility. As of December 31, 2015, we had an outstanding balance of $12,000. For additional information regarding our Credit Agreement refer to Note 8, Long-term Debt of our Consolidated Financial Statements.

Liquidity Requirements

We believe that our existing cash and cash equivalents, investment securities, available borrowing capacity of $25.0 million under the Revolving Facility, and cash generated from operating activities will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months.

Capital Requirements

Our future capital requirements will depend on many factors, including the continued market acceptance of our software solutions, the change in the number of our customers, the adoption and utilization of our Value+ services by new and existing customers, the timing and extent of the introduction of new core functionality and Value+ services in our existing markets and verticals, the timing and extent of our expansion into adjacent markets or new verticals and the timing and extent of our investments across our organization. In addition, we may in the future enter into arrangements to acquire or invest in complementary businesses, services, technologies or intellectual property rights, although we have no present plans with respect to any acquisitions or investments.

Cash Flows

The following table summarizes our cash flows for the periods indicated (in thousands):

	Years Ended December 31,		
	2016	2015	2014
Net cash provided by (used in) operating activities	$11,500	$(6,844)	$475
Net cash used in investing activities	(13,065)	(59,367)	(6,476)
Net cash provided by financing activities	201	72,862	144
Net (decrease) increase in cash and cash equivalents	$(1,364)	$6,651	$(5,857)

Cash Provided by (Used in) Operating Activities

Our primary source of operating cash inflows is cash collected from our customers in connection with their use of our core solutions and Value+ services. Our primary uses of cash from operating activities are for personnel-related expenditures and third-party costs incurred to support the delivery of our software solutions.

For the year ended December 31, 2016, cash provided by operating activities was $11.5 million resulting from our net loss of $8.3 million, adjusted by non-cash charges of $14.7 million and a net increase in our operating assets and liabilities of $5.0 million. The non-cash charges primarily consist of $9.9 million of depreciation and amortization of our property and equipment and capitalized software and $4.3 million of stock-based compensation. The net increase in our operating assets and liabilities was mostly attributable to an increase of $2.7 million in deferred revenue in line with our increased revenues, a $2.2 million increase in accrued employee expenses related to an overall increase in personnel-related costs, and a $1.1 million increase in accrued expenses primarily due to payment processing fees and fees associated with our resident screening services driven by growth in our Value+ services, and a $0.8 million increase in other liabilities. The increase in our operating assets and liabilities was partially offset by a decrease in accounts payable of $0.9 million, an increase in accounts receivable of $0.5 million, and an increase in our prepaid expenses and current assets of $0.4 million, in conjunction with our growth and expansion during 2016.

For the year ended December 31, 2015, cash used in operating activities was $6.8 million resulting from our net loss of $15.7 million, adjusted by non-cash charges of $6.8 million and a net increase in our operating assets and liabilities of $2.1 million. The net increase in our non-cash charges was primarily the result of an increase of $6.1 million of depreciation and amortization of our property and equipment and capitalized software and $1.0 million of stock-based compensation. The net increase in our operating assets and liabilities was mostly attributable to an increase of $1.9 million in accrued employee expenses related to an overall increase in personnel-related costs, a $1.2 million increase

in deferred revenue in line with our increased

revenues, a $1.1 million increase in accrued expenses mostly attributed to payment processing fees driven by growth in our Value+ services, and a $1.0 million increase in other liabilities. The increase in our operating assets and liabilities was offset by an increase in our prepaid expenses and current assets of $1.9 million, an increase in accounts receivable of $0.7 million in conjunction with our growth and expansion during 2015, and a decrease in accounts payable of $0.4 million.

For the year ended December 31, 2014, cash provided by operating activities was $0.5 million resulting from our net loss of $8.6 million, adjusted by non-cash charges of $4.9 million and a net increase of $4.2 million in our operating assets and liabilities. The net increase in our non-cash charges was primarily the result of an increase of $3.8 million of depreciation and amortization of our property and equipment and capitalized software, and $0.9 million of stock-based compensation. The net increase in our operating assets and liabilities was primarily the result of a $1.8 million increase in accounts payable, a $1.1 million increase in accrued employee expenses related to an overall increase in personnel-related costs, a $1.0 million increase in accrued expenses due to an overall increase in expenditures associated with the growth of our business, and a $0.8 million increase in deferred revenue as a result of increased subscription sales, offset by a $0.4 million decrease in accounts receivable as a result of improved collections.

Cash Used in Investing Activities

Cash used in investing activities is generally comprised of purchases, maturities and sales of investment securities, additions to capitalized software development, cash paid for business acquisitions and purchases and dispositions of capital expenditures.

For the year ended December 31, 2016, investing activities used $13.1 million in cash primarily as a result of $31.6 million of investment securities purchased offset by $21.3 million of maturities and $12.6 million of sales of investment securities. In addition, we had an increase in capitalized software development costs of $11.2 million for the continued investment in our software development, and capital expenditures of $4.2 million to purchase property and equipment for the continued growth and expansion of our business.

For the year ended December 31, 2015, investing activities used $59.4 million in cash primarily as a result of $74.2 million of investment securities purchased offset by $26.1 million of maturities and $4.1 million of sales of investment securities. In addition, we had an increase in capitalized software development costs of $7.7 million for the continued investment in our software development, an increase in capital expenditures of $3.7 million to purchase property and equipment for the continued growth and expansion of our business. We also used $4.0 million of cash for the acquisition of RentLinx.

For the year ended December 31, 2014, investing activities used $6.5 million in cash primarily as a result of an increase in capitalized software development costs of $4.6 million, and an increase in capital expenditures of $1.9 million to purchase property and equipment.

Cash Provided by Financing Activities

Cash provided by financing activities is generally comprised of proceeds from our IPO, proceeds from the exercise of stock options and restricted stock awards, proceeds from the issuance of debt or draws from our revolving credit facility and principal repayments of our term loan and on our revolving credit facility.

For the year ended December 31, 2016, financing activities provided $0.2 million in cash primarily as a result of proceeds from stock option exercises offset by tax withholdings from restricted stock unit, or RSU, net settlements.

For the year ended December 31, 2015, financing activities provided $72.9 million in cash primarily as a result of net proceeds from the IPO in the amount of $75.4 million, offset by a $2.4 million earnout payment relating to our acquisition of MyCase.

For the year ended December 31, 2014, financing activities provided $0.1 million in cash primarily as a result of proceeds from the exercise of stock options.

Contractual Obligations and Other Commitments

Our principal commitments consist of contractual obligations under our operating leases for office space. The following table summarizes our contractual obligations and other commitments as of December 31, 2016:

	Payments Due by Period				
	Total	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years
	(in thousands)				
Operating lease obligations	$8,292	$2,375	$3,449	$2,288	$180

At December 31, 2016, liabilities for unrecognized tax benefits of $4.0 million were not included in our contractual obligations in the table above because, due to their nature, there is a high degree of uncertainty regarding the timing of future cash outflows and other events that would extinguish these liabilities.

In February 2017, we signed a lease amendment for 50 Castilian Drive in Santa Barbara, California, our corporate headquarters. This amendment extends the term from February 2018 to December 2021. The total commitment under this lease extension is $3.1 million. All other terms and conditions from the original lease and previous amendments remain the same.

For additional information regarding our contractual obligations, commitments and indemnification arrangements refer to Note 9, Commitments and Contingencies of our Consolidated Financial Statements.

Off-Balance Sheet Arrangements

As of December 31, 2016, we did not have any off-balance sheet arrangements.

Critical Accounting Policies and Estimates

Our financial statements and the related notes included elsewhere in this Annual Report are prepared in accordance with GAAP. The preparation of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and operating expenses, provision for income taxes and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. However, actual results could differ significantly from the estimates made by our management. We evaluate our estimates and assumptions on an ongoing basis. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

We believe that the following critical accounting policies involve a greater degree of judgment or complexity than our other accounting policies. Accordingly, these are the policies we believe are the most critical to a full understanding and evaluation of our Consolidated Financial Statements. For additional information, refer to Note 2, Summary of Significant Accounting Policies of our Consolidated Financial Statements.

Revenue Recognition

We primarily generate revenue from our customers on a subscription basis for our core solutions and Value+ services for our cloud-based property management and legal software solutions. Subscription fees for our core solutions are charged on a per-unit per-month basis for our property management software solution and on a per-user per-month basis for our legal software solution. We recognize subscription revenue on a straight-line basis over the terms of the subscription agreements, which range from one month to one year. We generally invoice our customers for subscription services in monthly, quarterly or annual installments, typically in advance of the subscription period. Any revenues which are billed in advance are recorded as deferred revenue.

We also charge our customers on a subscription basis for many of our Value+ services. Our subscription fees are designed to scale to the size of our customers' businesses. We charge our customers usage-based fees for using certain Value+ services, although fees for electronic payment processing are generally paid by the clients of our customers. Usage-based fees are charged on a flat fee per transaction basis with no minimum usage commitments. We recognize

revenue for usage-based services in the period the service is rendered. We generally invoice our customers for usage-based services on a monthly basis for services rendered in the preceding month.

Our legal software core solution offers our customers a free-trial period to try our software. Revenue is not recognized until the free-trial period is complete and the customer has entered into a subscription agreement with us.

We recognize revenue when (i) there is persuasive evidence of an arrangement, (ii) our software solutions have been made available or delivered, or services have been performed, (iii) the amount of fees is fixed or determinable, and (iv) collectability is reasonably assured. Evidence of an arrangement generally consists of either a signed customer contract or an online click-through agreement. We consider that delivery of a solution or website has commenced once we provide the customer with access to use the solution or website. Fees are fixed based on rates specified in the subscription agreements, which do not provide for any refunds or adjustments. If collectability is not considered reasonably assured, revenue is deferred until the fees are collected. Some of our subscription agreements contain minimum cancellation fees in the event that the customer cancels the subscription early.

Internal-Use Software

We account for the costs of computer software obtained or developed for internal use in accordance with Accounting Standards Codification ("ASC") 350, Intangibles-Goodwill and Other ("ASC 350"). These include costs incurred in connection with the development of our internal-use software solutions when (i) the preliminary project stage is completed, (ii) management has authorized further funding for the completion of the project and (iii) it is probable that the project will be completed and perform as intended. These capitalized costs include personnel and related expenses for employees who are directly associated with and who devote time to internal-use software projects and, when material, interest costs incurred during the development. Capitalization of these costs ceases once the project is substantially complete and the software is ready for its intended purpose. Costs incurred for significant upgrades and enhancements to our software solutions are also capitalized. Costs incurred for post-configuration training, maintenance and minor modifications or enhancements are expensed as incurred. Capitalized software development costs are amortized using the straight-line method over an estimated useful life of three years. We do not transfer ownership of our software, or lease our software, to third parties.

Business Combinations

The results of a business acquired in a business combination are included in our consolidated financial statements from the date of acquisition. We allocate the purchase price, including the fair value of contingent consideration, to the identifiable assets and liabilities of the acquired business at their acquisition date fair values. The excess of the purchase price over the amount allocated to the identifiable assets and liabilities, if any, is recorded as goodwill. Determining the fair value of assets acquired and liabilities assumed requires management to make significant judgments and estimates, including the selection of valuation methodologies, estimates of future revenue and cash flows, discount rates and selection of comparable companies.

Acquisition-related transaction costs are not included as a component of consideration transferred, but are accounted for as an operating expense in the period in which the costs are incurred.

Goodwill and Intangible Assets

Goodwill and intangible assets are evaluated for impairment annually in the fourth quarter or whenever events or circumstances indicate the carrying value of goodwill may not be recoverable or when there is a triggering event. Triggering events that may indicate impairment include, but are not limited to, a significant adverse change in customer demand or business climate or a significant decline in expected cash flows.

When evaluating goodwill for impairment, an entity has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then additional impairment testing is not required. However, if an entity concludes otherwise, then it is required to perform the first of a two-step impairment test.

The first step of the impairment test involves comparing the estimated fair value of a reporting unit with its book value, including goodwill. If the estimated fair value exceeds book value, goodwill is considered not to be impaired and no additional steps are necessary. If, however, the fair value of the reporting unit is less than book value, then the carrying amount of the goodwill is compared with its implied fair value. The estimate of implied fair value of goodwill may require valuations of certain internally generated and unrecognized intangible assets. If the carrying

amount of goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to the excess above the estimated fair value.

At December 31, 2016, we determined our goodwill was not impaired as the fair value of our reporting unit significantly exceeded its carrying value.

Stock-Based Compensation

We account for stock-based compensation awards granted to employees and directors by recording compensation expense based on the awards' grant-date estimated fair value, in accordance with ASC 718, Compensation-Stock Compensation ("ASC 718") over the vesting period. We estimate the fair value of restricted stock awards ("RSA"), restricted stock units ("RSU") and performance based RSUs ("PSU") based on the fair value of our common stock on the date of grant. We estimate the fair value of stock options and performance based stock options ("PSO") using the Black-Scholes option-pricing model. Determining the fair value of stock options under this model requires highly subjective assumptions, including the fair value of the underlying common stock, the risk-free interest rate, the expected term of the award, the expected volatility of the price of our common stock, and the expected dividend yield of our common stock. These estimates involve inherent uncertainties and the application of management's judgment. If we had made different assumptions, our stock-based compensation expense could have been materially different. Since our IPO in June 2015, the fair value of our common stock is based on the closing price of our common stock, as quoted on the NASDAQ Global Market, on the date of grant.

Prior to our IPO, there was no public market for our common stock and our board of directors determined the fair value of our common stock at the time of the grant of stock options and restricted stock awards by considering a number of objective and subjective factors, including our actual operating and financial performance, market conditions and performance of comparable publicly traded companies, developments and milestones in our company, the likelihood of achieving a liquidity event and transactions involving our convertible preferred stock, among other factors. The fair value of the underlying common stock was determined by our board of directors in accordance with applicable elements of the practice aid issued by the American Institute of Certified Public Accountants Valuation of Privately Held Company Equity Securities Issued as Compensation. In valuing our common stock at various dates, our board of directors determined our equity value generally using the income approach and the market comparable approach valuation methods. Once we determined our equity value, we used an option pricing method or the Probability Weighted Expected Return Method to allocate the equity value to preferred stock and common stock. Application of these approaches and methods involves the use of estimates, judgments and assumptions, such as future revenue, expenses and cash flows, selections of comparable companies, probabilities and timing of exit events, and other factors.

The Black-Scholes option-pricing model utilizes the following assumptions and estimates in the calculation of the fair value for options and PSOs:

Risk-Free Interest Rate - The risk free interest rate assumption is based upon observed interest rates on United States government securities appropriate for the expected term of the stock option.

Expected Term - Given we do not have sufficient exercise history to develop reasonable expectations about future exercise patterns and post-vesting employment termination behavior, we determine the expected term using the simplified method, which is calculated as the midpoint of the stock option vesting term and the expiration date of the stock option.

Expected Volatility - We determine the expected volatility based on the historical average volatilities of publicly traded industry peers. We intend to continue to consistently apply this methodology using the same or similar public companies until a sufficient amount of historical information regarding the volatility of our own common stock price becomes available, unless circumstances change such that the identified companies are no longer similar to us, in which case, more suitable companies whose stock prices are publicly available would be utilized in the calculation.

Expected Dividend Yield - We have not paid and do not anticipate paying any cash dividends in the foreseeable future and, therefore, we use an expected dividend yield of zero.

In 2016, we began granting PSOs and PSUs. The fair value of the PSOs are estimated using the Black-Scholes option-pricing model and the PSUs fair value is based on the fair value of our common stock on the date of grant. The vesting of the PSOs and PSUs is based on achievement of a pre-established free cash flow performance metric and continued employment throughout the performance period. We recognize expense for the PSOs and PSUs based on the grant date fair value and combined with the determination of the probability of the number of shares that will vest at the end of the performance period. Adjustments to compensation expense are made each period based on changes in our estimate of the number of PSOs and PSUs that are probable of vesting.

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In addition to the assumptions used in the Black-Scholes option-pricing model, we also estimate a forfeiture rate to calculate our stock-based compensation expense. The forfeiture rate is based on an analysis of actual forfeitures for each type of grant made. We will continue to evaluate the appropriateness of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover, and other factors. Changes in the estimated forfeiture rate can have a significant impact on our stock-based compensation expense as the cumulative effect of adjusting the rate is recognized in the period the estimated forfeiture rate is changed. If a revised forfeiture rate is higher than the previously estimated forfeiture rate, an adjustment is made that will result in a decrease to our stock-based compensation expense recognized in our consolidated financial statements. If a revised forfeiture rate is lower than the previously estimated forfeiture rate, an adjustment is made that will result in an increase to our stock-based compensation expense recognized in our consolidated financial statements.

We will continue to use judgment in evaluating the expected volatility, expected term and forfeiture rate utilized in our stock-based compensation expense calculations on a prospective basis. As we continue to accumulate additional data related to our common stock, we may refine our estimates of expected volatility, expected term and forfeiture rates, which could materially impact our future stock-based compensation expense.

Income Taxes

We account for income taxes in accordance with ASC 740, Income Taxes, or ASC 740. ASC 740 requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the consolidated statements of operations in the period that includes the enactment date. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets will not be realized.

We 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 our consolidated financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized. We recognize interest and penalties accrued with respect to uncertain tax positions, if any, in our provision for income taxes in the consolidated statements of operations.

Recent Accounting Pronouncements

For information regarding recent accounting pronouncements, refer to Note 2, Summary of Significant Accounting Policies of our Consolidated Financial Statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Interest Rate Risk

At December 31, 2016, we had cash and cash equivalents of $10.7 million consisting of bank deposits and money market funds and $42.2 million of investment securities which are comprised of fixed rate debt securities and certificates of deposit. We did not purchase these investments for trading or speculative purposes and have not used any derivative financial instruments to manage our interest rate risk exposure.

In September 2015, we began investing in corporate debt securities, agency securities and certificate of deposits which we collectively refer to as investment securities. The primary objective of investing in the securities is to support our liquidity and capital needs. Our investment securities are exposed to market risk due to interest rate fluctuations. While fluctuations in interest rates do not impact our interest income from our investment securities as all of these securities have fixed interest rates, changes in interest rates may impact the fair value of the investment securities. Since our investment securities are held as available for sale, all changes in fair value impact our other comprehensive income unless an investment security is considered impaired in which case changes in fair value are reported in other expense. As of December 31, 2016, a hypothetical 100 basis point decrease in interest rates would have resulted in an approximate increase in fair value or unrealized gain of $0.5 million and a hypothetical 100 basis point decrease in interest rates would have resulted in an approximate decrease in fair value or unrealized loss of $0.5 million. This estimate is based on a sensitivity model which measures an instant change in interest rates by 1% or 100 basis points at December 31, 2016.

Inflation Risk

We have not been exposed to, nor do we anticipate being exposed to, material risks due to changes in inflation rates.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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The supplementary financial information required by this Item 8 is included in Item 7 under the caption "Quarterly Results of Operations."

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
To the Board of Directors and Stockholders of AppFolio, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, comprehensive loss, and convertible preferred stock and stockholders' deficit present fairly, in all material respects, the financial position of AppFolio, Inc. and its subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.
/s/ PricewaterhouseCoopers LLP
Los Angeles, California
February 27, 2017

APPFOLIO, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except par values)

	December 31,	
	2016	2015
Assets		
Current assets		
Cash and cash equivalents	$10,699	$12,063
Investment securities—current	15,473	10,235
Accounts receivable, net	2,511	2,048
Prepaid expenses and other current assets	3,537	3,160
Total current assets	32,220	27,506
Investment securities—noncurrent	26,688	34,417
Property and equipment, net	7,077	6,107
Capitalized software, net	15,539	10,022
Goodwill	6,737	6,737
Intangible assets, net	3,105	4,516
Other assets	1,217	1,176
Total assets	$92,583	$90,481
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$937	$2,369
Accrued employee expenses	7,550	5,159
Accrued expenses	4,044	3,340
Deferred revenue	7,638	4,953
Other current liabilities	1,192	1,084
Total current liabilities	21,361	16,905
Other liabilities	1,540	879
Total liabilities	22,901	17,784
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, $0.0001 par value, 25,000 authorized and no shares issued and outstanding as of December 31, 2016 and 2015	—	—
Class A common stock, $0.0001 par value, 250,000 shares authorized as of December 31, 2016 and 2015; 11,691 and 9,005 shares issued and outstanding as of December 31, 2016 and 2015, respectively	1	1
Class B common stock, $0.0001 par value, 50,000 shares authorized as of December 31, 2016 and 2015; 22,028 and 24,541 shares issued and outstanding as of December 31, 2016 and 2015, respectively	3	3
Additional paid-in capital	146,692	141,528
Accumulated other comprehensive loss	(51)	(153)
Accumulated deficit	(76,963)	(68,682)
Total stockholders' equity	69,682	72,697
Total liabilities and stockholders' equity	$92,583	$90,481

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

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APPFOLIO, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)

	Year Ended December 31,		
	2016	2015	2014
Revenue	$105,586	$74,977	$47,671
Costs and operating expenses:			
Cost of revenue (exclusive of depreciation and amortization)	44,630	33,903	22,555
Sales and marketing	28,827	26,076	16,876
Research and product development	12,638	9,554	6,505
General and administrative	17,979	14,343	6,489
Depreciation and amortization	9,935	6,104	3,805
Total costs and operating expenses	114,009	89,980	56,230
Loss from operations	(8,423)	(15,003)	(8,559)
Other income (expense), net	(37)	5	(121)
Interest income (expense), net	246	(595)	59
Loss before provision for income taxes	(8,214)	(15,593)	(8,621)
Provision for income taxes	67	75	—
Net loss	$(8,281)	$(15,668)	$(8,621)
Net loss per share, basic and diluted	(0.25)	(0.73)	(0.98)
Weighted average common shares outstanding, basic and diluted	33,561	21,336	8,757

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

APPFOLIO, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(in thousands)

	Year Ended December 31,		
	2016	2015	2014
Net loss	$(8,281)	$(15,668)	$(8,621)
Other comprehensive income (loss):			
Changes in unrealized gains (losses) on investment securities	102	(153)	—
Comprehensive loss	$(8,179)	$(15,821)	$(8,621)

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

APPFOLIO, INC.
CONSOLIDATED STATEMENTS OF CONVERTIBLE
PREFERRED STOCK AND STOCKHOLDERS' EQUITY (DEFICIT)
(in thousands)

	Convertible Preferred Stock		Common Stock Class A		Common Stock Class B		Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total
	Shares	Amount	Shares	Amount	Shares	Amount				
Balance December 31, 2013	68,027	$63,166	—	$ —	8,871	$ 1	$433	$ —	$(44,393)	$(43,959)
Exercise of stock options	—	—	—	—	171	—	168	—		168
Stock-based compensation	—	—	—	—	—	—	945	—		945
Net loss	—	—	—	—	—		—	—	(8,621)	(8,621)
Balance at December 31, 2014	68,027	63,166	—	—	9,042	1	1,546	—	(53,014)	(51,467)
Exercise of stock options	—	—	2	—	315	—	357	—	—	357
Stock-based compensation	—	—	—	—	—	—	1,103	—	—	1,103
Conversion of convertible preferred stock in connection with initial public offering	(68,027)	(63,166)	—	—	17,007	2	63,164	—	—	63,166
Issuance of common stock in connection with initial public offering, net of offering costs	—	—	7,130	1	—	—	75,358	—	—	75,359
Conversion of Class B stock to Class A stock	—	—	1,848	—	(1,848)	—	—	—	—	—
Issuance of restricted stock awards	—	—	25	—	25	—	—	—	—	—
Other comprehensive loss	—	—	—	—	—	—	—	(153)	—	(153)
Net loss	—	—	—	—	—	—	—	—	(15,668)	(15,668)
Balance at December 31, 2015	—	—	9,005	1	24,541	3	141,528	(153)	(68,682)	72,697
Exercise of stock options	—	—	140	—	1		352	—	—	352
Stock-based compensation	—	—	—	—	—	—	4,495	—	—	4,495
Vesting of restricted stock units, net of			10	—	—	—	127	—	—	127

shares withheld for taxes										
Vesting of early exercised shares	—	—	—	—	—	—	190	—	—	190
Conversion of Class B stock to Class A stock	—	—	2,514	—	(2,514)	—	—	—	—	—
Issuance of restricted stock awards	—	—	22	—	—	—	—	—	—	—
Other comprehensive income	—	—	—	—	—	—	—	102	—	102
Net loss	—	—	—	—	—	—	—	—	(8,281)	(8,281)
Balance at December 31, 2016	—	—	11,691	$ 1	22,028	$ 3	$146,692	$ (51)	$(76,963)	$69,682

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

APPFOLIO, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended December 31,		
	2016	2015	2014
Cash from operating activities			
Net loss	$(8,281)	$(15,668)	$(8,621)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	9,935	6,104	3,805
Purchased investment premium, net of amortization	245	(865)	—
Amortization of deferred financing costs	63	456	—
Loss on disposal of property, equipment and intangibles	41	67	116
Stock-based compensation	4,301	1,007	892
Lease abandonment	161	—	—
Change in fair value of contingent consideration	—	—	26
Loss on equity-method investment	—	—	19
Changes in operating assets and liabilities:			
Accounts receivable	(463)	(746)	(401)
Prepaid expenses and other current assets	(377)	(1,893)	(549)
Other assets	(103)	(56)	(5)
Accounts payable	(904)	(439)	1,831
Accrued employee expenses	2,223	1,887	1,088
Accrued expenses	1,148	1,135	1,011
Deferred revenue	2,685	1,173	837
Other liabilities	826	994	426
Net cash provided by (used in) operating activities	11,500	(6,844)	475
Cash from investing activities			
Purchases of property and equipment	(4,242)	(3,694)	(1,878)
Additions to capitalized software	(11,166)	(7,677)	(4,567)
Purchases of investment securities	(31,551)	(74,176)	—
Sales of investment securities	12,559	4,100	—
Maturities of investment securities	21,337	26,136	—
Cash paid in business acquisition, net of cash acquired	—	(4,039)	—
Purchases of intangible assets	(2)	(17)	(31)
Net cash used in investing activities	(13,065)	(59,367)	(6,476)
Cash from financing activities			
Proceeds from stock option exercises	352	357	168
Proceeds from issuance of restricted stock	—	141	—
Proceeds from issuance of options	—	208	—
Tax withholding for net share settlement	(111)	—	—
Principal payments under capital lease obligations	(29)	(27)	(24)
Proceeds from initial public offering, net of underwriting discounts and commissions	—	79,570	—
Payments of initial public offering costs	—	(4,213)	—
Payment of contingent consideration	—	(2,429)	—
Proceeds from issuance of debt	117	10,253	—
Principal payments on debt	(128)	(10,241)	—
Payment of debt issuance costs	—	(757)	—
Net cash provided by financing activities	201	72,862	144

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APPFOLIO, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended December 31,		
	2016	2015	2014
Net (decrease) increase in cash and cash equivalents	(1,364)	6,651	(5,857)
Cash and cash equivalents			
Beginning of period	12,063	5,412	11,269
End of period	$10,699	$12,063	$5,412
Supplemental disclosure of cash flow information			
Cash paid for interest	$191	$797	$—
Cash paid for taxes	27	91	—
Noncash investing and financing activities			
Purchases of property and equipment included in accounts payable and accrued expenses	$261	$1,220	$46
Additions of capitalized software included in accrued employee expenses	458	290	—
Stock-based compensation capitalized for software development	431	166	53
Conversion of convertible preferred stock into common stock in connection with initial public offering	—	63,166	—

The accompanying notes to the Consolidated Financial Statements are an integral part of these statements.

APPFOLIO, INC.
NOTES TO CONSOLIDATED AUDITED FINANCIAL STATEMENTS
1. Nature of Business

AppFolio, Inc. (“we” or “AppFolio”) provides industry-specific, cloud-based software solutions for small and medium-sized businesses (“SMBs”) in the property management and legal industries. Our platform is designed to be the system of record to automate essential business processes and the system of engagement to enhance business interactions between our customers and their clients and vendors. Our mobile-optimized software solutions have a user-friendly interface across multiple devices, enabling our customers to work at any time and from anywhere. Our property management software provides small and medium-sized property managers with an end-to-end solution to their business needs, enabling them to manage properties quickly and easily in a single, integrated environment. Our legal software provides solo practitioners and small law firms with a streamlined practice and case management solution, allowing them to manage their practices and case load within a flexible system. We also offer optional, but often mission-critical, Value+ services, such as our professionally designed websites, and electronic payment services which are seamlessly built into our core solutions.
2. Summary of Significant Accounting Policies
Basis of Presentation and Significant Accounting Policies
The accompanying Consolidated Financial Statements were prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”).
Principles of Consolidation
The accompanying Consolidated Financial Statements include the operations of AppFolio, Inc. and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.
Our investment in SecureDocs, Inc. (“SecureDocs”) is accounted for under the equity method of accounting as we have the ability to exert significant influence, but do not control and are not the primary beneficiary of the entity. Our investment in SecureDocs and our share of its losses are not material individually or in the aggregate to our financial position, results of operations or cash flows for any period presented.
Reclassifications
We reclassified certain amounts in our Consolidated Statements of Cash Flows within the cash from investing activities section in the prior year to conform to the current year's presentation.
Use of Estimates
The preparation of financial statements is in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates. On an ongoing basis, management evaluates its estimates based on historical data and experience, as well as various other factors that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources.
Segment Information
Our chief operating decision maker reviews financial information presented on an aggregated and consolidated basis, together with revenue information for our core solutions, Value+ and other service offerings, principally to make decisions about how to allocate resources and to measure our performance. Accordingly, management has determined that we have one reportable and operating segment.
Concentrations of Credit Risk
Financial instruments that potentially subject us to credit risk consist principally of cash, accounts receivable, investment securities and notes receivable. At times, we maintain cash balances at financial institutions in excess of amounts insured by United States government agencies or payable by the United States government directly. We place our cash with high credit, quality financial institutions. We invest in investment securities with a minimum rating of A by Standard & Poor's and A-1 by Moody's and regularly monitor our investment security portfolio for changes in credit ratings.

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Concentrations of credit risk with respect to accounts receivable and revenue are limited due to a large, diverse customer base. No individual customer represented 10% or more of accounts receivable as of December 31, 2016 and 2015 or revenue for the years ended December 31, 2016, 2015 and 2014.

Fair Value Measurements

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. Accounting Standard Codification (“ASC”) 820, Fair Value Measurements and Disclosures (“ASC 820”), describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value, which are the following:

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

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

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

Cash and Cash Equivalents and Restricted Cash

We consider all highly liquid investments, readily convertible to cash, and which have a remaining maturity date of three months or less at the date of purchase, to be cash equivalents. Cash and cash equivalents are recorded at fair value and consist primarily of bank deposits and money market funds.

Restricted cash of $0.4 million as of December 31, 2016 and 2015, is comprised of certificates of deposits relating to collateral requirements for customer automated clearing house (“ACH”) and credit card chargebacks and minimum collateral requirements for our insurance services, which are recorded in other long term assets.

Investment Securities

Our investment securities currently consist of corporate bonds, U.S. government agency securities (referred to as "Agency Securities") and certificates of deposit. We classify investment securities as available-for-sale at the time of purchase and reevaluate such classification as of each balance sheet date. All investments are recorded at estimated fair value. Unrealized gains and losses for available-for-sale securities are included in accumulated other comprehensive income (loss), a component of stockholders’ equity. We classify our investments as current when the period of time between the reporting date and the contractual maturity is twelve months or less and as noncurrent when the period of time between the reporting date and the contractual maturity is more than twelve months.

We evaluate our investments to assess whether those with unrealized loss positions are other than temporarily impaired. We consider impairments to be other than temporary if they are related to deterioration in credit risk or if it is likely we will sell the securities before the recovery of their cost basis. Declines in value judged to be other than temporary are determined based on the specific identification method and are reported in other income (expense), net in the Consolidated Statements of Operations.

Accounts Receivable

Accounts receivable are recorded at the invoiced amount, net of allowance for doubtful accounts. The allowance for doubtful accounts is based on historical loss experience, the number of days that receivables are past due, and an evaluation of the potential risk of loss associated with delinquent accounts. Accounts receivable considered uncollectable are charged against the allowance for doubtful accounts when identified. We do not have any off-balance sheet credit exposure related to our customers. As of December 31, 2016, 2015 and 2014, our allowance for doubtful accounts was not material.

Property and Equipment

Property and equipment is stated at cost, less accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of assets. The estimated useful lives of our property and equipment are as follows:

Asset Type	Depreciation Period
Data center and computer equipment	3 years
Furniture and fixtures	7 years
Office equipment	2 to 5 years
Leasehold improvements	Shorter of remaining life of lease or asset life

Repair and maintenance costs are expensed as incurred. Renewals and improvements are capitalized. Assets disposed of or retired are removed from the cost and accumulated depreciation accounts and any resulting gain or loss is reflected in our results of operations.

Leases

Leases are evaluated and classified as either operating or capital leases. All of our office space leases are operating leases.

Rent expense under operating leases is recognized on a straight-line basis over the lease term. The difference between recognized rent expense and the rent payment amount is recorded as an increase or decrease in deferred rent liability. If the lease has tenant allowances from the lessor for certain improvements made to the leased property, these allowances are capitalized as leasehold improvements. Tenant allowances and rent holidays in lease agreements are recognized as a deferred rent credit, which is amortized on a straight-line basis over the lease term as a reduction of rent expense.

Internal-Use Software

We account for the costs of computer software obtained or developed for internal use in accordance with ASC 350, Intangibles-Goodwill and Other (“ASC 350”). These include costs incurred in connection with the development of our internal-use software solutions when (i) the preliminary project stage is completed, (ii) management has authorized further funding for the completion of the project and (iii) it is probable that the project will be completed and performed as intended. These capitalized costs include personnel and related expenses for employees who are directly associated with and who devote time to internal-use software projects and, when material, interest costs incurred during the development. Capitalization of these costs ceases once the project is substantially complete and the software is ready for its intended purpose. Costs incurred for significant upgrades and enhancements to our software solutions are also capitalized. Costs incurred for post-configuration training, maintenance and minor modifications or enhancements are expensed as incurred. Capitalized software development costs are amortized using the straight-line method over an estimated useful life of three years. We do not transfer ownership of our software, or lease our software, to third parties.

Intangible Assets

Intangible assets primarily consist of customer and partner relationships, acquired technology, trademarks, domain names and patents, which are recorded at cost, less accumulated amortization. We determine the appropriate useful life of our intangible assets by performing an analysis of expected cash flows of the acquired assets. Intangible assets are amortized over their estimated useful lives using the straight-line method, which approximates the pattern in which the economic benefits are consumed.

Impairment of Long-Lived Assets

We assess the recoverability of our long-lived assets when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Such events or changes in circumstances may include a significant adverse change in the extent or manner in which a long-lived asset is being used, a significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset, an accumulation of costs significantly in excess of the amount originally expected for the acquisition or development of a long-lived asset, current or future operating or cash flow losses that demonstrate continuing losses associated with the use of a long-lived asset, or a current expectation that, more likely than not, a long-lived asset will be sold or otherwise

disposed of significantly before the end of its previously estimated useful life. Impairment testing is performed at an asset level that represents the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. We assess recoverability of long-lived assets by determining whether the carrying value of an asset can be recovered through projected undiscounted cash flows over its remaining life. If the carrying value of an asset exceeds the forecasted undiscounted cash flows, an impairment loss is recognized, measured as the amount by which the carrying value exceeds estimated fair value. An impairment loss is charged to operations in the period in which management determines such

impairment. There were no impairment charges related to the identified long-lived assets for the years ended December 31, 2016, 2015 and 2014.

Business Combinations

The results of a business acquired in a business combination are included in our consolidated financial statements from the date of acquisition. We allocate the purchase price, including the fair value of contingent consideration, to the identifiable assets and liabilities of the acquired business at their acquisition date fair values. The excess of the purchase price over the amount allocated to the identifiable assets and liabilities, if any, is recorded as goodwill. Determining the fair value of assets acquired and liabilities assumed requires management to make significant judgments and estimates, including the selection of valuation methodologies, estimates of future revenue and cash flows, discount rates and selection of comparable companies.

Acquisition-related transaction costs are not included as a component of consideration transferred, but are accounted for as an operating expense in the period in which the costs are incurred.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination. We test goodwill for impairment in accordance with the provisions of ASC 350. Goodwill is tested for impairment at least annually at the reporting unit level or whenever events or changes in circumstances indicate that goodwill might be impaired. Events or changes in circumstances which could trigger an impairment review include a significant adverse change in legal factors or in the business climate, unanticipated competition, loss of key personnel, significant changes in the use of the acquired assets or our strategy, significant negative industry or economic trends, or significant underperformance relative to expected historical or projected future results of operations.

ASC 350 provides that an entity has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then additional impairment testing is not required. However, if an entity concludes otherwise, then it is required to perform the first of a two-step impairment test.

The first step involves comparing the estimated fair value of a reporting unit with its book value, including goodwill. If the estimated fair value exceeds book value, goodwill is considered not to be impaired and no additional steps are necessary. If, however, the fair value of the reporting unit is less than book value, then the carrying amount of the goodwill is compared with its implied fair value. The estimate of implied fair value of goodwill may require valuations of certain internally generated and unrecognized intangible assets. If the carrying amount of goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to the excess. We have one reporting unit and we test for goodwill impairment annually during the fourth quarter of the calendar year. At December 31, 2016 and 2015, we determined our goodwill of $6.7 million was not impaired as the fair value of our reporting unit significantly exceeded its carrying value based on the results of our annual impairment tests.

Revenue Recognition

We primarily generate revenue from our customers for subscriptions to access to our core solutions and Value+ services for our cloud-based property management and legal software solutions. Subscription fees for our core solutions are charged on a per-unit per-month basis for our property management software solution and on a per-user per-month basis for our legal software solution. We recognize subscription revenue on a straight-line basis over the terms of the subscription agreements, which range from one month to one year. We generally invoice our customers for subscription services in monthly, quarterly or annual installments, typically in advance of the subscription period. Any revenues which are billed in advance are recorded as deferred revenue.

We charge our customers on a subscription basis for our core solutions and many of our Value+ services. Our subscription fees are designed to scale to the size of our customers' businesses. We also charge our customers usage-based fees for using certain Value+ services, including electronic payment processing. Usage-based fees are charged on a flat fee per transaction basis with no minimum usage commitments. We recognize revenue for usage-based services in the period the service is rendered. We generally invoice our customers for usage-based

services on a monthly basis for services rendered in the preceding month with the exception of fees for electronic payment processing, which are generally paid by the clients of our customers at the time the electronic payment is processed.

Our legal software core solution offers their customers a free-trial period to try our software. Revenue is not recognized until the free-trial period is complete and the customer has entered into a subscription agreement with us. Our customers do not have rights to the underlying software code of our solutions, and accordingly, the Company's revenue arrangements are outside the scope of the software revenue recognition guidance, and recognized in accordance with Staff Accounting Bulletin ("SAB") Topic 13. We recognize revenue when (i) there is persuasive evidence of an arrangement, (ii) our software solutions have been made available or delivered, or services have been performed, (iii) the amount of fees is fixed or determinable, and (iv) collectability is reasonably assured. Evidence of an arrangement generally consists of either a signed customer contract or an online click-through agreement. We consider that delivery of a solution or website has commenced once we provide the customer with access to use the solution or website. Fees are fixed based on rates specified in the subscription agreements, which do not provide for any refunds or adjustments. If collectability is not considered reasonably assured, revenue is deferred until the fees are collected. Some of our subscription agreements contain minimum cancellation fees in the event that the customer cancels the subscription early.

For multiple-deliverable arrangements, we first assess whether each deliverable has value to the customer on a standalone basis. We have determined that the subscription services related to our core solutions have value on a standalone basis because, once access is provided, they are fully functional and do not require additional development, modification or customization. Our Value+ services have value on a standalone basis as the services are sold separately by other vendors and are not essential to the functionality of the other deliverables. Usage-based services have value to the customer on a standalone basis as they are sold separately by other vendors and are not essential to the functionality of the other deliverables. The usage-based services are typically entered into subsequent to the initial customer arrangement. In multiple-deliverable arrangements that contain usage-based services, the customer has the option to purchase the services on an ad hoc basis, and payments are made when the services are rendered.

Based on the standalone value of the deliverables, and since our customers do not have a general right of return, we allocate revenue among the separate non-contingent deliverables in a multiple-deliverable arrangement under the relative selling price method using the selling price hierarchy within the revenue accounting guidance (ASU 2009-13, Revenue Recognition, Topic 605). The selling price hierarchy requires the selling price of each deliverable in a multiple-deliverable arrangement to be based on, in descending order, (i) vendor-specific objective evidence of fair value, or VSOE, (ii) third-party evidence of fair value, or TPE, or (iii) management’s best estimate of the selling price, or BESP.

For our property manager core solution, we have established VSOE based on our consistent historical pricing and discounting practices for customer renewals where the customer only subscribes to our core solutions, and based on the price established by management for elements not yet being sold separately. In establishing VSOE, the substantial majority of the selling prices for our core solutions fall within a reasonably narrow pricing range, and the price once established by management for elements not yet being sold separately are not offered at a discount. For our legal software core solution, we utilize BESP to allocate revenue among the separate non-contingent deliverables, as we have been unable to establish VSOE due to our discounting practices, and we have been unable to obtain TPE.

After the contract value is allocated to each non-contingent deliverable in a multiple-deliverable arrangement based on the relative selling price, revenue is recognized for each deliverable based on the pattern in which the revenue is earned. For subscriptions services, revenue is recognized on a straight-line basis over the subscription period. For usage-based services, revenue is recognized as the services are rendered. For one-time services, revenue is recognized upon completion of the related services. Sales commissions and other incremental costs to acquire contracts are expensed as incurred.

Cost of Revenue

Cost of revenue consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on customer service and the support of our operations, platform infrastructure costs (such as data center operations and hosting-related costs), fees paid to third-party service providers, payment processing fees, and allocated shared costs. We typically allocate shared costs across our organization based on headcount within the applicable part of our organization. Cost of revenue excludes depreciation of property and equipment, and amortization of capitalized software development costs and intangible assets.

Sales and Marketing

Sales and marketing expense consists of personnel-related costs (including salaries, sales commissions, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on sales and marketing, costs associated with sales and marketing activities, and allocated shared costs. Marketing activities include advertising, online lead generation, lead nurturing, customer and industry events, industry-related content creation and collateral creation. Sales commissions and other incremental costs to acquire customers and grow adoption and utilization of our Value+ services by new and existing customers are expensed as incurred. We focus our sales and marketing efforts on generating awareness of our software solutions, creating sales leads, establishing and promoting our brands, and cultivating an educated community of successful and vocal customers.

Advertising expenses were $3.6 million, $3.6 million and $2.1 million for the years ended December 31, 2016, 2015 and 2014, respectively, and are expensed as incurred.

Research and Product Development

Research and product development expense consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for our employees focused on research and product development, fees for third-party development resources, and allocated shared costs. Our research and product development efforts are focused on enhancing the ease of use and functionality of our existing software solutions by adding new core functionality, Value+ services and other improvements, as well as developing new products. We capitalize the portion of our software development costs that meets the criteria for capitalization. Amortization of software development costs is included in depreciation and amortization expense.

General and Administrative

General and administrative expense consists of personnel-related costs (including salaries, incentive-based compensation, benefits, and stock-based compensation) for employees in our executive, finance, information technology, or IT, human resources, legal and administrative organizations. In addition, general and administrative expense includes fees for third-party professional services (including consulting, legal and audit services), other corporate expenses, and allocated shared costs.

Depreciation and Amortization

Depreciation and amortization expense includes depreciation of property and equipment, amortization of capitalized software development costs and amortization of intangible assets. We depreciate or amortize property and equipment, software development costs and intangible assets over their expected useful lives on a straight-line basis, which approximates the pattern in which the economic benefits of the assets are consumed.

Stock-Based Compensation

We account for stock-based compensation awards granted to employees and directors by recording compensation expense based on the awards' grant-date estimated fair value, in accordance with ASC 718, Compensation-Stock Compensation ("ASC 718") over the vesting period. We estimate the fair value of restricted stock awards ("RSA"), restricted stock units ("RSU") and performance based RSUs ("PSU") based on the fair value of our common stock on the date of grant. We estimate the fair value of stock options and performance based stock options ("PSO") using the Black-Scholes option-pricing model. Determining the fair value of stock options under this model requires highly subjective assumptions, including the fair value of the underlying common stock, the risk-free interest rate, the expected term of the award, the expected volatility of the price of our common stock, and the expected dividend yield of our common stock. These estimates involve inherent uncertainties and the application of management's judgment. If we had made different assumptions, our stock-based compensation expense could have been materially different.

Prior to our IPO, there was no public market for our common stock and our board of directors determined the fair value of our common stock at the time of the grant of stock options and restricted stock awards by considering a number of objective and subjective factors, including our actual operating and financial performance, market conditions and performance of comparable publicly traded companies, developments and milestones in our company, the likelihood of achieving a liquidity event and transactions involving our convertible preferred stock, among other factors. The fair value of the underlying common stock was determined by our board of directors in accordance with applicable elements of the practice aid issued by the American Institute of Certified Public Accountants Valuation of Privately Held Company Equity Securities Issued as Compensation. In valuing our common stock at various dates, our board of directors determined our equity value generally using the income approach and the market comparable approach valuation methods. Once we determined our equity value, we used an option pricing method or the Probability Weighted Expected Return Method to allocate the equity value to preferred stock and common stock. Application of these approaches and methods involves the use of estimates, judgments and assumptions, such as future revenue, expenses and cash flows, selections of comparable companies, probabilities and timing of exit events, and other factors.

Since our IPO in June 2015, the fair value of our common stock is based on the closing price of our common stock, as quoted on the NASDAQ Global Market, on the date of grant and we utilized the following assumptions and estimates when utilizing the Black-Sholes option-pricing model when calculating the fair value of our options and PSOs:

Risk-Free Interest Rate - The risk free interest rate assumption is based upon observed interest rates on United States government securities appropriate for the expected term of the stock option.

Expected Term - Given we do not have sufficient exercise history to develop reasonable expectations about future exercise patterns and post-vesting employment termination behavior, we determine the expected term using the

simplified method, which is calculated as the midpoint of the stock option vesting term and the expiration date of the stock option.

Expected Volatility - We determine the expected volatility based on the historical average volatilities of publicly traded industry peers. We intend to continue to consistently apply this methodology using the same or similar public companies until a sufficient amount of historical information regarding the volatility of our own common stock price becomes available, unless circumstances change such that the identified companies are no longer similar to us, in which case, more suitable companies whose stock prices are publicly available would be utilized in the calculation.

Expected Dividend Yield - We have not paid and do not anticipate paying any cash dividends in the foreseeable future and, therefore, we use an expected dividend yield of zero.

Forfeiture Rate

In addition to the assumptions used in the Black-Scholes option-pricing model, we also estimate a forfeiture rate to calculate our stock-based compensation expense for our options and awards. The forfeiture rate is based on an analysis of actual forfeitures. We will continue to evaluate the appropriateness of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover, and other factors. Changes in the estimated forfeiture rate can have a significant impact on our stock-based compensation expense as the cumulative effect of adjusting the rate is recognized in the period the estimated forfeiture rate is changed. If a revised forfeiture rate is higher than the previously estimated forfeiture rate, an adjustment is made that will result in a decrease to our stock-based compensation expense recognized in our consolidated financial statements. If a revised forfeiture rate is lower than the previously estimated forfeiture rate, an adjustment is made that will result in an increase to our stock-based compensation expense recognized in our consolidated financial statements.

Restricted Stock Units

In September 2015, we began granting restricted stock units ("RSUs"). The vesting of RSUs is in equal tranches over four annual periods. The RSUs are expensed on a straight-line basis over the vesting period. The shares underlying the RSU grants are not issued and outstanding until the applicable vesting date.

Performance Based Equity Awards

In 2016, we began granting PSOs and PSUs. The fair value of the PSOs are estimated using the Black-Scholes option-pricing model and the PSUs fair value is based on the fair value of our common stock on the date of grant. The vesting of the PSOs and PSUs is based on achievement of a pre-established free cash flow performance metric and continued employment throughout the performance period. We recognize expense for the PSOs and PSUs based on the grant date fair value to the extent vesting of the award is probable. Adjustments to compensation expense are made each period based on changes in our estimate of the number of PSOs and PSUs that are probable of vesting. PSOs and PSUs will vest upon achievement of the performance metric once such calculation is reviewed and approved by the Board of Directors.

Income Taxes

We account for income taxes in accordance with ASC 740, Income Taxes (“ASC 740”). ASC 740 requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the consolidated statements of operations in the period that includes the enactment date. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets will not be realized.

We 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 our consolidated financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized. We recognize interest and penalties accrued with respect to uncertain tax positions, if any, in our provision for income taxes in the consolidated statements of operations.

Net Loss per Share

The following table presents a reconciliation of our weighted average number of Class A and Class B common shares used to compute net loss per share (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Weighted average shares outstanding	33,639	21,486	8,998
Less: Weighted average unvested restricted shares subject to repurchase	78	150	241
Weighted average number of shares used to compute basic and diluted net loss per share	33,561	21,336	8,757

Because we reported net losses for all periods presented, all potentially dilutive common stock equivalents are antidilutive for those periods and have been excluded from the calculation of net loss per share. The diluted net loss per a common share were the same for Class A and Class B common shares because they are entitled to the same liquidation and dividend rights.

The following table presents the number of anti-dilutive shares excluded from the calculation of diluted net loss per share as of December 31, 2016 and 2015 (in thousands):

	December 31,	
	2016	2015
Options to purchase common stock	1,718	1,171
Unvested restricted stock awards	46	120
Unvested restricted stock units	496	17
Contingent restricted stock units (1)	34	49
Total shares excluded from net loss per share attributable to common stockholders	2,294	1,357

(1) The reported shares are based on a fixed price RSU commitment for which the number of shares has not been determined at the grant date and performance based RSUs which have met the performance metric but, have not be issued. The RSUs disclosed with a fixed price in the table above are based on the closing price of our stock at December 31, 2016 divided by the future fixed price commitment to issue shares in the future. For additional information regarding the RSUs granted refer to Note 11, Stock-Based Compensation.

Recent Accounting Pronouncements

Under the Jumpstart our Business Startups Act (the “JOBS Act”), we meet the definition of an emerging growth company. We have irrevocably elected to opt out of the extended transition period for complying with new or revised accounting standards pursuant to Section 107(b) of the JOBS Act.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606) (“ASU 2014-09”), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. Subsequently, the FASB has issued the following standards related to ASU 2014-09: ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (“ASU 2016-08”); ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing (“ASU 2016-10”); ASU No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients (“ASU 2016-12”); and ASU No. 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers (“ASU 2016-20”). The Company must adopt ASU 2016-08, ASU 2016-10, ASU 2016-12 and ASU 2016-20 with ASU 2014-09 (collectively, the “new revenue standards”). The new revenue standards will be effective for the Company on January 1, 2018. Early adoption is permitted as of January 1, 2017. The Company expects to adopt ASU 2014-09 on January 1, 2018. The standard permits the use of either a retrospective or cumulative effect transition method. We have not yet selected a transition method and we are currently evaluating the effect that the new revenue standards will have on our consolidated financial statements and related disclosures. Based on our preliminary assessments, we do not expect there will be a material impact to our revenues upon adoption. We are continuing to evaluate the impact to our revenues related to our pending adoption of Topic 606 and our preliminary assessments are subject to change. While we are continuing to

assess all potential impacts of the standard, we currently believe the most significant impact relates to recognition of costs related to obtaining customer contracts. Under current GAAP, sales commissions and other incremental costs to acquire contracts are expensed as incurred. Under the new revenue standards, such costs will be deferred and

recognized over a period of time. We are still evaluating the new revenue standards and assessing the impact this identified difference in accounting treatment may have on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) ("ASU 2016-02"). Under ASU 2016-02, an entity will be required to recognize right-of-use assets and lease liabilities on its balance sheet and disclose key information about leasing arrangements. ASU 2016-02 offers specific accounting guidance for a lessee, a lessor and sale and leaseback transactions. Lessees and lessors are required to disclose qualitative and quantitative information about leasing arrangements to enable a user of the financial statements to assess the amount, timing and uncertainty of cash flows arising from leases. For public companies, ASU 2016-02 is effective for annual reporting periods beginning after December 15, 2018, including interim periods within that reporting period, and requires a modified retrospective adoption, with early adoption permitted. We anticipate this standard will have a material impact on our consolidated financial statements. While we are continuing to assess all potential impacts of the standard, we currently believe the most significant impact relates to our accounting and reporting of our operating leases on our balance sheet.

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 781), Improvements to Employee Share-Based Payment Accounting ("ASU 2016-09"), which amends and simplifies the accounting for share-based payment awards in three areas; (1) income tax consequences, (2) classification of awards as either equity or liabilities, and (3) classification on the statement of cash flows. ASU 2016-19 also provides an accounting policy election to account for forfeitures as they occur. For public companies, ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. We do not expect the adoption of ASU 2016-09 on January 1, 2017, to have a material impact on our consolidated financial statements due to the full valuation allowance on our deferred tax assets. We have elected to continue to estimate forfeitures expected to occur to determine the amount of compensation cost to be recognized each period.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"), which amends the current accounting guidance and requires the measurement of all expected losses based on historical experience, current conditions and reasonable and supportable forecasts. This guidance amends the accounting for credit losses for available-for-sale securities and purchased financial assets with credit deterioration. ASU 2016-13 is effective for annual periods beginning after December 15, 2019, and interim periods within those annual periods. Early adoption is permitted for any interim or annual period after December 15, 2018. We do not expect the adoption of this guidance to have a material impact on our financial condition, results of operations, cash flows or disclosures.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments ("ASU 2016-15"), which provides cash flow statement classification guidance for debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. We have not yet determined the effect of this guidance on our statement of cash flows.

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory (ASU 2016-16), which changes the timing of when certain intercompany transactions are recognized within the provision for income taxes. ASU 2016-16 is effective on January 1, 2018. Early adoption is permitted. We have not yet determined the effect of this guidance on our financial condition, results of operations, cash flows or disclosures.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (ASU 2016-18), which provides amendments to current guidance to address the classification and presentation of changes in restricted cash in the statement of cash flows. ASU 2014-09 is effective on January 1, 2018 and early adoption is

permitted. We are still evaluating the effect of this guidance on our financial statements, although we expect that adoption will change the current presentation of restricted cash on our statement of cash flows as well as require additional disclosures to reconcile cash and cash equivalents per the balance sheet to cash and cash equivalents on the statement of cash flows.

3. Acquisition of RentLinx

On April 1, 2015, we completed the acquisition of all of the membership interests of RentLinx, LLC ("RentLinx"), a San Diego, California-based company focused on developing a software platform that allows customers to advertise rental houses and apartments online. We acquired RentLinx to expand the Value+ services offered to our property manager customers, giving them the ability to better spend, track and optimize their marketing investments.

We paid the sellers $4.1 million, of which $0.5 million was placed into escrow to cover potential indemnification claims relating to breaches of representations, warranties and covenants. We also agreed to pay an additional amount of approximately $1.1 million to certain individuals subject to their continued employment with us, which was recorded as an expense over the service period and was paid in October 2015. All transaction costs were expensed in the period incurred and were approximately $0.3 million.

The goodwill related to our RentLinx acquisition is attributable to synergies expected from the acquisition and assembled workforce. The goodwill is deductible for income tax purposes.

The following table summarizes the purchase price allocation (in thousands):

	Amount	Estimated Useful Life
Net current assets	$ 114	
Intangible assets:		
Developed technology	810	6 years
Partner relationships	680	3 years
Customer and website relationships	560	5 years
Other intangible assets	170	3 years
Goodwill	1,739	Indefinite
Purchase consideration, paid in cash	$ 4,073	

As of the date of acquisition, we did not provide pro forma or current period financial information as it was not material to our Consolidated Financial Statements.

4. Investment Securities and Fair Value Measurements

Investment Securities

Investment securities classified as available-for-sale consisted of the following at December 31, 2016 and 2015 (in thousands):

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	$30,492	$ 9	$ (56)	$ 30,445
Agency securities	6,248	—	(20)	6,228
Certificates of deposit	$5,472	$ 16	$ —	5,488
Total available-for-sale investment securities	$42,212	$ 25	$ (76)	$ 42,161

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate bonds	$30,568	$ —	$ (126)	$ 30,442
Agency securities	8,012	—	(12)	8,000
Certificates of deposit	6,225	—	(15)	6,210
Total available-for-sale investment securities	$44,805	$ —	$ (153)	$ 44,652

We had certain investment securities in an unrealized loss position at December 31, 2016 and 2015, and none of these securities have been in a continuous unrealized loss position for more than 12 months. These unrealized loss positions are considered temporary and there were no impairments considered "other-than-temporary" as it is more likely than not we will hold the securities until maturity or a recovery of the cost basis.

At December 31, 2016 and 2015, the contractual maturities of our investments did not exceed 36 months. The fair values of available-for-sale investments, by remaining contractual maturity, are as follows (in thousands):

	December 31, 2016		December 31, 2015	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in 1 year or less	$15,475	$ 15,473	$10,249	$ 10,235
Due after 1 year through 3 years	26,737	26,688	34,557	34,417
Total available-for-sale investment securities	$42,212	$ 42,161	$44,806	$ 44,652

During the years ended December 31, 2016 and 2015, we had sales and maturities (which include calls) of investment securities, as follows (in thousands):

	Year Ended December 31, 2016			
	Gross Realized Gains	Gross Realized Losses	Gross Proceeds from Sales	Gross Proceeds from Maturities
Agency securities	$5	—	$3,005	11,557
Corporate bonds	7	—	7,554	2,480
Treasury bills	—	—	2,000	6,055
Certificates of deposit	—	—	—	1,245
	$12	$—	$12,559	$21,337

	Year Ended December 31, 2015			
	Gross Realized Gains	Gross Realized Losses	Gross Proceeds from Sales	Gross Proceeds from Maturities
Agency securities	$—	(2)	$1,500	7,500
Corporate bonds	21	—	2,600	18,636
	$21	$(2)	$4,100	$26,136

For the years ended December 31, 2016 and 2015, we received interest income net of the amortization and accretion of the premium and discount of $0.5 million and $0.2 million, respectively. We did not have investment securities during the year ended December 31, 2014.

Fair Value Measurements

Recurring Fair Value Measurements

Financial assets and financial liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The following tables summarize our financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2016 and 2015, by level within the fair value hierarchy (in thousands):

	December 31, 2016			
	Level 1	Level 2	Level 3	Total Fair Value
Cash equivalents:				
Money market funds	$4,849	$—	$—	$4,849
Available-for-sale investment securities:				
Corporate bonds	—	30,445	—	30,445
Agency securities	—	6,228	—	6,228
Certificates of deposit	5,488	—	—	5,488
Total Assets	$10,337	$36,673	$—	$47,010

	December 31, 2015			
	Level 1	Level 2	Level 3	Total Fair Value
Cash equivalents:				
Money market funds	$7,102	$—	$—	$7,102
Available-for-sale investment securities:				
Corporate bonds	—	30,442	—	30,442
Agency securities	—	8,000	—	8,000
Certificates of deposit	6,210	—	—	6,210
Total Assets	$13,312	$38,442	$—	$51,754

The carrying amounts of cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the short maturity of these items.

There were no changes to our valuation techniques used to measure asset and liability fair values on a recurring basis during the year ended December 31, 2016. The valuation techniques for the items in the table above are as follows:

Cash Equivalents

As of December 31, 2016 and 2015, cash equivalents include cash invested in money market funds. Market prices are based on market prices for identical assets.

Available-for-Sale - Investment Securities

The fair value of our investment securities is based on pricing determined using inputs other than quoted prices that are observable either directly or indirectly such as yield curve, volatility factors, credit spreads, default rates, loss severity, current market and contractual prices for the underlying instruments or debt, broker and dealer quotes, as well as other relevant economic measures.

Contingent Consideration

Contingent consideration payable in connection with acquisitions is measured at fair value each period and is based on significant inputs not observable in the market, which represents a Level 3 measurement within the fair value hierarchy. The valuation of contingent consideration uses assumptions we believe would be made by a market participant. We assessed these estimates on an on-going basis as additional data impacting the assumptions became available. Changes in the fair value of contingent consideration related to updated assumptions and estimates were recognized within general and administrative expense in the Consolidated Statements of Operations. We determined the fair value of the contingent consideration using the probability weighted discounted cash flow method. The significant inputs used in the fair value measurement of contingent consideration were the probability of achieving revenue thresholds and determining discount rates.

The following table summarizes the changes in contingent consideration liability (in thousands):

	Year Ended December 31,	
	2015	2014
Fair value, at beginning of period	$2,429	$2,403
Change in fair value recorded in general and administrative expenses	—	26
Payment of contingent consideration	(2,429)	—
Fair value, at end of period	$—	$2,429

Non-Recurring Fair Value Measurements

Certain assets, including goodwill, intangible assets and our note receivable with SecureDocs are also subject to measurement at fair value on a non-recurring basis using Level 3 measurement when they are deemed to be impaired as a result of an impairment review. For the years ended December 31, 2016 and 2015, no impairments were identified on those assets required to be measured at fair value on a non-recurring basis.

5. Property and Equipment

Property and equipment consists of the following as of December 31, 2016 and 2015 (in thousands):

	December 31,	
	2016	2015
Data center and computer equipment	$4,913	$3,923
Furniture and fixtures	2,465	1,723
Office equipment	726	434
Leasehold improvements	4,035	878
Construction in process	—	2,315
Gross property and equipment	12,139	9,273
Less: Accumulated depreciation	(5,062)	(3,166)
Total property and equipment, net	$7,077	$6,107

Depreciation expense for property and equipment totaled $2.3 million, $1.4 million, and $0.9 million for the years ended December 31, 2016, 2015 and 2014, respectively.

As of December 31, 2016, there was no property and equipment under capital lease. As of December 31, 2015, capital leases were included in property and equipment with a cost basis of $82,000. Accumulated depreciation on property and equipment under capital leases as of December 31, 2015 was $57,000.

6. Internal-Use Software Development Costs

Internal-use software development costs were as follows (in thousands):

	December 31,	
	2016	2015
Internal use software development costs, gross	$33,545	$21,894
Less: Accumulated amortization	(18,006)	(11,872)
Internal use software development costs, net	$15,539	$10,022

Capitalized software development costs were $11.8 million, $8.0 million and $4.6 million for the years ended December 31, 2016, 2015 and 2014, respectively. Amortization expense with respect to software development costs totaled $6.2 million, $3.5 million and $2.0 million for the years ended December 31, 2016, 2015, and 2014, respectively.

Future amortization expense with respect to capitalized software development costs as of December 31, 2016 is estimated as follows (in thousands):

Years Ending December 31,	
2017	$7,510
2018	5,645
2019	2,367
2020	17
Total amortization expense	$15,539

7. Intangible Assets and Goodwill

Intangible assets consisted of the following as of December 31, 2016 and 2015 (in thousands, except years):

	December 31, 2016			
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Weighted Average Useful Life in Years
Customer relationships	$790	$ (392)	$ 398	5.0
Technology	4,811	(3,070)	1,741	6.0
Trademarks	930	(416)	514	9.0
Partner relationships	680	(397)	283	3.0
Non-compete agreements	40	(23)	17	3.0
Domain names	273	(241)	32	5.0
Patents	284	(164)	120	5.0
	$7,808	$ (4,703)	$ 3,105	5.9

	December 31, 2015			
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Weighted Average Useful Life in Years
Customer relationships	$790	$ (234)	$ 556	5.0
Technology	4,811	(2,268)	2,543	6.0
Trademarks	930	(293)	637	9.0
Partner relationships	680	(170)	510	3.0
Non-compete agreements	40	(10)	30	3.0
Domain names	274	(199)	75	5.0
Patents	286	(121)	165	5.0
	$7,811	$ (3,295)	$ 4,516	5.9

A summary of the activity within our intangible assets since December 31, 2015 is as follows (in thousands):

Intangible assets, net at December 31, 2015	$4,516
Additions	2
Dispositions	(5)
Amortization	(1,408)
Intangible assets, net at December 31, 2016	$3,105

Amortization expense totaled $1.4 million, $1.3 million and $0.9 million for the twelve months ended December 31, 2016, 2015 and 2014, respectively. Amortization expense for each of the five fiscal years through December 31, 2021 and thereafter is estimated as follows (in thousands):

Years Ending December 31,	
2017	$1,378
2018	928
2019	352
2020	259
2021	123
Thereafter	65
Total amortization expense	$3,105

The change in the carrying amount of goodwill is as follows (in thousands):

Goodwill as of December 31, 2014	$4,998
Acquisition of RentLinx	1,739
Goodwill as of December 31, 2015	6,737
Activity during fiscal 2016	—
Goodwill as of December 31, 2016	$6,737

8. Long-term Debt

Credit Agreement

On March 16, 2015, we entered into a credit facility (the “Original Credit Agreement”) comprised of a $10.0 million term loan (the “Term Loan”), and a $2.5 million revolving line of credit ("Original Revolving Agreement") with Wells Fargo. In March 2015, we borrowed $10.0 million under the Term Loan and on July 16, 2015, we made an optional prepayment in full of the Term Loan.

On October 9, 2015, we entered into Amendment Number One to the Original Credit Agreement, which amended the terms of the Original Credit Agreement, dated March 16, 2015, entered into by and among us, Wells Fargo, as administrative agent, and the lenders that are parties thereto (as amended, the “Credit Agreement”).

Under the terms of the Credit Agreement, the lenders made available to us a $25.0 million revolving line of credit (the “Revolving Facility”). Subject to customary terms and conditions, we can seek to increase the principal amount of indebtedness available under the Credit Agreement by up to $10.0 million, in the form of revolving commitments or term loan debt, although the lenders are under no obligation to make additional amounts available to us. Borrowings under the Revolving Facility are subject to the satisfaction of customary conditions.

Borrowings under the Revolving Facility bear interest at a fluctuating rate per annum equal to, at our option, (i) a base rate equal to the highest of (a) the federal funds rate plus 1/2 of 1%, (b) the London Interbank Offered Rate (“LIBOR”) for a one-month interest period plus 1% and (c) the rate of interest in effect for such day as publicly announced from time to time by Wells Fargo as its prime rate, in each case plus an applicable margin of 1.5%, or (ii) LIBOR for the applicable interest period plus an applicable margin of 2.5%. Interest is due and payable monthly. We are also required to pay a commitment fee equal to 0.25% per annum of the unused portion of the Revolving Facility if revolver usage is above $10.0 million, or 0.375% per annum of the unused portion of the Revolving Facility if revolver usage is less than or equal to $10.0 million.

The Revolving Facility matures on October 9, 2020; however, we can make payments on, and cancel in full, the Revolving Facility at any time without premium or penalty.

The Credit Agreement contains customary affirmative, negative and financial covenants. The affirmative covenants require us to, among other things, disclose financial and other information to the lenders, maintain its business and properties, and maintain adequate insurance. The negative covenants restrict us from, among other things, incurring additional indebtedness,

prepaying certain types of indebtedness, encumbering or disposing of its assets, making fundamental changes to our corporate structure, and making certain dividends and distributions. The financial covenants require us to maintain liquidity of not less than $12.5 million and, to the extent liquidity is determined to be below $25.0 million, to comply with a maximum senior leverage ratio. At December 31, 2016, we were in compliance with the financial covenants of the Credit Agreement.

As of December 31, 2016, there was no outstanding balance and as of December 31, 2015, there was an outstanding balance of $12,000 under the Credit Agreement.

Debt Financing Costs

Debt financing costs are deferred and amortized, using the straight-line method for costs related to the Revolving Facility. In conjunction with the amendment to our Credit Agreement for the Revolving Facility, we incurred costs to process the amendment and we capitalized additional costs of $0.2 million. These additional costs were added to the unamortized debt financing costs from the Original Revolving Facility of $0.1 million and are amortized using a straight-line method over the term of the Revolving Facility's commitment within interest expense. The total unamortized debt financing costs for the amended Revolving Facility of $0.2 million were recorded within Other assets at December 31, 2016.

In 2015, we incurred fees to Wells Fargo attributable to the Term Loan of $0.3 million and other third-party debt financing costs of $0.1 million, which were recorded as a reduction of the carrying amount of the Term Loan. Amortization of such costs was included in interest expense. When the Term Loan was repaid prior to the maturity date, the unamortized debt financing costs related to the Term Loan of $0.4 million were expensed as interest expense. Total interest expense for the year ended December 31, 2015 was $0.8 million.

9. Commitments and Contingencies

Lease Obligations

As of December 31, 2016, we had operating lease obligations of approximately $8.3 million through 2022. A summary of our future minimum payments for obligations under non-cancellable operating leases were as follows (in thousands):

Years Ending December 31,	
2017	$2,375
2018	1,769
2019	1,680
2020	1,667
2021	621
Thereafter	180
Total lease commitments	$8,292

We recorded rent expense of $2.0 million, $1.2 million and $1.0 million for the twelve months ended December 31, 2016, 2015 and 2014, respectively.

In February 2017, we signed a lease amendment for 50 Castilian Drive in Santa Barbara, California, our corporate headquarters. This amendment extends the term from February 2018 to December 2021. The total commitment under this lease extension is $3.1 million. All other terms and conditions from the original lease and previous amendments remain the same.

Insurance

We have a wholly owned subsidiary, Terra Mar Insurance Company, Inc. (“Terra Mar”), which was established to provide our customers with the option to purchase tenant liability insurance. If our customers choose to use our insurance services, they are issued an insurance policy underwritten by our third-party service provider. The policy has a limit of $100,000 per incident for each insured residence. We have entered into a reinsurance agreement with our third-party service provider and, as a result, we assume a 100% quota share of the tenant liability insurance provided to our customers through our third-party service provider. Included in cost of revenue we accrue for reported claims and an estimate of losses incurred but not reported by our property manager customers, as we bear the risk related to claims. Our liability for reported claims and incurred but not reported claims as of December 31, 2016 and

2015 was $0.3 million and $0.5 million, respectively, and is included in other current liabilities on the Consolidated Balance Sheets.

Included in other current assets as of December 31, 2016 and 2015 are $1.2 million and $1.0 million, respectively, of deposits held with a third party related to requirements to maintain collateral for our insurance services.

Litigation

From time to time, we may become subject to certain legal proceedings, including without limitation claims and/or litigation matters, arising in the ordinary course of business. We are not currently a party to any such legal proceedings, nor are we aware of any pending or threatened litigation, that would have a material adverse effect on our business, operating results, cash flows or financial condition should such litigation be resolved unfavorably.

Indemnification

In the ordinary course of business, we may provide indemnification of varying scope and terms to customers, investors, directors and officers with respect to certain matters, including, but not limited to, losses arising out of our breach of any applicable agreements, services to be provided by us, or intellectual property infringement claims made by third parties. These indemnification provisions may survive termination of the underlying agreement and the maximum potential amount of future payments we could be required to make under these indemnification provisions may not be subject to maximum loss clauses. The maximum potential amount of future payments we could be required to make under these indemnification provisions is indeterminable. We have never paid a material claim, nor have we been sued in connection with these indemnification arrangements. As of December 31, 2016 and 2015, we had not accrued a liability for these indemnification arrangements because we have determined that the likelihood of incurring a payment obligation, if any, in connection with these indemnification arrangements is not probable or reasonably possible and the amount or range of amounts of any such liability is not reasonably estimable.

10. Stockholders' Equity

Amended and Restated Certificate of Incorporation

Upon the effectiveness of the Amended and Restated Certificate of Incorporation of the Company on June 25, 2015, the number of shares of capital stock that is authorized to be issued was increased to 325,000,000 shares, of which 250,000,000 shares are Class A common stock, 50,000,000 shares are Class B common stock and 25,000,000 are undesignated preferred stock. The Class A common stock, Class B common stock and preferred stock have a par value of $0.0001 per share.

At December 31, 2016, there were 11,691,000 of Class A common shares outstanding, 22,028,000 of Class B shares outstanding and no preferred shares outstanding.

Class A Common Stock and Class B Common Stock

Except for voting rights, or as otherwise required by applicable law, the shares of our Class A common stock and Class B common stock have the same powers, preferences and rights and rank equally, share ratably and are identical in all respects as to all matters. The rights and preferences are as follows:

Dividend Rights. Subject to preferences that may apply to any shares of preferred stock outstanding at the time, the holders of outstanding shares of our Class A common stock and Class B common stock are entitled to receive dividends out of funds legally available at the times and in the amounts that our board of directors may determine.

Voting Rights. The holders of our Class A common stock are entitled to one vote per share, and holders of our Class B common stock are entitled to 10 votes per share. The holders of our Class A common stock and Class B common stock will vote together as a single class on all matters submitted to a vote of our stockholders, unless otherwise required by Delaware law or our amended and restated certificate of incorporation. Delaware law could require either holders of our Class A common stock or holders of our Class B common stock to vote separately. In addition, our amended and restated certificate of incorporation requires the approval of the holders of at least a majority of the outstanding shares of our Class B common stock, voting as a separate class to approve a change-in-control transaction.

Conversion. Each share of our Class B common stock is convertible at any time at the option of the holder into one share of our Class A common stock. In addition, each share of our Class B common stock will convert into one share of our Class A common stock upon any transfer, whether or not for value, except for certain transfers described in our amended and restated certificate of incorporation, including, without limitation, (i) a transfer by a partnership or limited liability company that was a registered holder of our Class B common stock at the "effective time," as defined in our amended and restated certificate of incorporation, to a partner or member thereof at the effective time or (ii) a

transfer to a “qualified recipient,” as defined in our amended and restated certificate of incorporation.
All the outstanding shares of our Class B common stock will convert automatically into shares of our Class A common stock upon the date when the number of outstanding shares of our Class B common stock represents less than 10% of all outstanding

shares of our Class A common stock and Class B common stock. Once converted into our Class A common stock, our Class B common stock may not be reissued.

Right to Receive Liquidation Distributions. Upon our dissolution, liquidation or winding-up, the assets legally available for distribution to our stockholders are distributable ratably among the holders of our Class A common stock and Class B common stock, subject to prior satisfaction of all outstanding debt and liabilities and the preferential rights and payment of liquidation preferences, if any, on any outstanding shares of preferred stock.

Reverse Stock Split

On June 4, 2015, we effected a one-for-four reverse split of our common stock and a proportional adjustment to the conversion ratio of our convertible preferred stock. The par value and the number of authorized shares of our common stock and convertible preferred stock were not adjusted as a result of the reverse split. All share, per share and related information presented in these Consolidated Financial Statements and accompanying notes has been retroactively adjusted, where applicable, to reflect the impact of the reverse stock split, including an adjustment to the preferred stock conversion ratio.

Initial Public Offering - Class A Common Stock

On June 30, 2015, we completed an initial public offering ("IPO") of our Class A common stock. In connection with the offering, we sold 6,200,000 shares of common stock at $12.00 per share for aggregate net proceeds of $65.1 million after underwriting discounts and commissions and offering expenses. Upon the closing of the offering, all shares of our convertible preferred stock and common stock held prior to the offering were converted into shares of Class B common stock.

On July 8, 2015, in connection with the exercise of an overallotment option granted to the underwriters, we sold 930,000 additional shares of our Class A common stock to the underwriters at the public offering price of $12.00 per share, resulting in an additional $10.4 million in net proceeds, after deducting underwriting discounts and commissions. As a result, the aggregate net proceeds to us from the sale of shares in the IPO were approximately $75.4 million.

Preferred Stock

Effective upon the filing of our amended and restated certificate of incorporation in June 2015, no shares of preferred stock were outstanding because all outstanding shares of our convertible preferred stock converted into our Class B common stock.

Pursuant to the terms of our amended and restated certificate of incorporation, our board of directors will be authorized, subject to limitations prescribed by Delaware law, to issue up to 25,000,000 shares of our preferred stock in one or more series, to establish from time to time the number of shares to be included in each series, and to fix the designation, powers, preferences and rights of the shares of each series and any of its qualifications, limitations or restrictions, in each case without further action by our stockholders. The number of authorized shares of any series of preferred stock may be increased or decreased, but not below the number of shares of that series then outstanding, by the affirmative vote of the holders of a majority of the voting power of our outstanding capital stock entitled to vote thereon, or such other vote as may be required by the certificate of designation establishing the series.

Convertible Preferred Stock Prior to IPO

Up until our IPO, we had authorized preferred stock consists of Series A convertible preferred stock ("Series A"), Series B convertible preferred stock ("Series B"), Series B-1 convertible preferred stock ("Series B-1"), Series B-2 convertible preferred stock ("Series B-2") and Series B-3 convertible preferred stock ("Series B-3") (collectively the "preferred stock prior to IPO").

Each preferred stockholder was entitled to the number of votes equal to the number of shares of common stock into which each preferred share was convertible at the time of such vote. The preferred stock was also entitled to receive non-cumulative dividends, when and if declared by our board of directors. No dividends were declared by our board of directors. In the event of a liquidation, the preferred stock was entitled to receive prior to payment of any amounts to the common stockholders the greater of (i) the original issuance price plus any declared but unpaid dividends or (ii) such amount per share as would have been payable had all shares of preferred stock been converted into common

stock immediately prior to such liquidation, dissolution or winding up. The preferred stock was convertible into common stock at the option of the holder or automatically upon a qualified initial public offering. The preferred stock automatically converted to Class B common upon the Company's initial public offering.

The liquidation preference provisions of the convertible preferred stock prior to IPO are considered contingent redemption provisions because there are certain elements that were not solely within our control, such as a change in control. Accordingly, we presented the convertible preferred stock prior to IPO within the mezzanine portion of the consolidated balance sheets.

11. Stock-Based Compensation

Stock Options

2015 Stock Incentive Plan

In conjunction with our IPO in 2015, our board of directors and stockholders adopted the 2015 Stock Incentive Plan, or the 2015 Plan. Upon adoption of the 2015 Plan, 2,000,000 shares of our Class A common stock were reserved and available for grant and issuance. On January 1 of each subsequent calendar year, the number of shares available for grant and issuance under the Plan increase by the lesser of (i) the number of shares of our Class A common stock subject to awards granted under the Plan during the preceding calendar year and (ii) such lesser number of shares of our Class A common stock determined by our board of directors. As of December 31, 2016, we have reserved an aggregate of 2,199,574 shares of our Class A common stock for grant and issuance under the 2015 Plan. The number of shares of our Class A common stock is also subject to adjustment in the event of a recapitalization, stock split, reclassification, stock dividend or other change in our capitalization. The 2015 Plan authorizes the award of stock options, stock appreciation rights ("SARs"), RSAs, RSUs, performance awards and stock bonuses. The 2015 Plan provides for the grant of awards to our employees, directors, consultants and independent contractors, subject to certain exceptions. RSUs, PSUs, PSOs, stock options, RSAs and RSUs have been issued during 2016 pursuant to the 2015 Plan.

Stock options may vest based on the passage of time or the achievement of performance conditions at the discretion of our compensation committee. Our compensation committee may provide for stock options to be exercised only as they vest or to be immediately exercisable with any shares issued on exercise being subject to our right of repurchase that lapses as the shares vest. The maximum term of stock options granted under the 2015 Plan is 10 years. We began granting stock options with performance conditions in 2016.

RSUs and PSUs represent the right on the part of the holder to receive shares of our Class A common stock at a specified date in the future or the achievement of performance conditions at the discretion of our compensation committee, subject to forfeiture of that right due to termination of employment. If an RSU or PSU has not been forfeited, then, on the specified date, we will deliver to the holder of the RSU or PSU shares of our Class A common stock.

2007 Stock Incentive Plan

On February 14, 2007, our board of directors adopted the 2007 Stock Incentive Plan (the “2007 Plan”) as an amendment and restatement to an original 2006 Equity Incentive Plan and was most recently amended in July 2014. Under the 2007 Plan, the number of shares of our common stock to be granted or subject to options or rights may not exceed 4.3 million. The 2007 Plan was administered by our board of directors, which determines the terms and conditions of each grant. Employees, officers, directors and consultants are eligible to receive stock options and stock awards under the 2007 Plan. The aggregate number of shares available under the 2007 Plan and the number of shares subject to outstanding options automatically adjusts for any changes in the outstanding common stock by reason of any recapitalization, spin-off, reorganization, reclassification, stock dividend, stock split, reverse stock split, or similar transaction. The exercise price of incentive stock options may not be less than the fair value of our common stock at the date of grant. The exercise price of incentive stock options granted to individuals that own greater than 10% of our voting stock may not be less than 110% of the fair value of our common stock at the date of grant. The term of each stock option cannot exceed ten years. Our board of directors will determine the vesting terms of all stock options. Generally, our board of directors has granted options with vesting terms of four years and contractual terms of ten years.

A summary of our stock option activity for the year ended December 31, 2016 is as follows (number of shares in thousands):

	Number of Shares	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Life in Years
Options outstanding as of December 31, 2015	1,171	$ 5.30	8.0
Options granted	750	12.85	
Options exercised	(141)	2.49	
Options cancelled/forfeited	(62)	7.62	
Options outstanding as of December 31, 2016	1,718	$ 8.75	8.2
As of December 31, 2016:			
Options vested or expected to vest	1,702	$ 8.75	8.2
Options exercisable (1)	548	$ 4.66	6.8

(1) Included in the options exercisable is 83,000 shares which have an early exercise option. The weighted average exercise price of these options is $5.64 per share and the weighted average contractual life in years is 8.1 years.

During the year ended December 31, 2016, we granted PSOs to purchase up to 750,000 shares of our Class A common stock. The PSOs have a weighted average exercise price of $12.85 per share. Vesting of the PSOs is based on achievement of a pre-established free cash flow performance metric for the years ended December 31, 2016, 2017 and 2018 and continued employment throughout the performance period. We recognize expense for the PSOs based on the grant date fair value of the PSOs that we determine are probable of vesting. Adjustments to compensation expense are made each period based on changes in our estimate of the number of PSOs that are probable of vesting. The number of PSOs granted, as included in the above table, assumes achievement of the performance metric at the maximum level, which is 150% of the targeted performance metric. For performance at 100% of the targeted metric, approximately 67% of the PSOs would vest. For performance at 80% of the targeted metric, approximately 33% of the PSOs would vest. For performance below 80% of the 2016 and 2018 targeted metric, no PSOs would vest, no compensation expense would be recognized and all previously recognized compensation expense for PSOs would be reversed. For performance below 50% of the 2017 targeted metric, no PSOs would vest, no compensation expense would be recognized and all previously recognized compensation expense for PSOs would be reversed.

The fair value of stock options granted is estimated on the date of grant using the Black-Scholes option-pricing model. Our stock-based compensation expense for stock options for the years ended December 31, 2016, 2015 and 2014 was $2.4 million $0.7 million, and $0.1 million, respectively.

The following table summarizes information relating to our stock options granted during the years ended December 31, 2016, 2015 and 2014:

	Year Ended December 31,		
	2016	2015	2014
Stock options granted (in thousands)	750	359	702
Weighted average exercise price per share	$12.85	$9.53	$4.60
Weighted average grant-date fair value per share	$4.85	$6.89	$2.2
Weighted average Black-Scholes model assumptions:			
Risk-free interest rate	1.45 %	1.58 %	1.86 %
Expected term (in years)	5.9	6.2	6.2
Expected volatility	37 %	46 %	48 %
Expected dividend yield	—	—	—

As of December 31, 2016, the total remaining stock-based compensation expense for unvested stock options was $2.9 million, which is expected to be recognized over a weighted average period of 1.7 years.

The total intrinsic value of options exercised in 2016, 2015 and 2014 was $1.9 million, $3.1 million, and $0.4 million, respectively. This intrinsic value represents the difference between the fair value of our common stock on the date of exercise and the exercise price of each option. Based on the fair value of our common stock as of December 31, 2016, the total intrinsic value

of all outstanding options was $25.9 million. The total intrinsic value of exercisable options as of December 31, 2016 was $10.5 million. The total intrinsic value of options vested and expected to vest as of December 31, 2016 was $25.7 million.

The excess tax benefit realized from option exercises during the year ended December 31, 2016 was $0.2 million. There were no excess tax benefits realized for the tax deductions from stock options exercised during the years ended December 31, 2015 and 2014.

Restricted Stock Awards

A summary of activity in connection with our restricted stock awards for the year ended December 31, 2016 is as follows (number of shares in thousands):

	Number of Shares	Weighted-Average Grant Date Fair Value per Share
Unvested as of December 31, 2015	120	$ 4.68
Granted	22	13.46
Vested	(96)	4.86
Forfeited	—	—
Unvested as of December 31, 2016	46	$ 8.55

We have the right to repurchase any unvested restricted stock granted upon termination of employment. Restricted stock vests over a four-year period for employees and over a one-year period for non-employee directors. For the years ended December 31, 2016, 2015 and 2014, we recognized stock-based compensation expense for restricted stock awards of $454,000, $381,000 and $804,000, respectively. During 2016, the grant date fair value of the shares vested was $469,000.

As of December 31, 2016, the total remaining stock-based compensation expense for unvested restricted stock awards was $0.2 million, which is expected to be recognized over a weighted average period of 0.9 years.

Restricted Stock Units

A summary of activity in connection with our RSU for the year ended December 31, 2016 is as follows (number of shares in thousands):

	Number of Shares	Weighted- Average Grant Date Fair Value per Share
Unvested as of December 31, 2015	17	$ 15.45
Granted	536	$ 13.26
Vested	(16)	$ 15.45
Forfeited	(41)	$ 12.35
Unvested as of December 31, 2016	496	$ 13.34

During the year ended December 31, 2016, we granted 449,000 RSUs that vest annually over four years and 87,000 PSUs that vest based upon achievement of a pre-established free cash flow performance metric for the years ended December 31, 2016, 2017 and 2018 and continued employment throughout the performance period. We recognize expense for the PSUs based on the grant date fair value of the PSUs that we determine are probable of vesting. Adjustments to compensation expense are made each period based on changes in our estimate of the number of PSUs that are probable of vesting. The number of PSUs granted, as included in the above table, assumes achievement of the performance metric at 100% of the targeted performance metric. The actual number of shares to be issued at the end of the performance period will range from 0% to 150% of the initial target awards. For performance at 150% of the targeted metric, 150% of the PSUs would vest. For performance at 80% of the targeted metric, approximately 50% of the PSUs would vest. For performance below 80% of targeted metric for 2016 and 2018, no PSUs would vest and no compensation expense would be recognized and all previously recognized compensation expense for PSUs would be reversed. For performance below 50% of targeted metric for 2017, no PSUs would vest and no compensation expense

would be recognized and all previously recognized compensation expense for PSUs would be reversed.
Our stock-based compensation expense for the RSUs and PSUs for the year ended December 31, 2016 and 2015, was $1.8 million and $70,000, respectively. There were no RSU or PSU grants for the year ended December 31, 2014.

As of December 31, 2016, the total remaining stock-based compensation expense for these RSUs was $5.0 million, which is expected to be recognized over a weighted average period of 2.9 years.

12. Income Taxes

For the years ended December 31, 2016 and 2015, we recorded income tax expense of $67,000 and $75,000, respectively, associated with state minimum taxes and the amortization of tax deductible goodwill that is not an available source of income to realize the deferred tax asset. We had no provision for income taxes for the year ended December 31, 2014, because we incurred losses and maintained a full valuation allowance against our net deferred tax assets.

Our effective tax rate differs from the U.S. Federal statutory rate of 34% primarily because our losses have been offset by a valuation allowance due to uncertainty as to the realization of the tax benefit of net operating losses. Set forth below is a reconciliation of the components that caused our provision for income taxes to differ from amounts computed by applying the U.S. Federal statutory rate of 34% for the years ended December 31, 2016, 2015 and 2014:

	Year Ended December 31,		
	2016	2015	2014
Income tax benefit at the statutory rate	34 %	34 %	34 %
State and local income taxes, net of federal benefit	7	3	5
Stock-based compensation expense	(4)	(2)	—
Meals and entertainment	(2)	(1)	(1)
Permanent differences	(1)	—	(1)
Change in valuation allowance	(42)	(38)	(41)
Research and development credits	7	3	4
Provision for income taxes	(1)%	(1)%	— %

The components of deferred tax assets (liabilities) were as follows (in thousands):

	December 31,	
	2016	2015
Deferred income tax assets:		
Net operating loss carryforwards	$31,436	$29,178
Research and development tax credits	4,032	2,867
Other	2,771	1,030
Gross deferred tax assets	38,239	33,075
Valuation allowance	(29,417)	(25,926)
Deferred tax assets, net of valuation allowance	8,822	7,149
Deferred tax liabilities:		
Property, equipment and software	(5,820)	(4,208)
Intangible assets	(403)	(804)
State taxes	(2,040)	(1,742)
Other	(632)	(427)
Total deferred tax liabilities	(8,895)	(7,181)
Total net deferred tax liabilities	$(73)	$(32)

As of December 31, 2016, we had federal net operating loss carryforwards of $80.7 million, which will begin to expire in 2027. As of December 31, 2016, we had state net operating loss carryforwards of $50.5 million, which will begin to expire in 2017. As of December 31, 2016 we also had federal and state research and development credit carryforwards of $3.9 million and $4.1 million, respectively. The federal credit carryforwards will begin to expire in 2027, while the state credits carryforward indefinitely.

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The Internal Revenue Code of 1986, as amended ("IRC"), imposes substantial restrictions on the utilization of net operating losses and other tax attributes in the event of an "ownership change" of a corporation. Accordingly, a company's ability to use pre-change net operating loss and research tax credits may be limited as prescribed under IRC Section 382. Events which may cause limitation in the amount of the net operating losses and credits that we utilize in any one year include, but are not limited to, a cumulative ownership change of more than 50% over a three-year period. Due to the effects of historical equity issuances and the current year IPO, utilization of our net operating losses may be limited pursuant to IRC Section 382. The IRC Section 382 limitation is not expected to have a material effect on our financial statements.

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to use the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred through December 31, 2016. Such objective evidence limits the ability to consider other subjective positive evidence such as its future income projections. On the basis of this evaluation, as of December 31, 2016, a valuation allowance of $29.4 million has been recorded since it is more likely than not that the deferred tax assets will not be realized.

The change in the valuation allowance for the years ended December 31, 2016, 2015 and 2014 was as follows (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Valuation allowance, at beginning of year	$25,926	$19,900	$16,358
Increase in valuation allowance	3,491	6,026	3,542
Valuation allowance, at end of year	$29,417	$25,926	$19,900

The following is a reconciliation of the total amounts of unrecognized tax benefits (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Unrecognized tax benefit beginning of year	$2,867	$2,014	$1,600
Decreases-tax positions in prior year	—	—	(278)
Increases-tax positions in current year	1,165	853	692
Unrecognized tax benefit end of year	$4,032	$2,867	$2,014

The unrecognized tax benefits are recorded as a reduction to the deferred tax assets. Since there is a full valuation allowance recorded against the deferred tax assets, the recognition of previously unrecognized tax benefits on uncertain positions would result in no impact to the effective tax rate.

As of December 31, 2016 and 2015, we had no accrued interest and penalties related to uncertain income tax positions. We do not anticipate that the amount of unrecognized tax benefits will significantly increase or decrease within the next 12 months.

We are subject to taxation in the United States and various states. Due to the net operating loss carryforwards, the Company's federal and state returns are open to examination by the Internal Revenue Service and state jurisdictions for all years since inception. We are not currently under audit by any taxing authorities.

The Company has excluded excess windfall tax benefits resulting from stock option exercises as components of the Company's gross deferred tax assets and corresponding valuation allowance disclosures, as tax attributes related to such windfall tax benefits should not be recognized until they result in a reduction of taxes payable. The tax effected amount of gross unrealized net operating loss carryforwards, and their corresponding valuation allowances resulting from stock option exercises was $0.2 million at December 31, 2016; the corresponding gross amount is $0.7 million. When realized, excess windfall tax benefits are credited to additional paid-in capital. The Company follows the with-and-without allocation approach to determine when such net operating loss carryforwards have been realized.

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13. Revenue and Other Information

Our chief operating decision maker reviews separate revenue information for our core solutions, Value+ and other service offerings as a measure of growth in the number of our customers and growth in the adoption and utilization of our core solutions and Value+ services by new and existing customers. The following table presents our revenue categories for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Core solutions	$43,775	$32,119	$22,406
Value+ services	56,965	37,998	22,525
Other	4,846	4,860	2,740
Total revenues	$105,586	$74,977	$47,671

Core solutions revenues includes our subscription fees which are designed to scale to the size of our customers' businesses. We recognize subscription revenue ratably over the terms of the subscription agreements, which typically range from one month to one year. Revenue from subscription services is impacted by the change in the number and type of our customers, the size and needs of our customers' businesses and our customer renewal rates.

Value+ services revenue includes revenue from subscriptions or usage-based fees. Subscription Value+ services include website hosting services and contact center services. Usage-based Value+ services include fees for electronic payment processing, resident screening services, tenant liability insurance program, collections, and online vacancy advertising services based on the RentLinx software platform acquired in April 2015.

Other services revenue includes one-time services related to on-boarding our core solutions, website design services and online vacancy advertising services offered to legacy RentLinx customers.

Our revenue is generated primarily from U.S. customers. All of our property and equipment is located in the U.S.

14. Retirement Plans

We have a 401(k) retirement and savings plan made available to all employees. The 401(k) plan allows each participant to contribute up to an amount not to exceed an annual statutory maximum. We may, at our discretion, make matching contributions to the 401(k) plan. Cash contributions to the plan were $1.1 million for the year ended December 31, 2016, and no cash contributions to the plan were made during the years ended December 31, 2015 and 2014. Contribution expense recognized for the 401(k) plan was $0.7 million, $0.4 million, and $0, for the years ended December 31, 2016, 2015, and 2014, respectively.

15. Subsequent Events

In February 2017, we signed a lease amendment for 50 Castilian Drive in Santa Barbara, California, our corporate headquarters. This amendment extends the term from February 2018 to December 2021. The total commitment under this lease extension is $3.1 million. All other terms and conditions from the original lease and previous amendments remain the same.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the supervision and participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2016, the last day of the period covered by this Annual Report. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to provide reasonable assurance that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and other procedures designed to provide reasonable assurance that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time period specified by the SEC’s rules and forms and that such information is accumulated and communicated to the company’s management, including its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Based on our management's evaluation, our principal executive officer and principal financial officer have concluded that, as of December 31, 2016, our disclosure controls and procedures were effective at the reasonable assurance level.

Inherent Limitations on Effectiveness of Disclosure Control

In designing and evaluating our disclosure controls and procedures, our management recognizes that no evaluation of controls can provide absolute assurance that all control issues within a company have been detected. In addition, the design of disclosure controls and procedures must reflect the fact that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs. Accordingly, our disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the objectives of our disclosure controls system are met.

Management’s Annual Report on Internal Control over Financial Reporting

We are responsible for establishing and maintaining internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, our management used the Internal Control – Integrated Framework (2013) as issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Based on this assessment, management concluded that our internal control over financial reporting is effective as of December 31, 2016.

This Annual Report does not include an attestation report of our registered public accounting firm due to an exemption established by rules of the Commission for emerging growth companies.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13(a)-15(d) and 15d-15(d) under the Exchange Act that occurred during the quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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ITEM 9B. OTHER INFORMATION

Execution of Fourth Amendment to Lease Agreement

On February 22, 2017, we entered into a Fourth Amendment to Lease, or the Lease Amendment, with Nassau Land Company, L.P., which amends the terms of that certain Multi-Tenant Industrial Lease, as amended, or the Lease, originally entered into by and between the parties on April 1, 2011, pursuant to which the Company leases office space in the building located at 50 Castilian Drive in Santa Barbara, California.

Pursuant to the Lease Amendment, the lease term was extended from February 2018 to December 2021. The Lease Amendment does not change any other material provisions of the Lease.

The foregoing summary of the Lease Amendment is qualified in its entirety by reference to the full text of the Lease Amendment, which is filed as Exhibit 10.2 to this Annual Report.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item will be included in the Proxy Statement, which will be filed with the SEC not later than 120 days after the end of our fiscal year ended December 31, 2016, and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this item will be included in the Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENTS SCHEDULES

The following documents are filed as part of this Annual Report:

1. Consolidated Financial Statements
Our consolidated financial statements are listed in the “Index to Consolidated Financial Statements” under Part II, Item 8, of this Annual Report.

2. Financial Statement Schedules
All financial statement schedules have been omitted because they are not required or are not applicable, or the required information is shown in our consolidated financial statements or the notes thereto.

3. Exhibits
The documents listed in the Exhibit Index of this Annual Report are filed, furnished or incorporated by reference with this Annual Report, in each case as indicated therein.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this Annual Report to be signed on its behalf by the undersigned thereunto duly authorized.

AppFolio, Inc.

Date: February 27, 2017 By: /s/ Ida Kane
Ida Kane
Chief Financial Officer
(Principal Financial and Accounting Officer)

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each individual whose signature appears below hereby constitutes and appoints Brian Donahoo and Ida Kane, and each or either of them, acting individually, as his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report, and to file the same, with all exhibits thereto and other documents in connection therewith, with the SEC, granting unto said attorney-in-fact and agent, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully for all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or any of them, or their or his or her substitutes, may lawfully do or cause to be done or by virtue hereof.

Pursuant to the requirements of the Exchange Act, as amended, this Annual Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

SIGNATURE	TITLE	DATE
/s/ Brian Donahoo Brian Donahoo	President, Chief Executive Officer and Director (Principal Executive Officer)	February 27, 2017
/s/ Ida Kane Ida Kane	Chief Financial Officer (Principal Financial and Accounting Officer)	February 27, 2017
/s/ Andreas von Blottnitz Andreas von Blottnitz	Chairman of the Board	February 27, 2017
/s/ Timothy Bliss Timothy Bliss	Director	February 27, 2017
/s/ Janet Kerr Janet Kerr	Director	February 27, 2017
/s/ James Peters James Peters	Director	February 27, 2017
/s/ William Rauth William Rauth	Director	February 27, 2017
/s/ Klaus Schauser Klaus Schauser	Chief Strategist and Director	February 27, 2017

EXHIBIT INDEX

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Certificate of Incorporation of the registrant as currently in effect.	10-Q	001-37468	3.1	8/6/2015	
3.2	Amended and Restated Bylaws of the registrant as currently in effect.	10-Q	001-37468	3.2	8/6/2015	
4.1	Specimen Certificate for Class A Common Stock.	S-1/A	333-204262	4.1	6/4/2015	
4.2	Amended and Restated Investor Rights Agreement, by and among the registrant and the investors named therein, dated November 26, 2013.	S-1/A	333-204262	4.2	6/4/2015	
10.1	Multi-Tenant Industrial Lease, by and between the registrant and Nassau Land Company, L.P., dated April 1, 2011 ("2011 Lease"), as amended by First Amendment to 2011 Lease, dated November 11, 2011, Second Amendment to 2011 Lease, dated February 23, 2012, and Third Amendment to 2011 Lease, dated November 5, 2013.	S-1/A	333-204262	10.1	6/4/2015	
10.2	Fourth Amendment to 2011 Lease, by and between the registrant and Nassau Land Company, L.P., dated February 22, 2017.					X
10.3	Multi-Tenant Industrial Lease, by and between the registrant and Nassau Land Company, L.P., dated February 17, 2015 ("2015 Lease").	S-1/A	333-204262	10.2	6/4/2015	
10.4	First Amendment to 2015 Lease, by and between the registrant and Nassau Land Company, L.P., dated October 5, 2015.	10-Q	001-37468	10.2	11/9/2015	
10.5	Second Amendment to 2015 Lease, by and between the registrant and Nassau Land Company, L.P., dated February 22, 2016.	10-K	001-37468	10.4	2/29/2016	
10.6#	2007 Stock Incentive Plan, as amended, and related form agreements.	S-1/A	333-204262	10.3	6/4/2015	
10.7#	2015 Stock Incentive Plan and related form agreements.	S-1/A	333-204262	10.4	6/4/2015	
10.8#	2015 Employee Stock Purchase Plan.	S-1/A	333-204262	10.5	6/4/2015	
10.9	Form of Indemnification Agreement by and between the registrant and each of its executive officers and directors.	S-1	333-204262	10.6	5/18/2015	
10.10	Credit Agreement, by and among the registrant, Wells Fargo Bank, N.A., as administrative agent, and the lenders that are parties thereto, dated March 16, 2015.	S-1	333-204262	10.7	5/18/2015	
10.11	Amendment Number One to Credit Agreement, by and among the registrant, Wells Fargo Bank, N.A., as administrative agent, and the lenders that are parties thereto, dated October 9, 2015.	10-Q	001-37468	10.1	11/9/2015	

21.1	Subsidiaries of the registrant.	10-K	001-37468	21.1	2/29/2016

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
23.1	Consent of independent registered public accounting firm.					X
24.1	Power of Attorney (included on the signature page of this report).					X
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.					X
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.					X
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					X
101.INS	XBRL Instance Document.					X
101.SCH	XBRL Taxonomy Extension Schema Document.					X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.					X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.					X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.					X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.					X

# Indicates a management contract or compensatory plan or arrangement

* The certifications attached as Exhibit 32.1 accompany this Annual Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed “filed” by the registrant for purposes of Section 18 of the Exchange Act and are not to be incorporated by reference into any of the registrant’s filings under the Securities Act or the Exchange Act, irrespective of any general incorporation language contained in any such filing.