

MARCHEX INC  
Form 10-K  
March 03, 2014  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K**

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2013

or

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

Commission File Number 000-50658

**Marchex, Inc.**

(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of

incorporation or organization)

520 Pike Street, Suite 2000, Seattle, Washington 98101

35-2194038  
(I.R.S Employer

Identification No.)

Edgar Filing: MARCHEX INC - Form 10-K

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (206) 331-3300

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

Title of Each Class	Name of Exchange on Which Registered
Class B Common Stock,	The NASDAQ Stock Market LLC
\$0.01 par value per share	(NASDAQ Global Select Market)

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

None

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the 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.

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 <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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

Aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant was approximately \$136,247,265 as of June 30, 2013 based upon the closing sale price on the NASDAQ Global Select Market reported for such date. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

There were 7,770,215 shares of the registrant's Class A common stock issued and outstanding as of February 26, 2014 and 30,900,094 shares of the registrant's Class B common stock issued and outstanding as of February 26, 2014.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive proxy statement for the 2014 Annual Meeting of Stockholders are incorporated herein by reference in Part III of this Annual Report on Form 10-K to the extent stated herein.



**Table of Contents****TABLE OF CONTENTS**

	<b>Page</b>
<b>Part I</b>	
ITEM 1. <u>BUSINESS</u>	1
ITEM 1A. <u>RISK FACTORS</u>	14
ITEM 1B. <u>UNRESOLVED STAFF COMMENTS</u>	37
ITEM 2. <u>PROPERTIES</u>	37
ITEM 3. <u>LEGAL PROCEEDINGS</u>	37
ITEM 4. <u>MINE SAFETY DISCLOSURES</u>	37
<b>Part II</b>	
ITEM 5. <u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	38
ITEM 6. <u>SELECTED FINANCIAL DATA</u>	41
ITEM 7. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	43
ITEM 7A. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	71
ITEM 8. <u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	72
ITEM 9. <u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	111
ITEM 9A. <u>CONTROLS AND PROCEDURES</u>	111
ITEM 9B. <u>OTHER INFORMATION</u>	111
<b>Part III</b>	
ITEM 10. <u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	112
ITEM 11. <u>EXECUTIVE COMPENSATION</u>	112
ITEM 12. <u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	112
ITEM 13. <u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE</u>	112
ITEM 14. <u>PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	112
<b>Part IV</b>	
ITEM 15. <u>EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u>	113

---

**Table of Contents**

**FORWARD-LOOKING STATEMENTS**

*This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We use words such as believes , intends , expects , anticipates , plans , may , will and similar expressions to identify forward-looking statements. All forward-looking statements, including, but not limited to, statements regarding our future operating results, financial position, prospects, acquisitions and business strategy, expectations regarding our growth and the growth of the industry in which we operate, and plans and objectives of management for future operations, are inherently uncertain as they are based on our expectations and assumptions concerning future events. Any or all of our forward-looking statements in this report may turn out to be inaccurate. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. They may be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties, including the risks, uncertainties and assumptions described in Item 1A of this Annual Report on Form 10-K under the caption Risk Factors and elsewhere in this report. In light of these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this report may not occur as contemplated, and actual results could differ materially from those anticipated or implied by the forward-looking statements. All forward-looking statements in this report are made as of the date hereof, based on information available to us as of the date hereof, and we assume no obligation to update any forward-looking statement.*

**PART 1**

**ITEM 1. BUSINESS.**

**Overview**

References herein to we , us or our refer to Marchex, Inc. and its wholly-owned subsidiaries unless the context specifically states or implies otherwise.

Marchex is a mobile and call advertising technology company. We provide products and services for businesses of all sizes that depend on consumer calls to drive sales. Our technology platform delivers performance-based, pay-for-call advertising across numerous mobile and online publishers to connect millions of high-intent consumers with businesses over the phone. Our call analytics technology facilitates call quality, analyzes calls in real time and measures the outcomes of calls to close the loop between digital marketing and offline transactions. We help large national brands and small-and medium-sized businesses ( SMBs ) facilitate efficient and cost-effective marketing campaigns to drive calls and customer leads to their business. With our Archeo division, we provide a performance-based pay-per-click advertising service that connects advertisers with consumers across our owned and operated web sites as well as third party web sites and we also sell domain names.

Our technology-based products and services enable our customers to connect with consumers across leading third-party mobile and online channels, as well as our proprietary network of locally-focused web sites. We have direct relationships with large national advertisers and advertising agencies which utilize our products and services to plan, execute and measure their call-focused advertising campaigns. We also provide private-label performance marketing solutions for SMBs through a network of large reseller partners, which include Yellow Pages publishers, media and telecommunications companies and vertical marketing service providers. We enable these partners to sell pay-for-call advertising, call-analytics, search engine marketing and other digital marketing services to their millions of small business customers. We execute these campaigns for them using our technology. Our primary products offerings are:

**Marchex Call Marketplace.** Through the Marchex Call Marketplace, we deliver a variety of call advertising products and services to national advertisers, advertising agencies and small advertiser reseller partners. The Marchex Call Marketplace is a mobile advertising solution focused on delivering

---

## **Table of Contents**

customers on a pay-for-call basis. We offer exclusive and preferred ad placements across numerous mobile and online media sources to drive advertisers qualified calls to their businesses. It leverages our Marchex Call Analytics platform to secure call tracking numbers and to provide qualified calls to advertisers that block spam and other telemarketing calls while working to optimize the return on investment for advertisers' marketing investment.

***Marchex Call Analytics.*** Our Marchex Call Analytics technology platform provides data and insights that measure the performance of mobile, online and offline ad campaigns for advertisers and small business resellers. Our analytics technology tracks calls and helps advertisers understand which marketing channels, advertisements, keywords and creatives are driving calls to their business, allowing them to optimize their advertising expenditures across media channels. Call Analytics also includes call recording, call quality filtering and real-time call intelligence to provide rich insights into what is happening during a call and to measure the outcome of calls and return on investment. Advertisers pay us a fee for each call they receive from call-based ads we distribute through our sources of call distribution or for each phone number tracked based on a pre-negotiated rate.

***Local Leads.*** Our Local Leads platform is a white-labeled, full service advertising solution for small business resellers, such as Yellow Pages providers and vertical marketing service providers, to sell call advertising, search marketing and other lead generation products through their existing sales channels to their small business advertisers. These calls and leads are then fulfilled by us across our distribution network, including mobile sources, and leading search engines. The lead services we offer to small business advertisers through our Local Leads platform include products typically available only to national advertisers, including pay-for-call, search marketing and presence management, ad creation and include advanced features such as call tracking, geo-targeting, campaign management, reporting, and analytics. The Local Leads platform is highly scalable and has the capacity to support hundreds of thousands of advertiser accounts. Reseller partners and publishers generally pay us account fees and agency fees for our products in the form of a percentage of the cost of every click or call delivered to their advertisers.

In addition to our call-driven business, we operate the Archeo Domains Marketplace, which enables the buying, selling and development of premium domain names, and includes more than 200,000 of our owned and operated websites. Our portfolio of websites contains more than 75,000 U.S. ZIP code sites, including 90210.com and covering ZIP code areas nationwide. The Archeo domain marketplace also consists of other locally-focused sites such as Yellow.com, OpenList.com and geo-targeted sites. We monetize this portfolio via pay-per-click and banner advertising and also make these domains available for sale to third parties.

We generate two categories of revenue. Call-driven revenue consists of payments from advertisers for pay-for-call marketing services and for use of our Call Analytics technology. Call-driven revenue also consists of payments from our reseller partners for use of our technology platform and marketing services, which they offer to their small business customers, as well as payments from advertisers for cost-per-action services. Archeo revenue includes revenue generated from advertisements on our network of owned and operated websites and third-party distribution, as well as from the sale of domain names in our domain marketplace. During the years ended December 31, 2011, 2012 and 2013, call-driven revenue accounted for approximately 73%, 84%, and 89% of total revenues, respectively. We operate primarily in domestic markets. For detail on revenue by geographical area for the three most recent fiscal years, see *Note 13. Segment Reporting and Geographic Information* of the notes to our consolidated financial statements.

## **Industry Overview**

***Calls are critical for businesses to drive sales.*** For businesses of all sizes, in-bound phone calls are a key source of new customer leads and increased revenue. We believe consumers that call businesses directly typically have higher purchase intent and are more likely to make a purchase or become a customer. According to BIA/Kelsey Local Commerce Monitor (LCM) survey in 2012, 61.3% of advertisers believe that in-bound calls from prospective customers are the single most important type of lead. Calls are particularly relevant in high-value

## **Table of Contents**

categories, such as professional services, financial services, automotive and travel, where transaction values are large, complex or require additional information prior to completion. Calls are also important for local businesses that set appointments or sell products and services over the phone. According to 2012 data from BIA/Kelsey, advertisers in the U.S. spent \$68 billion to drive telephone leads. Historically, the majority of this advertising has been spent on traditional media such as television, newspapers and directories. Now with the mass adoption of mobile, both large and small advertisers are increasingly seeking new marketing channels that allow them to connect with consumers over the phone.

***Mobile search and calls from search are growing rapidly.*** Today we are witnessing an evolution in consumer behavior as Internet-enabled mobile devices proliferate and media consumption shifts to mobile devices. This trend is increasingly evident in the way consumers research products and services and connect with businesses when they are ready to make a purchase decision. BIA/Kelsey estimates that consumers conducted over 30 billion mobile searches in 2013, and that the number of mobile searches will exceed searches on desktop computers by 2016. Given the nature of mobile devices and embedded technology in mobile phones, consumers want and expect to be able to directly call businesses they are researching on mobile devices. According to a 2013 study by Google/Ipsos, over 70% of mobile search users have used a click-to-call feature to connect with a business directly from their mobile devices. BIA /Kelsey estimates that the total number of calls initiated from searches on mobile devices will increase from 15 billion in 2013 to 50 billion by 2015.

***Ad budgets are shifting to performance-based models.*** As businesses have expanded their marketing through digital channels, they have increasingly turned to performance-based advertising formats in which they are only charged when a desired outcome is reached. Performance-based advertising models provide advertisers with greater transparency into their advertising spend and the ability to accurately measure results and return on investment. Over time, the online advertising market has experienced a dramatic shift from CPM-based banner and display advertisements to cost-per-click search advertising and other forms of performance marketing. According to the Interactive Advertising Bureau, performance-based formats accounted for only 7% of the \$5 billion online advertising market in 1999, but grew to over 65% of the \$40 billion market in 2013.

***Calls are becoming the currency of mobile advertising.*** In 2013, the global mobile advertising market was \$15 billion and is expected to grow to \$52 billion by 2017, according to IDC. As the mobile advertising market matures, we believe advertisers will increasingly utilize performance based advertising formats available on mobile devices, as they did on desktop. Further, we believe the demand for businesses to connect with consumers over the phone combined with the inherent functionality and technical capabilities of mobile devices will result in calls becoming a primary measurement unit/format for mobile advertising. As advertisers continue to shift their budgets to accommodate for the growth of mobile and online channels, we believe the market for call-driven advertising will grow even more.

***Understanding calls is highly complex.*** Unlike clicks, impressions and other actions that are tracked and measured in digital format, calls take place offline and require unique technical capabilities and expertise to accurately measure and analyze. To realize the full benefit of call-based marketing, advertisers need technology that allows them to capture and analyze attributes of a call before, during and after the call is completed. This technology helps them properly measure return on investment ( ROI ) and optimize their marketing campaigns across media channels. For example, advertisers must be able to dynamically track the source of a call back to the media channels and advertisements that influenced the consumer to make the call. Once a call is initiated, technology is required to understand what is happening on a call in real-time, to record calls, and to block unwanted or spam calls. For advertisers with call center operations, calls are often tracked and routed through interactive voice response ( IVR ) phone systems and integrated with customer relationship management ( CRM ) applications and back-office systems to measure transactions and return on investment. Successful marketing analytics for calls requires expertise from multiple disciplines, including digital advertising, communications infrastructure, voice and speech recognition expertise, and marketing software.

## **Table of Contents**

### **Our Competitive Strengths**

***Focus on calls.*** We were early to realize the value of calls and the importance that mobile devices would play in advertising. Over the past several years, we have shifted the focus of our company to address the large opportunity for mobile performance-based advertising focused on calls. As a pioneer in the category, we have developed a unique business model that delivers measurable return on investment to both large national advertisers and local small businesses. Our technology platform and call analytics technology and products are specifically designed to address the unique challenges associated with closing the loop between digital marketing and phone calls. Working closely with our customers, we have innovated in call-based technology, creating specific solutions to address common needs and wants among both SMBs and large advertisers. We believe we are unique with our call-focused approach to technology developments and marketing solutions, providing a competitive advantage as mobile advertising grows and advertising budgets shift towards performance-based formats.

***Proprietary call analytics technology.*** Our call analytics technology and solutions are designed specifically to analyze and measure the performance of advertising and media spending that results in calls to businesses. The technology and solutions further help advertisers optimize their overall marketing strategies and specific campaigns by gaining insights into the different factors that can drive conversions. Our advertisers are able to benefit from increased intelligence about their specific media placement decisions and investments with dynamically driven data and information that capture and evaluate the originating media channel, advertisement, keyword or creative that drove the consumer to make the call. As a result, our technology helps advertisers understand the most effective use of advertising resources and helps to optimize their marketing spend across campaigns and distribution sources. We provide varying levels of integration with customers to enhance their information review and analysis. Our technology scales for larger customers to provide greater access and transparency on significant volumes of call leads, including with assisting the understanding of call outcomes and quality of customer experience. This integration may take the form of working with CRM platforms or customer-specific systems, with the purpose of improving each customer's understanding of the analytics within their organization. On the technology back end of these solutions are proprietary methods and features that allow for the smoother functioning and increased efficiencies in presenting the most potentially promising leads. We are always working to create appropriate and relevant filters to improve our customer experience. For example, our Clean Call technology blocks many unwanted, unintended, misdirected or spam calls from reaching our advertiser customers, reducing time and cost wasted on unproductive calls. Our focus on features that promote ease and efficiency of use for advertisers is aligned with improving their understanding of the quality and efficiency of the sources they have deployed to drive customer acquisition, including which sources may or may not be desirable or cost-effective. In each case, they may be able to better measure the performance of their advertisement investments across their spend mobile, online and offline ad campaigns.

***Transparent, performance-based model.*** We have developed a unique, pay-for-call business model that aligns our interests with those of our advertising customers and our publishing partners. We work closely with each customer to define a quality call for their business, and then only charge our customers, on a per call basis. As a result, we are able to deliver qualified leads that provide a measurable return on investment for our advertisers. We typically pay our publishing partners a percentage of the revenue we generate from advertisements on their properties. Through our Call Analytics, we have a deep understanding of which publishers, devices, ad formats, keywords and ad creatives drive call conversion for specific advertising verticals. This allows us to help optimize the placements of advertisements across our network to maximize the number of calls for our advertisers and revenue for our partners. As a result, advertisers utilize us to place ads on their behalf and our partners believe in us that we will only deliver ads on their properties to help generate revenue for them.

***Scalable technology platform and business model.*** We have developed our technology platform to address the large advertisers, while also being able to support a large number of small local business advertisers. Our platform currently supports over 100,000 unique advertiser accounts, and in aggregate manages hundreds of millions of dollars in advertising spend across various digital channels. We leverage our relationships with



## **Table of Contents**

Yellow Pages providers and vertical market service providers to efficiently re-sell our solutions to their small businesses customers, adding scale and data to our platform, which provides us with recurring revenues with minimal associated sales costs. We have deployed a direct sales model to acquire and service large advertisers and also have been successful at deepening our relationships with existing advertiser clients over time to capture a greater share of their advertising budgets.

### **Strategy**

#### **Our Strategy**

To take advantage of the shift to performance-based models in marketing, key elements of our strategy include:

***Building and Expanding Relationships with Advertising Agencies.*** Advertising agencies are influential in determining how large national advertisers allocate their advertising budgets. We believe building deep relationships with leading global advertising agencies and creating awareness within these agencies about the benefits of our offerings is an important step in attracting new large advertising customers. We plan to expand our agency relations efforts and hire personnel with strong existing relationships with advertising agencies.

***Innovating on Our Mobile Performance Advertising.*** We plan to continue to expand our range of call-based advertising product capabilities by offering innovative performance-based products such as pay-for-call advertising, along with the supporting analytics including number provisioning, call tracking, call mining, keyword-level tracking and other products as part of our owned, end-to-end, call-based advertising solutions. We are also focused on growing our base of call distribution by bringing in new sources of the rapidly growing mobile advertising market as well as other online and offline sources of distribution.

***Innovating on Our Products for Small Businesses.*** We plan to build and integrate new products into our marketing products for small businesses. This includes, (1) launching new performance-based small business solutions like pay-for-call advertising enhancements; (2) integrating more options for small businesses to acquire new customers over the phone, such as enhanced local ad-targeting capabilities that will enable us to consistently improve the matching of our small advertisers with our sources of call supply; (3) introducing products that enable small businesses to better cultivate relationships with existing customers; and (4) adding additional features and functionality to our web sites that connect consumers with small businesses and provide additional monetization capabilities. We believe these new products will increase our cross-sell opportunities, enable us to continue to grow our advertiser base, unlock more budget from our existing advertisers, enable us to attract new reseller partnerships and deliver better performance to our existing partners.

***Supporting the Number of Advertisers Using Our Products and Services.*** We plan to continue to provide a consistently high level of service and support to our advertisers and we will continue to help them achieve their return on investment goals. We are focused on continuing to grow our advertiser base through our direct sales and marketing efforts, including strategic sales, inside sales, online acquisition initiatives and additional partnerships with large local advertiser reseller partners.

***Developing New Markets including International Expansion.*** We intend to analyze opportunities and may seek to expand our technology-based products into new business areas or geographic markets where our services can be replicated on a cost-effective basis, or where the creation or development of a product or service may be appropriate. We anticipate utilizing various strategies to enter new markets, including: developing strategic relationships; acquiring products that address a new category or opportunity; and creating joint venture relationships and internal initiatives where existing services can be extended internationally.

**Table of Contents**

***Pursuing Selective Acquisition Opportunities.*** We may pursue select acquisition opportunities and will apply rigorous evaluation criteria to any acquisitions we may pursue in order to enhance our strategic position, strengthen our financial profile, augment our points of defensibility and increase shareholder value. We will focus on acquisition opportunities that represent a combination of the following characteristics:

under-leveraged and under-commercialized assets;

opportunities for business model, product or service innovation and evolution;

critical mass of transactions volume, advertisers, traffic, revenue and profits;

business defensibility;

revenue growth and expanding margins and operating profitability or the characteristics to achieve significant scale and profitability; and

an opportunity to enhance efficiencies and provide incremental growth opportunities for our operating businesses.

**Our Distribution Network**

We have built a broad distribution network for our pay-for-call and pay-per-click advertising services that includes hundreds of mobile sources, search engines and applications, directories, third party vertical and branded web sites, our proprietary web site traffic sources through our Archeo division, which are comprised of our owned and operated web sites, and offline sources.

***Syndicated Distribution:***

Through our call advertising services, our local leads, pay-per-click advertising services, and search marketing services, we distribute advertisements from our tens of thousands of advertisers, as well as from our reseller partners advertisers, through hundreds of call-ready media and traffic sources, including mobile sources, search engines and directories, web sites and our proprietary web site traffic sources.

Our Syndicated Distribution partners include:

<b>Selected Carriers</b>	<b>Selected Search Engines</b>	<b>Selected Call Sources and Vertical and Local Distribution Partners</b>
AT&T	Google	Avantar
Verizon	Microsoft	CityGrid
Sprint (Boost Mobile)	Yahoo!	Google Mobile
Metro PCS		MapQuest
T-Mobile		MSN
TracFone		Whitepages, Inc.

## Edgar Filing: MARCHEX INC - Form 10-K

Yahoo!

Payment arrangements with our distribution partners are often subject to minimum payment amounts per phone call or click-through. Other payment structures that we may use to a lesser degree include:

advance or fixed payments, based on a guaranteed minimum amount of usage delivered;

variable payments based on a specified metric, such as number of paid phone calls or click-throughs; and

a combination arrangement with both fixed and variable amounts.

## **Table of Contents**

### ***Proprietary Web Site Traffic Sources:***

We believe our proprietary web site traffic through our Archeo division is a source of local information online and is a source of click-throughs. It includes more than 200,000 web sites focused on helping users make informed decisions about products and services, including where to get local products and services.

The more than 200,000 owned and operated web sites in the network include more than 75,000 U.S. ZIP code sites, including 98102.com and 90210.com, covering ZIP code areas nationwide, as well as tens of thousands of other locally-focused sites such as Yellow.com, OpenList.com and geo-targeted sites. Traffic to our proprietary web sites is primarily monetized with pay-per-click listings that are relevant to the web sites, as well as other forms of advertising, including impression-based advertising.

### **Sales, Marketing & Business Development**

Our sales department focuses on adding new advertisers to our business, while our business development and partnership department focuses on adding new reseller partnerships, selectively adding new distribution partnerships and servicing existing partnerships. Our marketing department focuses on promoting our services through online customer acquisition, affiliate relationships, press coverage, strategic marketing campaigns and industry exposure. Advertising and promotion of our services is broken into the following main categories:

***Direct Sales.*** Our direct sales team targets new relationships with national advertisers and advertising agencies through in-person presentations, direct marketing, telesales and attendance at industry events, among other methods. Our advertiser agreements include a combination of agency fees, per-call and per-click fees.

***Reseller Partnerships.*** We have a business development team that focuses primarily on securing partnerships with large local advertiser reseller partners under which we supply our private-label small business advertising platform and/or other services, including advertiser distribution in our proprietary web site traffic network or our distribution network. Our reseller partner agreements include a combination of revenue sharing, licensing revenue, per-call and per-click fees.

***Online Acquisition.*** We market to advertisers for our proprietary web site traffic network, pay-per-click advertising and contextual advertising through certain online advertising and direct marketing campaigns that lead advertisers to our self-serve online sign up processes. Self-serve advertisers generally pay us per-click fees.

***Referral Agreements.*** We have referral agreements with entities that promote our services to large numbers of potential advertisers. Our referral partner agreements are based on a combination of revenue sharing and performance-based fees.

***Archeo Domains Marketplace.*** We launched Domains Marketplace in September 2013 which includes more than 200,000 of our owned and operated web sites that are for available for sale and facilitates the buying and transacting of domain names.

We intend to continue our strategy of growing our advertiser base through sales and marketing programs while being as efficient as possible in terms of our marketing and advertising costs. We continually evaluate our marketing and advertising strategies to maximize the effectiveness of our programs and their return on investment.

### **Information Technology and Systems**

We have a proprietary technology platform for the purposes of managing and delivering call and click-based advertising products and services to our partners. We also combine third party licenses and hardware to create an operating environment for delivering high quality products and services, with such features as automated online



## **Table of Contents**

account creation and management process for advertisers, real-time customer support with both interactive and online reporting for customers and partners. We employ commercially available technologies and products distributed by various companies, including Cisco, Dell, Oracle, Intel, AMD, Microsoft, IBM, Nuance and Veritas. We also utilize public domain software such as Apache, Linux, MySQL, PostgreSQL, Java, Scala and Tomcat.

Our technology platform is compatible with the systems used by our distribution partners, enabling us to deliver call and click-based advertising products and services through mobile, online and offline sources in rapid response to user queries made through such partners at scale. We continue to build and innovate additional functionality to attempt to meet the quickly evolving demands of the marketplace. We devote significant financial and human resources to improving our advertiser and partner experiences by continuing to develop our technology infrastructure. The cost of developing our technology solutions is included in the overall cost structure of our services and is not separately funded by any individual advertisers or partners. In order to maintain a professional level of service and availability, we primarily rely upon third parties to provide hosting services, including hardware support and service, and network monitoring at various domestic and international locations. Our servers are configured for high availability and large volumes of call, mobile and Internet traffic and are located in leased third party facilities. Back-end databases make use of redundant servers and data storage arrays. We also have standby servers that provide for additional capacity as necessary. The facilities housing our servers provide redundant HVAC, power and internet connectivity. As revenue grows and the volume of transactions and call, mobile and internet traffic increases, we will need to expand our network infrastructure. Inefficiencies in our network infrastructure to scale and adapt to higher call, mobile and internet traffic volumes could materially and adversely affect our revenue and results of operations.

We continuously review ways to improve major aspects of our technology support and maintenance, including improving, upgrading and implementing business continuity plans, data retention initiatives, and backup and recovery processes.

## **Competition**

Our call driven offerings currently or potentially compete with a variety of companies in a highly competitive and fragmented industry. We compete with leading search engines such as Google and Microsoft, digital advertising networks, mobile ad networks and call analytics technology providers. We also face competition on the call supply side, where competing companies look to outbid, partner with or otherwise secure sources of call supply we utilize. Our Archeo Domains Marketplace competitors include Demand Media, Name Media and Oversee.net. Many of our potential competitors, as well as potential entrants into our target markets, have longer operating histories, larger customer or user bases, greater brand recognition and greater financial, marketing and other resources than we have. Many current and potential competitors can devote substantially greater resources than we can to marketing, web site and systems development. In addition, as the use of the mobile, Internet, and other online services increases, there will likely be larger, more well-established and well-financed entities that acquire companies relevant to our business strategy; and invest in or form joint ventures in categories or countries relevant to our business strategy; all of which could adversely impact our business. Any of these trends could increase competition, reduce the demand for any of our services and could have a material adverse effect on our business, operating results and financial condition.

We believe our strategy allows us to work with most, if not all, of the relevant companies in our industry, even those companies that may be perceived as our competitors. To some extent, we may compete with our business partners, as we do with all other types of advertising sales companies and agencies. We may also compete with traditional offline media such as television, radio and print and direct marketing companies, for a share of advertisers' total advertising budgets. Although our strategy enables us to work with most, if not all, of our competitors, there are no guarantees that all companies will view us as a potential partner.

We provide our services to and also may compete with: (1) mobile and online advertisers; (2) partners who provide a distribution network for mobile, online, and offline advertising; and (3) other intermediaries who may

## **Table of Contents**

provide purchasing and/or sales opportunities, including advertising agencies, and other search engine marketing companies. Many of the companies that could fall into these categories are also our partners, including Google, Yahoo!, Citysearch, Microsoft and YP. We depend on maintaining and continually expanding our network of partners and advertisers to generate mobile and online transactions.

The mobile and online advertising and marketing services industry is highly competitive. In addition, we believe today's typical Internet and mobile advertiser is becoming more sophisticated in utilizing the different forms of Internet and mobile advertising, purchasing Internet and mobile advertising in a cost-effective manner, and measuring return on investment. The competition for this pool of advertising dollars has also put downward pressure on price points and mobile and online advertisers have demanded more effective means of reaching customers. We believe these factors have contributed to the growth in performance-based advertising relative to certain other forms of online advertising and marketing, and as a result this sector has attracted many competitors.

Due to the long-term growth trends in mobile and online advertising, these competitors, real and potential, range in size and focus. Our competitors may include such diverse participants as small referral companies, established advertising agencies, inventory resellers, search engines, and destination web sites. We are also affected by the competition among destination web sites that reach users or customers of search services. While thousands of smaller outlets are available to customers, several large media and search engine companies, such as Google, Yahoo!, Microsoft and IAC, dominate online user traffic. The online search industry continues to experience consolidation of major web sites and search engines, which has the effect of increasing the negotiating power of these parties in relation to smaller providers. The major destination web sites and distribution providers may have leverage to demand more favorable contract terms, such as pricing, renewal and termination provisions.

There are additional competitive factors relating to attracting and retaining users, including the quality and relevance of our search results, and the usefulness, accessibility, integration and personalization of the mobile and online services that we offer as well as the overall user experience on our web sites. The other features that we offer, which we believe attract advertisers are reach, effectiveness and creativity of marketing services, and tools and information to help track performance.

Finally, we operate in the relatively nascent market of call-based advertising. The adoption of these call-based products could take longer than we expect and could become more competitive as the category becomes more developed and visible.

## **Seasonality**

We believe we will experience seasonality. Our quarterly results have fluctuated in the past and may fluctuate in the future due to seasonal fluctuations in levels of mobile and Internet usage and seasonal purchasing cycles of many advertisers. Our experience has shown that during the spring and summer months, mobile and Internet usage is lower than during other times of the year and during the latter part of the fourth quarter of the calendar year we generally experience lower call volume and reduced demand for calls. The extent to which usage and call volume may decrease during these off-peak periods is difficult to predict. Prolonged or severe decreases in usage and call volume during these periods may adversely affect our growth rate and results. Additionally, the current business environment has generally resulted in advertisers and reseller partners reducing advertising and marketing services budgets or changing such budgets throughout the year, which we expect will impact our quarterly results of operations in addition to the typical seasonality seen in our industry. Our quarterly results will also be impacted by the timing of domain name sales which were recognized as revenue starting in September 2013 with the launch of our Domains Marketplace.

## **Table of Contents**

### **Intellectual Property and Proprietary Rights**

We seek to protect our intellectual property through existing laws and regulations and by contractual restrictions. We rely upon trademark, patent and copyright law, trade secret protection and confidentiality or license agreements with our employees, customers, partners and others to help us protect our intellectual property.

Our technologies involve a combination of proprietary rights, owned and developed by us, commercially available software and hardware elements that are licensed or purchased by us from various providers, including Cisco, Dell, Oracle, Intel, Microsoft, IBM and Veritas, and public domain software, such as Apache, Linux, MySQL, IBM Java and Tomcat. We continue to develop additional technologies to update, supplement and replace existing components of the platform. We intend to protect our proprietary rights through patent and additional intellectual property laws.

Our policy is to apply for patents or for other appropriate intellectual property protection when we develop valuable new or improved technology. We currently own the following pending patent applications and issued patents:

U.S. Patent Number 7,668,950 entitled *Automatically Updating Performance-Based Online Advertising System and Method* was issued February 23, 2010.

U.S. Patent Number 8,442,862 entitled *Method and System for Tracking Telephone Calls* was issued on May 14, 2013 and a corresponding divisional Patent Application Number 13/294,436 was filed November 11, 2011.

U.S. Patent Number 6,822,663 entitled *Transform Rule Generator for Web-Based Markup Languages* was issued November 23, 2004.

U.S. Patent Application Number 12/512,821 entitled *Facility for Reconciliation of Business Records Using Genetic Algorithms* was filed on July 30, 2009.

U.S. Patent Number 8,433,048 entitled *System and Method to Direct Telephone Calls to Advertisers* was issued April 30, 2013.

U.S. Patent Application Number 12/829,373 entitled *System and Method for Calling Advertised Telephone Numbers on a Computing Device* was filed July 1, 2010.

U.S. Patent Number 8,259,915 entitled *System and Method to Analyze Calls to Advertised Telephone Numbers* was issued September 4, 2012 and its continuation Patent Application Number 13/603,283 was filed September 4, 2012.

U.S. Patent Application Number 13/176,709 entitled *Method and System for Automatically Generating Advertising Creatives* was filed July 5, 2011.

U.S. Patent Application Number 12/844,488 entitled *Systems and Methods for Blocking Telephone Calls* was filed on July 27, 2010,

U.S. Patent Number 7,212,615 entitled *Criteria Based Marketing For Telephone Directory Assistance* was issued May 1, 2007 and owned by Jingle Networks, which we acquired in 2011.



## Edgar Filing: MARCHEX INC - Form 10-K

U.S. Patent Number 7,702,084 entitled Toll-Free Directory Assistance With Preferred Advertisement Listing was issued April 20, 2010.

U.S. Patent Number 7,961,861 entitled Telephone Search Supported By Response Location Advertising was issued June 14, 2011 and corresponding European Application Number 5826299.99 was filed November 29, 2005.

U.S. Patent Application Number 11/290,148 entitled Telephone Search Supported By Advertising Based On Past History Of Requests was filed November 29, 2005.

U.S. Patent Application Number 11/291,094 entitled Telephone Search Supported By Keyword Map To Advertising was filed November 29, 2005.

---

**Table of Contents**

U.S. Patent Number 8,175,231 entitled Toll-Free Directory Assistance With Automatic Selection Of An Advertisement From A Category issued May 8, 2012.

U.S. Patent Number 8,107,602 entitled Directory Assistance With Data Processing Station was issued January 31, 2012.

U.S. Patent Application Number 13/677,248 entitled System and Method to Customize a Connection Interface for Multimodal Connection to a Telephone Number was filed November 14, 2012.

U.S. Patent Application Number 13/756,380 entitled Call Tracking System Utilizing an Automated Filtering Function was filed January 31, 2013.

U.S. Patent Application Number 13/756,441 entitled Call Tracking System Utilizing a Pooling Algorithm was filed January 31, 2013.

U.S. Patent Application Number 13/756,480 entitled Call Tracking System Utilizing a Sampling Algorithm was filed January 31, 2013.

U.S. Patent Application Number 13/865,966 entitled Correlated Consumer Telephone Numbers and User Identifiers for Advertising Retargeting was filed April 18, 2013, claiming priority to U.S. Patent Application Number 61/801,893 entitled Cross-Channel Targeting Using Historical Online and Call Data filed March 15, 2013.

U.S. Patent Application Number 13/842,769 entitled System and Method for Analyzing and Classifying Calls without Transcription was filed March 15, 2013.

The status of any patent involves complex legal and factual questions. The scope of allowable claims is often uncertain. As a result, we cannot be sure that: (1) any patent application filed by us will result in a patent being issued; (2) that any patents issued in the future will afford adequate protection against competitors with similar technology; and (3) that the patents issued to us, if any, will not be infringed upon or designed around by others. Furthermore, the performance-based mobile and search advertising industry has been the subject of numerous patents and patent applications, which in turn has resulted in litigation. The mobile advertising industry is also witnessing a significant number of patent related lawsuits. The outcome of this ongoing litigation or any future claims in this sector may adversely affect our business or financial prospects.

We have registered trademarks in the United States for Adhere by Marchex, DPG, Form to Phone, Local Is The New Black, Marchex, Marchex and Design, Marchex Adhere, Marchex Adhere Logo, Marchex Voice Services, Openlist, JingleConnect and Jingle Networks. We also own pending U.S. trademark applications for Archeo, CALL DNA, A Logo, ARCHEO and Design, CALL GENOME, SEARCH GENOME and CLEAN CALL. In addition, we have trademark registrations for Marchex in the following jurisdictions: Australia, Benelux, Brazil, Canada, China, the European Union, Hong Kong, India, Japan, Republic of Korea, Russian Federation and Taiwan.

We do not know whether we will be able to successfully defend our proprietary rights since the validity, enforceability and scope of protection of proprietary rights in Internet-related industries are uncertain and still evolving.

**Regulation**

The manner in which existing laws and regulations should be applied to the Internet and call-based advertising services in general, and how they relate to our businesses in particular, is unclear. A host of federal and state laws covering user privacy, defamation, pricing, advertising, taxation, gambling, sweepstakes, promotions, financial market regulation, quality of products and services, computer trespass, telemarketing, spyware, adware, child protection and intellectual property ownership and infringement are potentially applicable to our business practices and the content offered by our mobile and online distribution partners.

## Edgar Filing: MARCHEX INC - Form 10-K

In addition, our business is impacted by laws in a constant state of flux, and new legislation is introduced on a regular basis. Any such new legislation could expose us to substantial liability, including significant expenses

## **Table of Contents**

necessary to comply with such laws and regulations. Courts may apply each of these laws in unintended and unexpected ways. As a company that provides services over the Internet as well as call recording and call tracking services, we may be subject to an action brought under any of these or future laws.

A number of federal and state laws that could have an impact on our business practices and compliance costs have already been adopted:

The Digital Millennium Copyright Act (DMCA) provides protection from copyright liability for online service providers that list or link to third party web sites. We currently qualify for the safe harbor under the DMCA; however, if it were determined that we did not meet the safe harbor requirements, we could be exposed to copyright infringement litigation, which could be costly and time-consuming.

The Children's Online Privacy Protection Act (COPPA) restricts the online collection of personal information about children and the use of that information. The Federal Trade Commission (FTC) has the authority to impose fines and penalties upon web site operators and online service providers that do not comply with the law's requirements. We do not currently offer any web sites or online services directed to children, nor do we knowingly collect personal information from children.

The Protection of Children from Sexual Predators Act requires online service providers to report evidence of violations of federal child pornography laws under certain circumstances.

The Controlling the Assault of Non-Solicited Pornography and Marketing (CAN-SPAM) Act of 2003 establishes requirements for those who send commercial e-mails, spells out penalties for entities that transmit noncompliant commercial e-mail and/or whose products are advertised in noncompliant commercial e-mail and gives consumers the right to opt-out of receiving commercial e-mails. The majority of the states also have adopted similar statutes governing the transmission of commercial e-mail. The FTC and the states, as applicable, are authorized to enforce the CAN-SPAM Act and the state-specific statutes, respectively. CAN-SPAM gives the Department of Justice the authority to enforce its criminal sanctions. Other federal and state agencies can enforce the law against organizations under their jurisdiction, and companies that provide Internet access may sue violators as well.

The Electronic Communications Privacy Act prevents private entities from disclosing Internet subscriber records and the contents of electronic communications, subject to certain exceptions.

The Computer Fraud and Abuse Act and other federal and state laws protect computer users from unauthorized computer access/hacking, and other actions by third parties which may be viewed as a violation of privacy. Courts may apply each of these laws in unintended and unexpected ways. As a company that provides services over the Internet as well as call recording and call tracking services, we may be subject to an action brought under any of these or future laws.

Among the types of legislation currently being considered at the federal and state levels are consumer laws regulating for the use of certain types of software applications or downloads and the use of cookies. These proposed laws are intended to target specific types of software applications often referred to as spyware, invasiveware or adware, and may also cover certain applications currently used in the online advertising industry to serve and distribute advertisements. In addition, the FTC has sought inquiry regarding the implementation of a do-not-track requirement. Federal legislation is also expected to be introduced that would regulate online behavioral advertising practices. If passed, these laws would impose new obligations for companies that use such software applications or technologies.

The Communications Act of 1934, as amended by the Telecommunications Act of 1996 (the Act), and the regulations promulgated by the Federal Communications Commission under Title II of the Act, may impose federal licensing, reporting and other regulatory

## Edgar Filing: MARCHEX INC - Form 10-K

obligations on the Company. To the extent we contract with and use the networks of voice over IP service providers, new legislation or FCC regulation in this area could restrict our business, prevent us from offering service or increase our cost of doing business. There are an increasing number of regulations and rulings that specifically address access to commerce and communications services on the Internet, including IP telephony. We are unable to

---

**Table of Contents**

predict the impact, if any that future legislation, legal decisions or regulations concerning voice services offered via the Internet may have on our business, financial condition, and results of operations.

The U.S. Congress, the FCC, state legislatures or state agencies may target, among other things, access or settlement charges, imposing taxes related to Internet communications, imposing tariffs or other regulations based on encryption concerns, or the characteristics and quality of products and services that we may offer. Any new laws or regulations concerning these or other areas of our business could restrict our growth or increase our cost of doing business.

The FCC has initiated a proceeding regarding the regulation of broadband services. The increasing growth of the broadband IP telephony market and popularity of broadband IP telephony products and services heighten the risk that the FCC or other legislative bodies will seek to regulate broadband IP telephony and the Internet. In addition, large, established telecommunication companies may devote substantial lobbying efforts to influence the regulation of the broadband IP telephony market, which may be contrary to our interests.

There is risk that a regulatory agency will require us to conform to rules that are unsuitable for IP communications technologies or rules that cannot be complied with due to the nature and efficiencies of IP routing, or are unnecessary or unreasonable in light of the manner in which we offer voice-related services such as call recording and pay-for-call services to our customers.

Federal and state telemarketing laws including the Telephone Consumer Protection Act, the Telemarketing Sales Rule, the Telemarketing Consumer Fraud and Abuse Prevention Act and the rules and regulations promulgated thereunder.

Laws affecting telephone call recording and data protection, such as consent and personal data statutes. Under the federal Wiretap Act, at least one party taking part in a call must be notified if the call is being recorded. Under this law, and most state laws, there is nothing illegal about one of the parties to a telephone call recording the conversation. However, several states (i.e., California, Connecticut, Florida, Illinois, Maryland, Massachusetts, Michigan, Montana, Nevada, New Hampshire, Pennsylvania and Washington) require that all parties consent when one party wants to record a telephone conversation. The telephone recording laws in other states, like federal law, require only one party to be aware of the recording.

The Communications Assistance for Law Enforcement Act may require that the Company undertake material modifications to its platforms and processes to permit wiretapping and other access for law enforcement personnel.

Under various Orders of the Federal Communications Commission, including its Report and Order and Further Notice of Proposed Rulemaking in Docket Number WC 04-36, dated June 27, 2006, the Company may be required to make material retroactive and prospective contributions to funds intended to support Universal Service, Telecommunications Relay Service, Local Number Portability, the North American Numbering Plan and the budget of the Federal Communications Commission.

Laws in most states of the United States of America may require registration or licensing of one or more subsidiaries of the Company, and may impose additional taxes, fees or telecommunications surcharges on the provision of the Company's services which the Company may not be able to pass through to customers.

In addition, there are a large number of federal and state legislative proposals related to our business. It is not possible to predict whether, or when, such legislation might be adopted, and certain proposals, if adopted, could result in a decrease in user registrations and revenue.

We comply with existing law and intend to fully comply with all future laws and regulations that may govern our industry. We have dedicated internal resources and hired outside professionals who regularly establish, review and maintain policies and procedures to reduce the risk of noncompliance. Nevertheless, these



## **Table of Contents**

laws may impose significant additional costs on our business or subject us to additional liability, if we failed to fully comply, even if such failure was unintentional.

The acquisition of Internet domains generally is governed by Internet regulatory bodies, predominantly the Internet Corporation for Assigned Names and Numbers (ICANN). The regulation of Internet domains in the United States and in foreign countries is subject to change. ICANN and other regulatory bodies could establish additional requirements for previously owned Internet domains or modify the requirements for Internet domains. Furthermore, ICANN has and will likely continue to make changes to the scope of domain products available to the marketplace that could have an impact on the competition for premium domain sales.

Compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business in international jurisdictions and could interfere with our ability to offer our products and services to one or more countries or expose us or our employees to fines and penalties. Our continued international expansion also subjects us to increased foreign currency exchange rate risks and will require additional management attention and resources. We cannot assure you that we will be successful in our international expansion.

We post a privacy policy which describes our practices concerning the use and disclosure of any user data collected or submitted via our web sites. Any failure by us to comply with our posted privacy policies, Federal Trade Commission requirements or other federal, state or international privacy or direct marketing laws and regulations could result in governmental or regulatory investigations that could potentially harm our businesses, operational results and overall financial condition.

## **Employees**

As of December 31, 2013, we employed a total of 405 full-time employees. We have never had a work stoppage, and none of our employees are represented by a labor union. We consider our employee relationships to be positive. If we were unable to retain our key employees or we were unable to maintain adequate staffing of qualified employees, particularly during peak sales seasons, our business would be adversely affected.

## **Web site**

Our web site, [www.marchex.com](http://www.marchex.com), provides access, without charge, to our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such materials are electronically filed with the Securities and Exchange Commission. To view these filings, please go to our web site and click on Investor Relations and then click on SEC Filings. Investors and others should note that we announce material financial information to our investors using our investor relations website, press releases, SEC filings, and public conference calls and webcasts. We also use the following social media channels as a means of disclosing information about us, our services, and other matters, and for complying with our disclosure obligations under Regulation FD:

Marchex Twitter Account (<https://twitter.com/marchex>)

Marchex Company Blog (<http://blog.marchex.com/>)

The information we post through these social media channels may be deemed material. Accordingly, investors should monitor the above account and the blog, in addition to following our investor relations website, press releases, SEC filings, and public conference calls and webcasts. This list may be updated from time to time. The information we post through these channels is not a part of this Annual Report on Form 10-K.

## **ITEM 1A. RISK FACTORS**

An investment in our Class B common stock involves various risks, including those mentioned below and those that are discussed from time to time in our other periodic filings with the SEC. Investors should carefully



---

## **Table of Contents**

consider these risks, along with the other information contained in this report, before making an investment decision regarding our stock. There may be additional risks of which we are currently unaware, or which we currently consider immaterial. All of these risks could have a material adverse effect on our business, financial condition, results of operations, and the value of our stock.

### **Risks Relating to Our Company**

#### **We have largely incurred net losses since our inception, and we may incur net losses in the foreseeable future.**

We had an accumulated deficit of \$171.1 million as of December 31, 2013. Our net expenses may increase based on the initiatives we undertake which for instance, may include increasing our sales and marketing activities, hiring additional personnel, incurring additional costs as a result of being a public company, acquiring additional businesses and making additional equity grants to our employees.

#### **We are dependent on certain distribution partners, for distribution of our services, and we derive a significant portion of our total revenue through these distribution partners. A loss of distribution partners or a decrease in revenue from certain distribution partners could adversely affect our business.**

A relatively small number of distribution partners currently deliver a significant percentage of calls and traffic to our advertisers. Our largest distribution partner was paid less than 15% of total revenues for the year ended December 31, 2013. Our existing agreements with many of our other larger distribution partners permit either company to terminate without penalty on short notice and are primarily structured on a variable-payment basis, under which we make payments based on a specified percentage of revenue or based on the number of paid phone calls or click-throughs. We intend to continue devoting resources in support of our larger distribution partners, but there are no guarantees that these relationships will remain in place over the short-or long-term. In addition, we cannot be assured that any of these distribution partners will continue to generate current levels of revenue for us or that we will be able to maintain the applicable variable payment terms at their current levels. A loss of any of these distribution partners or a decrease in revenue due to lower calls and traffic or less favorable variable payment terms from any one of these distribution relationships could have a material adverse effect on our business, financial condition and results of operations.

Companies distributing advertising through mobile or online Internet have experienced, and will likely continue to experience, consolidation. This consolidation has reduced the number of partners that control the mobile and online advertising outlets with the most user calls and traffic. According to the comScore qSearch analysis of the U.S. search marketplace for December 2013, Yahoo! and Microsoft accounted for 11% and 18%, respectively, of the core search market in the United States and Google accounted for 67%. As a result, the larger distribution partners have greater control over determining the market terms of distribution, including placement of call and click-based advertisements and cost of placement. In addition, many participants in the performance-based advertising and search marketing industries control significant portions of mobile and online traffic that they deliver to advertisers. We do not believe, for example, that Yahoo! and Google are as reliant as we are on a third party distribution network to deliver their services. This gives these companies a significant advantage over us in delivering their services, and with a lesser degree of risk.

#### **We rely on certain advertiser reseller partners and agencies, including YP, hibu, Inc., The Cobalt Group, Super Media, Inc., Yodle and Yellow Media, Inc. for the purchase of various advertising and marketing services, as well as to provide us with a large number of advertisers. A loss of certain advertiser reseller partners and agencies or a decrease in revenue from these reseller partners could adversely affect our business. Such advertisers are subject to varying terms and conditions which may result in claims or credit risks to us.**

We benefit from the established relationships and national sales teams that certain of our reseller partners, who are leading reseller partners of advertisers and advertising agencies, have in place throughout the U.S. and

---

**Table of Contents**

international markets. These advertiser reseller partners and agencies refer or bring advertisers to us for the purchase of various advertising products and services. We derive a sizeable portion of our total revenue through these advertiser reseller partners and agencies. Additionally, these advertiser reseller partners and agencies may decide to operate the advertising services we perform internally with their own teams and technology. A loss of certain advertiser reseller partners and agencies or a decrease in revenue from these clients could adversely affect our business. Through our contract with Yellowpages.com LLC d/b/a AT&T Interactive which is a subsidiary of AT&T (collectively, AT&T ), our arrangement with AT&T relates to a business unit that is included in YP Holdings, LLC ( YP ) that AT&T sold a majority stake in to a private equity third party in April 2012. YP is our largest reseller partner and was responsible for 25% of our total revenues for the year ended December 31, 2013 of which the majority is derived from our local leads platform. We cannot predict whether our business with YP in the future will continue at or near current levels and any decrease in such levels could have a material adverse impact on our business and results of operations.

These advertisers may in certain cases be subject to negotiated terms and conditions separate from those applied to online clients accepted and processed through our automated advertiser management platform. In some cases, the applicable contract terms may be the result of legacy or industry association documentation or simply customized advertising solutions for large reseller partners and agencies. In any case, as a consequence of such varying terms and conditions, we may be subject to claims or credit risks that we may otherwise mitigate more efficiently across our automated advertiser management platform.

These claims and risks may vary depending on the nature of the aggregated client base. Among other claims, we may be subject to disputes based on third party tracking information or analysis. We may also be subject to differing credit profiles and risks based on the agency relationship associated with these advertisers. For such advertisers, payment may be made on an invoice basis, unlike our retail platform which in many instances is paid in advance of the service. In some limited circumstances we may also have accepted individual advertiser payment liability in place of liability of the advertising agency or media advisor.

**We received approximately 53% and 61% of our revenue from our five largest customers for the year ended December 31, 2012 and 2013, respectively, and the loss of one or more of these customers could adversely impact our results of operations and financial condition.**

Our five largest customers accounted for approximately 53% and 61% of our total revenues for the years ended December 31, 2012 and 2013, respectively. YP, ADT, and Allstate are our largest customers and were responsible for 25%, 13% and 12% of our total revenues for the year ended December 31, 2013, respectively, and 41%, 14% and 13% of accounts receivable at December 31, 2013, respectively. Most of these customers are not subject to long term contracts with us and are generally able to reduce advertising spending at any time and for any reason. A significant reduction in advertising spending by our largest customers, or the loss of one or more of these customers, if not replaced by new customers or an increase in business from existing customers, would adversely affect revenues. This could have a material adverse effect on our results of operations and financial condition.

**Our large customers have substantial negotiating leverage, which may require that we agree to terms and conditions that may have an adverse effect on our business.**

Our large customers have substantial purchasing power and leverage in negotiating contractual arrangements with us. These customers may seek for us to develop additional features, may require penalties for failure to deliver such features, may seek discounted product or service pricing and may seek more favorable contractual terms. As we sell more products and services to this class of customer, we may be required to agree to such terms and conditions. Such large customers also have substantial leverage in negotiating resolution of any disagreements or disputes that may arise. Any of the foregoing factors could result in a material adverse effect on our business, financial condition and results of operations.

---

**Table of Contents**

**If some of our customers experience financial distress or suffer disruptions in their business, their weakened financial position could negatively affect our own financial position and results.**

We have a diverse customer base and, at any given time, one or more customers may experience financial distress, file for bankruptcy protection, go out of business, or suffer disruptions in their business. If a customer with whom we do a substantial amount of business experiences financial difficulty or suffers disruptions in their business, it could delay or jeopardize the collection of accounts receivable, result in significant reductions in services provided by us and may have a material adverse effect on our results of operations and liquidity.

**We may incur liabilities for the activities of our advertisers, reseller partners, distribution partners and other users of our services, which could adversely affect our business.**

Many of our advertisement generation and distribution processes are automated. In some cases, advertisers or reseller partners use our online tools and account management systems to create and submit advertiser listings and in other cases we create and submit advertising listings on behalf of our advertisers or reseller partners. These advertiser listings are submitted in a bulk data feed or through the distribution partners' user interface. Although we monitor our distribution partners on an ongoing basis primarily for traffic quality, these partners control the distribution of the advertiser listings provided in the data feed or user interface submissions.

We have a large number of distribution partners who display our advertiser listings on their networks. Our advertiser listings are delivered to our distribution partners in an automated fashion through an XML data feed or data dump or through the distribution partners' user interface. Our distribution partners are contractually required to use the listings created by our advertiser customers in accordance with applicable laws and regulations and in conformity with the publication restrictions in our agreements, which are intended to promote the quality and validity of the traffic provided to our advertisers. Nonetheless, we do not operationally control or manage these distribution partners and any breach of these agreements on the part of any distribution partner or its affiliates could result in liability for our business. These agreements include indemnification obligations on the part of our distribution partners, but there is no guarantee that we would be able to collect against offending distribution partners or their affiliates in the event of a claim under these indemnification provisions. Alternatively, we may incur substantial costs as part of our indemnification obligations to distribution partners for liability they may incur as a result of displaying content we have provided them.

We do not conduct a manual editorial review of a substantial number of the advertiser listings directly submitted by advertisers or reseller partners online, nor do we manually review the display of the vast majority of the advertiser listings by our distribution partners submitted to us by XML data feeds or data dumps or the distribution partners' user interface. Likewise, in cases where we provide editorial or value-added services for our large reseller partners or agencies, such as ad creation and optimization for local advertisers or landing pages and micro-sites for pay-for-call customers, we rely on the content and information provided to us by these agents on behalf of their individual advertisers. We do not investigate the individual business activities of these advertisers other than the information provided to us or in some cases review of advertiser web sites. We may not successfully avoid liability for unlawful activities carried out by our advertisers or reseller partners and other users of our services or unpermitted uses of our advertiser listings by distribution partners and their affiliates.

Our potential liability for unlawful activities of our advertisers and other users of our services or unpermitted uses of our advertiser listings and advertising services and platform by distribution partners and reseller partners and agencies could require us to implement measures to reduce our exposure to such liability, which may require us, among other things, to spend substantial resources, to discontinue certain service offerings or to terminate certain distribution partner relationships. For example, as a result of the actions of advertisers in our network, we may be subject to private or governmental actions relating to a wide variety of issues, such as privacy, gambling, promotions, and intellectual property ownership and infringement. Under agreements with certain of our larger distribution partners, we may be required to indemnify these distribution partners against liabilities or losses resulting from the content of our advertiser listings, or resulting from third party intellectual property infringement claims. Although our advertisers agree to indemnify us with respect to claims arising from

## **Table of Contents**

these listings, we may not be able to recover all or any of the liabilities or losses incurred by us as a result of the activities of our advertisers.

Our insurance policies may not provide coverage for liability arising out of activities of users of our services. In addition, our reliance on some content and information provided to us by our large advertiser reseller partners and agencies may expose us to liability not covered by our insurance policies. Furthermore, we may not be able to obtain or maintain adequate insurance coverage to reduce or limit the liabilities associated with our businesses. Any costs incurred as a result of such liability or asserted liability could have a material adverse effect on our business, operating results and financial condition.

**If we do not maintain and grow a critical mass of advertisers and distribution partners, the value of our services could be adversely affected.**

Our success depends, in large part, on the maintenance and growth of a critical mass of advertisers and distribution partners and a continued interest in our pay-for-call, performance-based advertising, call analytics and search marketing services. Advertisers will generally seek the most competitive return on investment from advertising and marketing services. Distribution partners will also seek the most favorable payment terms available in the market. Advertisers and distribution partners may change providers or the volume of business with a provider, unless the product and terms are competitive. In this environment, we must compete to acquire and maintain our network of advertisers and distribution partners. If our business is unable to maintain and grow our base of advertisers, our current distribution partners may be discouraged from continuing to work with us, and this may create obstacles for us to enter into agreements with new distribution partners. Our business also in part depends on certain of our large reseller partners and agencies to grow their base of advertisers as these advertisers become increasingly important to our business and our ability to attract additional distribution partners and opportunities. Similarly, if our distribution network does not grow and does not continue to improve over time, current and prospective advertisers and reseller partners and agencies may reduce or terminate this portion of their business with us. Any decline in the number of advertisers and distribution partners could adversely affect the value of our services.

**The mobile advertising market may develop more slowly than expected, which could harm our business.**

If the market for mobile marketing and advertising develops more slowly than we expect, our business could suffer. Our future success is highly dependent on the commitment of advertisers and marketers to mobile communications as an advertising and marketing medium, the willingness of our potential advertisers to outsource their mobile advertising and marketing needs, and our ability to sell our mobile advertising services to reseller partners and agencies. The mobile advertising and marketing market is relatively new and rapidly evolving. Businesses, including current and potential advertisers, may find mobile advertising or marketing to be less effective than traditional advertising media or marketing methods or other technologies for promoting their products and services. As a result, the future demand and market acceptance for mobile marketing and advertising is uncertain. Many of our current or potential advertisers have little or no experience using mobile communications for advertising or marketing purposes and have allocated only a limited portion of their advertising or marketing budgets to mobile communications advertising or marketing, and there is no certainty that they will allocate more funds in the future, if any. Funds to these types of campaigns may fluctuate greatly as different agencies and advertisers test and refine their overall marketing strategies to include mobile advertising and analytics tools. The adoption rate and budget commitments may vary from period to period as agencies and advertisers determine the appropriate mix of media and lead sources in short term and longer term campaigns.

---

**Table of Contents**

**We are dependent upon the quality of mobile, online, offline and other traffic sources in our network to provide value to our advertisers and the advertisers of our reseller partners, and any failure in our quality control could have a material adverse effect on the value of our services to our advertisers and adversely affect our revenues.**

We utilize certain monitoring processes with respect to the quality of the mobile, online, offline and other traffic sources that we deliver to our advertisers. Among the factors we seek to monitor are sources and causes of low quality phone calls such as unwanted telemarketer calls and clicks such as non-human processes, including robots, spiders or other software, the mechanical automation of clicking, and other types of invalid clicks, click fraud, or click spam, the purpose of which is something other than to view the underlying content. Additionally, we also seek to identify other indicators which may suggest that a user may not be targeted by or desirable to our advertisers. Even with such monitoring in place, there is a risk that a certain amount of low quality mobile, online, offline and other traffic or traffic that is deemed to be less valuable by our advertisers will be delivered to such advertisers, which may be detrimental to those relationships. We have regularly refunded fees that our advertisers had paid to us which were attributed to low quality mobile, online, offline and other traffic. If we are unable to stop or reduce low quality Internet traffic and low quality phone calls, these refunds may increase. Low quality mobile, online, offline and other traffic may further prevent us from growing our base of advertisers and cause us to lose relationships with existing advertisers, or become the target of litigation, both of which would adversely affect our revenues.

**We depend on being able to secure enough phone numbers to support our advertisers and other users of our services and any obstacles that we face which prevent us from meeting this demand could adversely affect our business.**

We utilize phone numbers as part of a number of information and analytic services to advertisers, such as our pay-for-call, call tracking and call analytics services. Our services that utilize phone numbers are designed to enable advertisers and other users of our services to utilize mobile, online and offline advertising and to help measure the effectiveness of mobile, online and offline advertising campaigns. We secure a majority of our phone numbers through telecommunication carriers that we have contracted with and a smaller number through the 800 Service Management System, and such telecommunication carriers provide the underlying telephone service. Our telecommunications carriers and telephone number acquisition process are subject to the rules and guidelines established by the Federal Communications Commission. Furthermore, to the extent we offer call recording and pay-for-call services, we may be directly subject to certain telecommunications-related regulations. The Federal Communications Commission and our telecommunication carriers may change the rules and guidelines for securing phone numbers or change the requirements for retaining the phone numbers we have already secured. As a result, we may not be able to secure or retain sufficient phone numbers needed for our services. We may also be limited in the number of available telecommunications carriers or vendors to provide such phone numbers to us in the event of any industry consolidations.

**Our acquisition of certain automated voice and mobile advertising-based technologies is heavily reliant on vendors.**

Certain voice and mobile advertising-based products that we acquired as part of our acquisition of Jingle are heavily reliant on vendors. The free directory product that we provide relies on technology provided by third party vendors that include voice recognition software and business, government and residence data listings. We cannot guarantee that the technology, data and services provided by our third party vendors will be of sufficient quality to meet the demands of our customers and partners. Further, we cannot guarantee that the technologies, data and services will be available to us in the future on acceptable terms, if at all. Any perception by our customers or partners that our voice and mobile advertising-based products are incomplete or not of sufficient quality could lead to a loss in confidence by our customers or partners, which in turn could lead to a decline in revenues. If we are unable to continue maintaining, advancing and improving our voice and mobile advertising-based products, our operating results may be adversely affected.

---

**Table of Contents**

**We may be subject to intellectual property claims, which could adversely affect our financial condition and ability to use certain critical technologies, divert our resources and management attention from our business operations and create uncertainty about ownership of technology essential to our business.**

Our success depends, in part, on our ability to operate without infringing on the intellectual property rights of others. There can be no guarantee that any of our intellectual property will not be challenged by third parties. We may be subject to patent infringement claims or other intellectual property infringement claims, including claims of trademark infringement in connection with our acquisition of previously-owned Internet domain names and claims of copyright infringement with respect to certain of our proprietary web sites that would be costly to defend and could limit our ability to use certain critical technologies.

The expansion of our call advertising business increases the potential intellectual property infringement claims we may be subject to, particularly in light of the large number of patents which have been issued (or are pending) in the telecommunications field over the last several decades, both in the U.S. and internationally. Jingle, which we acquired in 2011, was subject to patent infringement claims which were unsuccessful at trial. We resolved this matter and obtained a license to the patents at issue.

We believe that a consolidation of patent portfolios by major technology companies and independent asset holding companies will increase the chances of aggressive assertions of patent and other intellectual property claims. Within the technology telecommunications and online sectors, among other related sectors, we have witnessed various claim holders and alleged rights holders pursue business strategies devoted to extracting settlements or license fees for a wide range of basic and commonly accepted methods and practices. We may be subject to those intellectual property claims in the ordinary course of our business. Also, our partners and customers may also find that they are subject to similar claims, in which case we may be included in any related process or dispute settlement.

Any patent or other intellectual property litigation could negatively impact our business by diverting resources and management attention from other aspects of the business and adding uncertainty as to the ownership of technology, services and property that we view as proprietary and essential to our business. In addition, a successful claim of patent infringement against us and our failure or inability to license the infringed or similar technology on reasonable terms, or at all, could prevent us from using critical technologies which could have a material adverse effect on our business.

**We may need additional funding to meet our obligations and to pursue our business strategy. Additional funding may not be available to us and our financial condition could therefore be adversely affected.**

We may require additional funding to meet our ongoing obligations and to pursue our business strategy, which may include the selective acquisition of businesses and technologies. In addition, we have incurred and we may incur certain obligations in the future. There can be no assurance that if we were to need additional funds to meet these obligations that additional financing arrangements would be available in amounts or on terms acceptable to us, if at all. Furthermore, if adequate additional funds are not available, we will be required to delay, reduce the scope of, or eliminate material parts of the implementation of our business strategy, including potential additional acquisitions or internally-developed businesses.

**Our acquisitions could divert management's attention, cause ownership dilution to our stockholders, cause our earnings to decrease and be difficult to integrate.**

Our business strategy includes identifying, structuring, completing and integrating acquisitions. Acquisitions in the technology and Internet sectors involve a high degree of risk. We may also be unable to find a sufficient number of attractive opportunities to meet our objectives which include revenue growth, profitability and competitive market share. Our acquired companies may have histories of net losses and may expect net losses for the foreseeable future. Acquisitions are accompanied by a number of risks that could harm our business, operating results and financial condition:

We could experience a substantial strain on our resources, including time and money, and we may not be successful;

## **Table of Contents**

Our management's attention could be diverted from our ongoing business concerns;

While integrating new companies, we may lose key executives or other employees of these companies;

We may issue shares of our Class B common stock as consideration for acquisitions which may result in ownership dilution to our stockholders;

We could fail to successfully integrate our financial and management controls, technology, reporting systems and procedures, or adequately expand, train and manage our workforce;

We could experience customer dissatisfaction or performance problems with an acquired company or technology;

We could become subject to unknown or underestimated liabilities of an acquired entity or incur unexpected expenses or losses from such acquisitions;

We could incur possible impairment charges related to goodwill or other intangible assets or other unanticipated events or circumstances, any of which could harm our business; and

We may be exposed to investigations and/or audits by federal, state or other taxing authorities.

Consequently, we might not be successful in integrating any acquired businesses, products or technologies, and might not achieve anticipated revenue and cost benefits.

### **Our expanding international operations subject us to additional risks and uncertainties and we may not be successful with our strategy to continue to expand such operations.**

One potential area of growth for us is in international markets. We have initiated operations, through our subsidiaries, in Ireland and the United Kingdom. Our international expansion and the integration of international operations present unique challenges and risks. Compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business in international jurisdictions and could interfere with our ability to offer our products and services to one or more countries or expose us or our employees to fines and penalties. Our continued international expansion also subjects us to increased foreign currency exchange rate risks and will require additional management attention and resources. We cannot assure you that we will be successful in our international expansion. There are risks inherent in conducting business in international markets, including the need to localize our products and services to foreign customers preferences and customs, difficulties in managing operations due to language barriers, distance, staffing and cultural differences, application of foreign laws and regulations to us, tariffs and other trade barriers, fluctuations in currency exchange rates, establishing management systems and infrastructures, reduced protection for intellectual property rights in some countries, changes in foreign political and economic conditions, and potentially adverse tax consequences. Our failure to address these risks adequately could materially and adversely affect our business, revenue, results of operations and financial condition.

### **The loss of our senior management, including our executive officer founders, could harm our current and future operations and prospects.**

We are heavily dependent upon the continued services of Russell C. Horowitz, our chairman and chief executive officer, and the other members of our senior management team. Each member of our senior management team is an at-will employee and may voluntarily terminate his employment with us at any time with minimal notice. Following any termination of employment, each of these employees would only be subject to a twelve-month non-competition and non-solicitation obligation with respect to our customers and employees under our standard confidentiality agreement. Further, as of December 31, 2013, Russell C. Horowitz, Ethan A. Caldwell and Peter Christothoulou, our executive officer founders, together controlled 87% of the combined voting power of our outstanding capital stock. Their collective voting control is not

## Edgar Filing: MARCHEX INC - Form 10-K

ties to their continued employment with Marchex. The loss of the services of any member of our senior management, including our executive officer founders, for any reason, or any conflict among our executive officer founders, could harm our current and future operations and prospects.



---

**Table of Contents**

**We may have difficulty retaining current personnel as well as attracting and retaining additional qualified, experienced, highly skilled personnel, which could adversely affect the implementation of our business plan.**

Our performance is largely dependent upon the talents and efforts of highly skilled individuals. In order to fully implement our business plan, we will need to retain our current qualified personnel, as well as attract and retain additional qualified personnel. Thus, our success will in significant part depend upon our retention of current personnel as well as the efforts of personnel not yet identified and upon our ability to attract and retain highly skilled managerial, engineering, sales and marketing personnel. We are also dependent on managerial and technical personnel to the extent they may have knowledge or information about our businesses and technical systems that may not be known by our other personnel. There can be no assurance that we will be able to attract and retain necessary personnel. The failure to hire and retain such personnel could adversely affect the implementation of our business plan.

**If we are unable to obtain and maintain adequate insurance, our financial condition could be adversely affected in the event of uninsured or inadequately insured loss or damage. Our ability to effectively recruit and retain qualified officers and directors may also be adversely affected if we experience difficulty in maintaining adequate directors and officers liability insurance.**

We may not be able to obtain and maintain insurance policies on terms affordable to us that would adequately insure our business and property against damage, loss or claims by third parties. To the extent our business or property suffers any damages, losses or claims by third parties that are not covered or adequately covered by insurance, our financial condition may be materially adversely affected.

We currently have directors and officers liability insurance. If we are unable to maintain sufficient insurance as a public company to cover liability claims made against our officers and directors, we may not be able to retain or recruit qualified officers and directors to manage our company, which could have a material adverse effect on our operations.

**It may be difficult for us to retain or attract qualified officers and directors, which could adversely affect our business and our ability to maintain the listing of our Class B common stock on the NASDAQ Global Select Market.**

We may be unable to attract and retain qualified officers, directors and members of board committees required to provide for our effective management as a result of changes in the rules and regulations which govern publicly-held companies, including, but not limited to, certifications from executive officers and requirements for financial experts on boards of directors. The perceived increased personal risk associated with these changes may deter qualified individuals from accepting these roles. Further, applicable rules and regulations of the Securities and Exchange Commission and the NASDAQ Stock Market heighten the requirements for board or committee membership, particularly with respect to an individual's independence from the corporation and level of experience in finance and accounting matters. We may have difficulty attracting and retaining directors with the requisite qualifications. If we are unable to attract and retain qualified officers and directors, our business and our ability to maintain the listing of our shares of Class B common stock on the NASDAQ Global Select Market could be adversely affected.

**If we fail to maintain an effective system of internal controls, we may not be able to accurately report our financial results or prevent fraud, which could harm our brand and operating results.**

Effective internal controls are necessary for us to provide reliable and accurate financial reports and effectively prevent fraud. We have devoted significant resources and time to comply with the internal control over financial reporting requirements of the Sarbanes-Oxley Act of 2002. In addition, Section 404 under the Sarbanes-Oxley Act of 2002 requires that we assess and our auditors attest to the effectiveness of our controls

---

**Table of Contents**

over financial reporting. Our current and future compliance with the annual internal control report requirement will depend on the effectiveness of our financial reporting and data systems and controls across our operating subsidiaries. We expect these systems and controls to become increasingly complex to the extent that we integrate acquisitions and our business grows. To effectively manage this growth, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. We cannot be certain that these measures will ensure that we design, implement and maintain adequate controls over our financial processes and reporting in the future. Any failure to implement required new or improved controls, or difficulties encountered in their implementation or operation, could harm our operating results or cause us to fail to meet our financial reporting obligations. Inadequate internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our stock and our access to capital.

**Impairment of goodwill and other intangible assets would result in a decrease in earnings.**

Current accounting rules require that goodwill and other intangible assets with indefinite useful lives be tested for impairment at least annually. These rules also require that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Events and circumstances considered in determining whether the carrying value of amortizable intangible assets and goodwill may not be recoverable include, but are not limited to, significant changes in performance relative to expected operating results, significant changes in the use of the assets, significant negative industry or economic trends, or a significant decline in our stock price and/or market capitalization for a sustained period of time. To the extent such evaluation indicates that the useful lives of intangible assets are different than originally estimated, the amortization period is reduced or extended and, accordingly, the quarterly amortization expense is increased or decreased. To the extent such evaluation indicates that the useful lives of intangible assets are different than originally estimated, the amortization period is reduced or extended and, accordingly, amortization expense is increased or decreased.

We recorded a substantial non-cash impairment charge for goodwill and intangible assets during the fourth quarter of 2008 as a result of the impact of the adverse economic environment including the deterioration in the equity and credit markets. During the fourth quarter of 2012, we recorded a non-cash impairment charge for goodwill of \$15.8 million within the Archeo reporting unit as a result of lower projected revenue growth rates and profitability levels compared to historical results and other market-based factors. We may be required to record a future charge to earnings in our financial statements during the period in which any additional impairment of our goodwill or amortizable intangible assets is determined. Any impairment charges or changes to the estimated amortization periods could have a material adverse effect on our financial results.

**We may be required to increase or decrease the valuation allowance against our deferred tax assets.**

Factors in our ability to realize a tax benefit from our deferred tax assets include tax attributes and operating results of acquired businesses, the nature, extent and periods that temporary differences are expected to reverse and our expectations about future operating results. We regularly review our deferred tax assets to assess whether or not it is more likely than not that the deferred tax assets will be realized, and if necessary, increase or decrease the valuation allowance for portions of such assets to reduce the carrying value. At the end of the fourth quarter of 2012, we recognized a partial valuation allowance of \$16.4 million on our federal deferred tax assets which reduced our net deferred assets to \$28.5 million. At the end of the second quarter of 2013, our gross deferred tax assets increased by approximately \$651,000 due primarily to the 2012 and 2013 research and development credit which was reinstated as part the 2012 American Taxpayer Relief Act signed into law in January 2013. This increase was offset by a corresponding increase in our valuation allowance. If we determine that our deferred tax assets will not result in a future tax benefit, an additional valuation allowance may be recorded with a corresponding charge to net income. Such charges may have a material adverse effect on our results of operations or financial condition. The likelihood of recording such a valuation allowance may be impacted by our acquisitions and increases during periods of economic downturn.

---

## **Table of Contents**

**We may not be able to realize the intended and anticipated benefits from our acquisitions of Internet domain names in part due to our increasing business focus on call advertising products, which could affect the value of these acquisitions to our business and our ability to meet our financial obligations and targets.**

We may not be able to realize the intended and anticipated benefits from our acquisitions of Internet domain names in part due to our increasing focus on call advertising products. These intended and anticipated benefits included increasing our cash flow from operations, broadening our distribution offerings and delivering services that strengthen our advertiser relationships. In addition, our ability to maintain and grow revenues will also depend on maintaining and growing the number of domain name sales and the average revenue per domain. If we are unable to attract prospective buyers to purchase domains and at the price we value the domains, our revenue and results of operations could be materially and adversely affected.

**We do not control the means by which users access our web sites, and material changes to current navigation practices or technologies or marketing practices or significant increases in our marketing costs could result in a material adverse effect on our business.**

The success of our proprietary web site traffic sources depends in large part upon consumer access to our web sites. Consumers access our web sites primarily through the following methods: directly accessing our web sites by typing descriptive keywords or keyword strings into the uniform resource locator (URL) address box of an Internet browser; accessing our web sites by clicking on bookmarked web sites; and accessing our web sites through search engines and directories.

Each of these methods requires the use of a third party product or service, such as an Internet browser or search engine application or directory. Internet browsers may provide alternatives to the URL address box to locate web sites, and search engines may from time to time change and establish rules regarding the indexing and optimization of web sites. We also market certain web sites through search engine applications. Historically, we have limited our search engine marketing to less than five leading search engines.

Product developments and market practices for these means of access to our web sites are not within our control. We may experience a decline in traffic to our web sites if third party browser technologies or search engine methodologies and rules are changed to our disadvantage. We have experienced abrupt search engine algorithm and policy changes in the past. We expect the search engine applications we utilize to market and drive users to our web sites to continue to periodically change their algorithms, policies and technologies. These changes may result in an interruption in user's ability to access our web sites or impair our ability to maintain and grow the number of users who visit our web sites. We may also be forced to significantly increase marketing expenditures in the event that market prices for online advertising and paid-listings escalate. Any of these changes could have a material adverse effect on our business.

**We may experience unforeseen liabilities in connection with our acquisitions of Internet domain names or arising out of third party domain names included in our distribution network, which could negatively impact our financial results.**

Certain of our acquisitions involved the acquisition of a large number of previously-owned Internet domain names. Furthermore, we have separately acquired and may acquire in the future additional previously-owned Internet domain names. In some cases, these acquired names may have trademark significance that is not readily apparent to us or is not identified by us in the bulk purchasing process. As a result we may face demands by third party trademark owners asserting infringement or dilution of their rights and seeking transfer of acquired Internet domain names under the Uniform Domain Name Dispute Resolution Policy administered by ICANN or actions under the U.S. Anti-Cybersquatting Consumer Protection Act. Additionally, we display pay-for-call or pay-per-click listings on third party domain names and third party web sites that are part of our distribution network, which also could subject us to a wide variety of civil claims including intellectual property ownership and infringement.

## **Table of Contents**

We intend to review each claim or demand which may arise from time to time on its merits on a case-by-case basis with the assistance of counsel and we intend to transfer any rights acquired by us to any party that has demonstrated a valid prior right or claim. We cannot, however, guarantee that we will be able to resolve these disputes without litigation. The potential violation of third party intellectual property rights and potential causes of action under consumer protection laws may subject us to unforeseen liabilities including injunctions and judgments for money damages.

**With the recent suspension of our previously announced spin off transaction, we may continue to explore various strategic alternatives for our Archeo assets.**

In November 2012, we announced our intention to pursue the spin-off of our Archeo assets and in September 2013 following a strategic review, we announced the suspension of the planned spin-off of the Archeo assets in its previously announced form. At such time we announced our intention to explore various strategic alternatives for the Archeo assets. Archeo continues to operate as an independent division of the Company. We cannot predict whether Archeo will continue as such within our organization or whether we will pursue another strategic alternative for the Archeo assets going forward. If we do pursue another strategic alternative for the Archeo assets, there can be no assurances such efforts will be successful.

## **Risks Relating to Our Business and Our Industry**

**If we are unable to compete in the highly competitive performance-based advertising and search marketing industries, we may experience reduced demand for our products and services.**

We operate in a highly competitive and changing environment. We principally compete with other companies which offer services in the following areas:

sales to advertisers of pay-for-call services;

sales to advertisers of pay-per-click services;

aggregation or optimization of online advertising for distribution through mobile and online search engines and applications, product shopping engines, directories, web sites or other offline outlets;

provision of local and vertical web sites containing information and user feedback designed to attract users and help consumers make better, more informed local decisions, while providing targeted advertising inventory for advertisers;

delivery of pay-for-call advertising to end users or customers of advertisers through mobile and online destination web sites or other offline distribution outlets;

delivery of online advertising to end users or customers of advertisers through mobile and online destination web sites or other offline distribution outlets;

local search sales training;

services and outsourcing of technologies that allow advertisers to manage their advertising campaigns across multiple networks and track the success of these campaigns;

third party domain monetization;

sales to advertisers of call tracking, call analytics, and presence management services; and

sales to third parties of domain names.

## Table of Contents

Although we currently pursue a strategy that allows us to potentially partner with all relevant companies in the industry, there are certain companies in the industry that may not wish to partner with us. Despite the fact that we currently work with several of our potential competitors, there are no guarantees that these companies will continue to work with us in the future.

We currently or potentially compete with a variety of companies, including Google, Millennial Media, Microsoft, Mongoose Metrics and Telemetrics. Our Archeo Domains Marketplace competitors include Demand Media, Name Media and Oversee.net. Many of these actual or perceived competitors also currently or may in the future have business relationships with us, particularly in distribution. However, such companies may terminate their relationships with us. Furthermore, our competitors may be able to secure agreements with us on more favorable terms, which could reduce the usage of our services, increase the amount payable to our distribution partners, reduce total revenue and thereby have a material adverse effect on our business, operating results and financial condition. We expect competition to intensify in the future because current and new competitors can enter our market with little difficulty. The barriers to entering our market are relatively low. In fact, many current Internet and media companies presently have the technical capabilities and advertiser bases to enter the search marketing services industry. Further, if the consolidation trend continues among the larger media and search engine companies with greater brand recognition, the share of the market remaining for smaller search marketing services providers could decrease, even though the number of smaller providers could continue to increase. These factors could adversely affect our competitive position.

Some of our competitors, as well as potential entrants into our market, may be better positioned to succeed in this market. They may have:

longer operating histories;

more management experience;

an employee base with more extensive experience;

better geographic coverage;

larger customer bases;

greater brand recognition; and

significantly greater financial, marketing and other resources.

Currently, and in the future, as the use of the Internet and other mobile and online services increases, there will likely be larger, more well-established and well-financed entities that acquire companies and/or invest in or form joint ventures in categories or countries of interest to us, all of which could adversely impact our business. Any of these trends could increase competition and reduce the demand for any of our services.

**We face competition from traditional media companies, and we may not be included in the advertising budgets of large advertisers, which could harm our operating results.**

In addition to Internet companies, we face competition from companies that offer traditional media advertising opportunities. Most large advertisers have set advertising budgets, a very small portion of which is allocated to Internet advertising. We expect that large advertisers will continue to focus most of their advertising efforts on traditional media. If we fail to convince these companies to spend a portion of their advertising budgets with us, or if our existing advertisers reduce the amount they spend on our programs, our operating results would be harmed.

**If we are not able to respond to the rapid technological change characteristic of our industry, our products and services may cease to be competitive.**

## Edgar Filing: MARCHEX INC - Form 10-K

The market for our products and services is characterized by rapid change in business models and technological infrastructure, and we will need to constantly adapt to changing markets and technologies to

**Table of Contents**

provide new and competitive products and services. If we are unable to ensure that our users, advertisers, reseller partners, and distribution partners have a high-quality experience with our products and services, then they may become dissatisfied and move to competitors' products and services. Accordingly, our future success will depend, in part, upon our ability to develop and offer competitive products and services for both our target market and for applications in new markets. We may not, however, be able to successfully do so, and our competitors may develop innovations that render our products and services obsolete or uncompetitive.

**Our technical systems are vulnerable to interruption and damage that may be costly and time-consuming to resolve and may harm our business and reputation.**

A disaster could interrupt our services for an indeterminate length of time and severely damage our business, prospects, financial condition and results of operations. Our systems and operations are vulnerable to damage or interruption from:

fire;

floods;

network failure;

hardware failure;

software failure;

power loss;

telecommunications failures;

break-ins;

terrorism, war or sabotage;

computer viruses;

denial of service attacks;

penetration of our network by unauthorized computer users and hackers and other similar events;

natural disasters, including, but not limited to, hurricanes, tornadoes, and earthquakes; and



other unanticipated problems.

We may not have developed or implemented adequate protections or safeguards to overcome any of these events. We also may not have anticipated or addressed many of the potential events that could threaten or undermine our technology network. Any of these occurrences could cause material interruptions or delays in our business, result in the loss of data or render us unable to provide services to our customers. In addition, if a person is able to circumvent our security measures, he or she could destroy or misappropriate valuable information, including sensitive customer information, or disrupt our operations. We have deployed firewall hardware intended to thwart hacker attacks. Although we maintain property insurance and business interruption insurance, our insurance may not be adequate to compensate us for all losses that may occur as a result of a catastrophic system failure or other loss, and our insurers may not be able or may decline to do so for a variety of reasons. If we fail to address these issues in a timely manner, we may lose the confidence of our advertisers, reseller partners, and distribution partners, our revenue may decline and our business could suffer. In addition, as we expand our service offerings and enter into new business areas, we may be required to significantly modify and expand our software and technology platform. If we fail to accomplish these tasks in a timely manner, our business and reputation will likely suffer. Furthermore, some of these events could disrupt the economy and/or our customers business activities and in turn materially affect our operating results.

---

**Table of Contents**

**We rely on third party technology, platforms, carriers, communications providers, and server and hardware providers, and a failure of service by these providers could adversely affect our business and reputation.**

We rely upon third party colocation providers to host our main servers. If these providers are unable to handle current or higher volumes of use, experience any interruption in operations or cease operations for any reason or if we are unable to agree on satisfactory terms for continued hosting relationships, we would be forced to enter into a relationship with other service providers or assume hosting responsibilities ourselves. If we are forced to switch hosting facilities, we may not be successful in finding an alternative service provider on acceptable terms or in hosting the computer servers ourselves. We may also be limited in our remedies against these providers in the event of a failure of service. In the past, we have experienced short-term outages in the service maintained by one of our colocation providers.

We also rely on a select group of third party providers for components of our technology platform and support for our advertising and call-based services, such as hardware and software providers, telecommunications carriers and Voice over Internet Protocol (VoIP) providers, credit card processors and domain name registrars. As a result, key operational resources of our business are concentrated with a limited number of third party providers. A failure or limitation of service or available capacity by any of these third party providers could adversely affect our business and reputation. Furthermore, if any of these significant providers are unable to provide the levels of service and dedicated resources over time that we required in our business, we may not be able to replace certain of these providers in a manner that is efficient, cost-effective or satisfactory to our customers, and as a result our business could be materially and adversely affected. Short term or repeat problems with any of these service providers could provide an interruption of service or service quality impairment to significant customers, which could also impact materially our revenue in any period due to credits or potential loss of significant customers.

**If our security measures are breached or are perceived as not being secure, we may lose advertisers, reseller partners and distribution partners and we may incur significant legal and financial exposure.**

We store and transmit data and information about our advertisers, reseller partners, distribution partners and their respective users. We deploy security measures to protect this data and information, as do third parties we utilize to assist in data and information storage. Our security measures and those of the third parties we partner with to assist in data and information storage may suffer breaches. Security breaches of our data storage systems or our third party colocation and technology providers we utilize to store data and information relating to our advertisers, reseller partners, distribution partners and their respective users could expose us to significant potential liability. In addition, security breaches, actual or perceived, could result in the loss of advertisers, reseller partners and distribution partners that could potentially have an adverse effect on our business.

**We may not be able to protect our intellectual property rights, which could result in our competitors marketing competing products and services utilizing our intellectual property and could adversely affect our competitive position.**

Our success and ability to compete effectively are substantially dependent upon our internally developed and acquired technology and data resources, which we protect through a combination of copyright, trade secret, and patent and trademark law. To date, we have had issued or have applications pending for the following patents:

U.S. Patent Number 7,668,950 entitled *Automatically Updating Performance-Based Online Advertising System and Method* was issued February 23, 2010.

U.S. Patent Number 8,442,862 entitled *Method and System for Tracking Telephone Calls* was issued on May 14, 2013 and a corresponding divisional Patent Application Number 13/294,436 was filed November 11, 2011. The following divisional applications of Patent Application Number 13/294,436

**Table of Contents**

were also filed: 14/045,536 titled *Method and System for Phone Number Cleaning* was filed November 3, 2011; 14/058,037 titled *Method and System for Collecting Data from Advertising Campaigns Including Phone Number Placement Techniques* was filed November 18, 2013; 14/058,080 titled *Method and System for Monitoring Campaign Referral Sources* was filed November 18, 2013, and 14/065,345 titled *Method and System for Tracking Telephone Calls* was filed November 28, 2013.

U.S. Patent Number 6,822,663 entitled *Transform Rule Generator for Web-Based Markup Languages* was issued November 23, 2004.

U.S. Patent Number 8,583,571 entitled *Facility for Reconciliation of Business Records Using Genetic Algorithms* was issued on November 12, 2013.

U.S. Patent Number 8,433,048 entitled *System and Method to Direct Telephone Calls to Advertisers* was issued April 30, 2013.

U.S. Patent Application Number 12/829,373 entitled *System and Method for Calling Advertised Telephone Numbers on a Computing Device* was filed July 1, 2010.

U.S. Patent Number 8,259,915 entitled *System and Method to Analyze Calls to Advertised Telephone Numbers* was issued September 4, 2012 and its continuation Patent Application Number 13/603,283 was filed September 4, 2012.

U.S. Patent Application Number 13/176,709 entitled *Method and System for Automatically Generating Advertising Creatives* was filed July 5, 2011.

U.S. Patent Application Number 12/844,488 entitled *Systems and Methods for Blocking Telephone Calls* was filed on July 27, 2010,

U.S. Patent Number 7,212,615 entitled *Criteria Based Marketing For Telephone Directory Assistance* was issued May 1, 2007 and owned by Jingle Networks, which we acquired in 2011.

U.S. Patent Number 7,702,084 entitled *Toll-Free Directory Assistance With Preferred Advertisement Listing* was issued April 20, 2010.

U.S. Patent Number 7,961,861 entitled *Telephone Search Supported By Response Location Advertising* was issued June 14, 2011 and corresponding European Application Number 5826299.99 was filed November 29, 2005.

U.S. Patent Application Number 11/290,148 entitled *Telephone Search Supported By Advertising Based On Past History Of Requests* was filed November 29, 2005.

U.S. Patent Application Number 11/291,094 entitled *Telephone Search Supported By Keyword Map To Advertising* was filed November 29, 2005.

U.S. Patent Number 8,175,231 entitled *Toll-Free Directory Assistance With Automatic Selection Of An Advertisement From A Category* issued May 8, 2012.

## Edgar Filing: MARCHEX INC - Form 10-K

U.S. Patent Number 8,107,602 entitled Directory Assistance With Data Processing Station was issued January 31, 2012.

U.S. Patent Application Number 13/677,248 entitled System and Method to Customize a Connection Interface for Multimodal Connection to a Telephone Number was filed November 14, 2012.

U.S. Patent Application Number 13/756,380 entitled Call Tracking System Utilizing an Automated Filtering Function was filed January 31, 2013.

U.S. Patent Application Number 13/756,441 entitled Call Tracking System Utilizing a Pooling Algorithm was filed January 31, 2013.

U.S. Patent Application Number 13/756,480 entitled Call Tracking System Utilizing a Sampling Algorithm was filed January 31, 2013.

---

**Table of Contents**

U.S. Patent Application Number 13/865,966 entitled Correlated Consumer Telephone Numbers and User Identifiers for Advertising Retargeting was filed April 18, 2013, claiming priority to U.S. Patent Application Number 61/801,893 entitled Cross-Channel Targeting Using Historical Online and Call Data filed March 15, 2013.

U.S. Patent Application Number 13/842,769 entitled System and Method for Analyzing and Classifying Calls without Transcription was filed March 15, 2013.

U.S. Patent Application Number 14/045,118 entitled System and Method for Analyzing and Classifying Calls Without Transcription via Keyword Spotting was filed October 3, 2013.

In the future, additional patents may be filed with respect to internally developed or acquired technologies. Our industry is highly competitive and many individuals and companies have sought to patent processes in the industry. We may decide not to protect certain intellectual properties or business methods which may later turn out to be significant to us. In addition, the patent process takes several years and involves considerable expense. Further, patent applications and patent positions in our industry are highly uncertain and involve complex legal and factual questions due in part to the number of competing technologies. As a result, we may not be able to successfully prosecute these patents, in whole or in part, or any additional patent filings that we may make in the future. We also depend on our trademarks, trade names and domain names. We may not be able to adequately protect our technology and data resources. In addition, intellectual property laws vary from country to country, and it may be more difficult to protect our intellectual property in some foreign jurisdictions in which we may plan to enter. If we fail to obtain and maintain patent or other intellectual property protection for our technology, our competitors could market competing products and services utilizing our technology.

Despite our efforts to protect our proprietary rights, unauthorized parties domestically and internationally may attempt to copy or otherwise obtain and use our services, technology and other intellectual property. We cannot be certain that the steps we have taken will prevent any misappropriation or confusion among consumers and advertisers. If we are unable to protect our intellectual property rights from unauthorized use, our competitive position could be adversely affected.

**We may be involved in lawsuits to protect or enforce our patents, which could be expensive and time consuming.**

We may initiate patent litigation against third parties to protect or enforce our patent rights, and we may be sued by others seeking to invalidate our patents or prevent the issuance of future patents. We may also become subject to interference proceedings conducted in the patent and trademark offices of various countries to determine the priority of inventions. The defense and prosecution, if necessary, of intellectual property suits, interference proceedings and related legal and administrative proceedings is costly and may divert our technical and management personnel from their normal responsibilities. We may not prevail in any of these suits. An adverse determination of any litigation or defense proceedings could put our patents at risk of being invalidated or interpreted narrowly and could put our patent applications at risk of not being issued. Furthermore, because of the substantial amount of discovery required in connection with intellectual property litigation, there is a risk that some of our confidential information could be compromised by disclosure during this type of litigation. In addition, during the course of this kind of litigation, there could be public announcements of the results of hearings, motions or other interim proceedings or developments in the litigation. If securities analysts or investors perceive these results to be negative, it could have an adverse effect on the trading price of our Class B common stock.

**Our quarterly results of operations might fluctuate due to seasonality, which could adversely affect our growth rate and in turn the market price of our securities.**

Our quarterly results have fluctuated in the past and may fluctuate in the future due to seasonal fluctuations in the level of mobile and Internet usage and seasonal purchasing cycles of many advertisers. Our experience has

---

**Table of Contents**

shown that during the spring and summer months of the year, mobile and Internet usage is lower than during other times of the year and during the latter part of the fourth quarter of the calendar year we generally experience lower call volume and reduced demand for calls. The extent to which usage and call volume may decrease during these off-peak periods is difficult to predict. Prolonged or severe decreases in usage and call volume during these periods may adversely affect our growth rate and in turn the market price of our securities. Additionally, the current business environment has resulted in many advertisers and reseller partners reducing advertising and marketing services budgets or changing such budgets throughout the year, which may impact our quarterly results of operations in addition to typical seasonality seen in our industry. Our quarterly results will also be impacted by the timing of domain name sales which were recognized as revenue starting in September 2013 with the launch of our Domains Marketplace.

**We are susceptible to general economic conditions, and a downturn in advertising and marketing spending by advertisers could adversely affect our operating results.**

Our operating results will be subject to fluctuations based on general economic conditions, in particular those conditions that impact advertiser-consumer transactions. Deterioration in economic conditions could cause decreases in or delays in advertising spending and reduce and/or negatively impact our short term ability to grow our revenues. Further, any decreased collectability of accounts receivable or early termination of agreements due to deterioration in economic conditions could negatively impact our results of operations.

**We depend on the growth of mobile technologies, the Internet and the Internet infrastructure for our future growth and any decrease in growth or anticipated growth in mobile and Internet usage could adversely affect our business prospects.**

Our future revenue and profits, if any, depend upon the continued widespread use of mobile technologies and the Internet as an effective commercial and business medium. Factors which could reduce the widespread use of mobile technologies (including mobile devices, in particular) and the Internet include:

possible disruptions or other damage to the mobile, Internet or telecommunications infrastructure and networks;

failure of the individual networking infrastructures of our advertisers, reseller partners, and distribution partners to alleviate potential overloading and delayed response times;

a decision by advertisers and consumers to spend more of their marketing dollars on offline programs;

increased governmental regulation and taxation; and

actual or perceived lack of security or privacy protection.

In particular, concerns over the security of online transactions and the privacy of users, including the risk of identity theft, may inhibit the growth of Internet usage, including commercial transactions. In order for the mobile and online commerce market to develop successfully, we and other market participants must be able to transmit confidential information, including credit card information, securely over public networks. Any decrease in anticipated mobile and Internet growth and usage could have a material adverse effect on our business prospects.

**We are exposed to risks associated with credit card fraud and credit payment, and we may continue to suffer losses as a result of fraudulent data or payment failure by advertisers.**

We have suffered losses and may continue to suffer losses as a result of payments made with fraudulent credit card data. Our failure to control fraudulent credit card transactions could reduce our net revenue and gross margin and negatively impact our standing with applicable credit card authorization agencies. In addition, under limited circumstances, we extend credit to advertisers who may default on their accounts payable to us or fraudulently charge-back amounts on their credit cards for services that have already been delivered by us.



## **Table of Contents**

### **Regulation of E-Commerce, Online Tracking, Online Data Collection, and Use of the Internet may adversely affect our business and operating results.**

Mobile and online search, e-commerce and related businesses face uncertainty related to new or future government regulation at the federal, state, and international levels regarding e-commerce, online tracking, online data collection, and use of the Internet. Due to the rapid growth and widespread use of the Internet, state and federal legislatures (both domestically and abroad) have enacted and may continue to enact various laws and regulations relating to the Internet. Individual states may also enact consumer protection laws that are more restrictive than the ones that already exist.

Furthermore, the application of existing laws and regulations to companies that engage in e-commerce, or otherwise interact with the Internet remains somewhat unclear. For example, as a result of the actions of advertisers in our network, we may be subject to existing laws and regulations relating to a wide variety of issues such as consumer privacy, gambling, sweepstakes, advertising, promotions, defamation, pricing, taxation, financial market regulation, quality of products and services, computer trespass, spyware, adware, child protection and intellectual property ownership and infringement. In addition, it is not clear whether existing laws that require licenses or permits for certain of our advertisers' lines of business apply to us, including those related to insurance and securities brokerage, law offices and pharmacies. Existing federal and state laws that may affect the growth and profitability of our business include, among others:

The Digital Millennium Copyright Act (DMCA) provides protection from copyright liability for online service providers that list or link to third party web sites. We currently qualify for the safe harbor under the DMCA; however, if it were determined that we did not meet the safe harbor requirements, we could be exposed to copyright infringement litigation, which could be costly and time-consuming.

The Children's Online Privacy Protection Act (COPPA) restricts the online collection of personal information about children and the use of that information. The Federal Trade Commission (FTC) has the authority to impose fines and penalties upon web site operators and online service providers that do not comply with the law. We do not currently offer any web sites or online services directed to children, nor do we knowingly collect personal information from children.

The Protection of Children from Sexual Predators Act requires online service providers to report evidence of violations of federal child pornography laws under certain circumstances.

The Controlling the Assault of Non-Solicited Pornography and Marketing (CAN SPAM) Act of 2003 establishes requirements for those who send commercial e-mails, spells out penalties for entities that transmit noncompliant commercial e-mail and/or whose products are advertised in noncompliant commercial e-mail and gives consumers the right to opt-out of receiving commercial e-mails. The majority of the states also have adopted similar statutes governing the transmission of commercial e-mail. The FTC and the states, as applicable, are authorized to enforce the CAN-SPAM Act and the state-specific statutes, respectively. CAN-SPAM gives the Department of Justice the authority to enforce its criminal sanctions. Other federal and state agencies can enforce the law against organizations under their jurisdiction, and companies that provide Internet access may sue violators as well.

The Electronic Communications Privacy Act prevents private entities from disclosing Internet subscriber records and the contents of electronic communications, subject to certain exceptions.

The Computer Fraud and Abuse Act and other federal and state laws protect computer users from unauthorized computer access/hacking, and other actions by third parties which may be viewed as a violation of privacy. Courts may apply each of these laws in unintended and unexpected ways. As a company that provides services over the Internet as well as call recording and call tracking services, we may be subject to an action brought under any of these or future laws.



## Edgar Filing: MARCHEX INC - Form 10-K

Among the types of legislation currently being considered at the federal and state levels are consumer laws regulating for the use of certain types of software applications or downloads and the use of

---

**Table of Contents**

cookies. These proposed laws are intended to target specific types of software applications often referred to as spyware, invasiveware or adware, and may also cover certain applications currently used in the online advertising industry to serve and distribute advertisements. In addition, the FTC has sought inquiry regarding the implementation of a do-not-track requirement. Federal legislation is also expected to be introduced that would regulate online behavioral advertising practices. If passed, these laws would impose new obligations for companies that use such software applications or technologies. At least one state already has enacted a law, which will go into effect in January 2014, regarding online tracking.

Many Internet services are automated, and companies such as ours may be unknowing conduits for illegal or prohibited materials. It is possible that some courts may impose a strict liability standard or require such companies to monitor their customers' conduct. Although we would not be responsible or involved in any way in such illegal conduct, it is possible that we would somehow be held responsible for the actions of our advertisers or distribution partners.

We may also be subject to costs and liabilities with respect to privacy issues. Several companies have incurred penalties for failing to abide by the representations made in their public-facing privacy policies. In addition, several states have passed laws that require businesses to implement and maintain reasonable security procedures and practices to protect sensitive personal information and to provide notice to consumers in the event of a security breach. Further, it is anticipated that additional federal and state privacy-related legislation will be enacted. Such legislation could negatively affect our business.

In addition, foreign governments may pass laws that could negatively impact our business and/or may prosecute us for violating existing laws. Such laws might include EU member country conforming legislation under applicable EU Privacy, eCommerce, Telecommunications and Data Protection Directives. Any costs incurred in addressing foreign laws could negatively affect the viability of our business. Our exposure to this risk will increase to the extent we expand our operations internationally.

**Federal and state regulation of telecommunications may adversely affect our business and operating results.**

Subsidiaries of the Company provide information and analytics services to certain advertisers and reseller partners that may include information services. In connection therewith, the Company, through its subsidiaries, obtains certain telecommunications products and services from carriers in order to deliver these packages of information and analytic services.

Telecommunications laws and regulations (and interpretations thereof) are evolving in response to rapid changes in the telecommunications industry. If our carrier partners were to be subject to any changes in applicable law or regulation (or interpretations thereof), or additional taxes or surcharges, then we in turn may be subject to increased costs for their products and services or receive products and services that may be of less value to our customers, which in turn could adversely affect our business and operating results. Furthermore, our call recording and pay-for-call services may directly subject us to certain telecommunications-related regulations. Finally, in the event that any federal or state regulators were to expand the scope of applicable laws and regulations or their application to include certain end users and information service providers, then our business and operating results could also be adversely affected. The following existing and possible future federal and state laws could impact the growth and profitability of our business:

The Communications Act of 1934, as amended by the Telecommunications Act of 1996 (the Act), and the regulations promulgated by the Federal Communications Commission under Title II of the Act, may impose federal licensing, reporting and other regulatory obligations on the Company. To the extent we contract with and use the networks of voice over IP service providers, new legislation or FCC regulation in this area could restrict our business, prevent us from offering service or increase our cost of doing

---

**Table of Contents**

business. There are an increasing number of regulations and rulings that specifically address access to commerce and communications services on the Internet, including IP telephony. We are unable to predict the impact, if any, that future legislation, legal decisions or regulations concerning voice services offered via the Internet may have on our business, financial condition, and results of operations.

The U.S. Congress, the FCC, state legislatures or state agencies may target, among other things, access or settlement charges, imposing taxes related to Internet communications, imposing tariffs or other regulations based on encryption concerns, or the characteristics and quality of products and services that we may offer. Any new laws or regulations concerning these or other areas of our business could restrict our growth or increase our cost of doing business.

The FCC has initiated a proceeding regarding the regulation of broadband services. The increasing growth of the broadband IP telephony market and popularity of broadband IP telephony products and services heighten the risk that the FCC or other legislative bodies will seek to regulate broadband IP telephony and the Internet. In addition, large, established telecommunication companies may devote substantial lobbying efforts to influence the regulation of the broadband IP telephony market, which may be contrary to our interests.

There is risk that a regulatory agency will require us to conform to rules that are unsuitable for IP communications technologies or rules that cannot be complied with due to the nature and efficiencies of IP routing, or are unnecessary or unreasonable in light of the manner in which we offer voice-related services such as call recording and pay-for-call services to our customers.

Federal and state telemarketing laws including the Telephone Consumer Protection Act, the Telemarketing Sales Rule, the Telemarketing Consumer Fraud and Abuse Prevention Act and the rules and regulations promulgated thereunder.

Laws affecting telephone call recording and data protection, such as consent and personal data statutes. Under the federal Wiretap Act, at least one party taking part in a call must be notified if the call is being recorded. Under this law, and most state laws, there is nothing illegal about one of the parties to a telephone call recording the conversation. However, several states (i.e., California, Connecticut, Florida, Illinois, Maryland, Massachusetts, Michigan, Montana, Nevada, New Hampshire, Pennsylvania and Washington) require that all parties consent when one party wants to record a telephone conversation. The telephone recording laws in other states, like federal law, require only one party to be aware of the recording. A Wiretap Act violation is a Class D felony; the maximum authorized penalties for a violation of section 2511(1) of the Wiretap Act are imprisonment of not more than five years and a fine under Title 18. Authorized fines are typically not more than \$250,000 for individuals or \$500,000 for an organization, unless there is a substantial loss. State laws impose similar penalties.

The Communications Assistance for Law Enforcement Act may require that the Company undertake material modifications to its platforms and processes to permit wiretapping and other access for law enforcement personnel.

Under various Orders of the Federal Communications Commission, the Company may be required to make material retroactive and prospective contributions to funds intended to support Universal Service, Telecommunications Relay Service, Local Number Portability, the North American Numbering Plan and the budget of the Federal Communications Commission.

Laws in most states of the United States of America may require registration or licensing of one or more subsidiaries of the Company, and may impose additional taxes, fees or telecommunications surcharges on the provision of the Company's services which the Company may not be able to pass through to customers.

## **Table of Contents**

**State and local governments may in the future be permitted to levy additional taxes on Internet access and electronic commerce transactions, which could result in a decrease in the level of usage of our services. In addition, we may be required to pay additional income, sales, or other taxes.**

On November 19, 2004, the federal government passed legislation placing a ban on state and local governments' imposition of new taxes on Internet access or electronic commerce transactions which expires in November 2014. The proposed Marketplace Fairness Act of 2013 if enacted into law would allow states to require online and other out of state merchants to collect and remit sales and use tax on products and services that they may sell. An increase in taxes may make electronic commerce transactions less attractive for advertisers and businesses, which could result in a decrease in the level of usage of our services. Additionally, from time to time, various state, federal and other jurisdictional tax authorities undertake reviews of the Company and the Company's filings. In evaluating the exposure associated with various tax filing positions, the Company on occasion accrues charges for probable exposures. We cannot predict the outcome of any of these reviews.

### **Risks Relating to Ownership of our Common Stock**

**Our Class B common stock prices have been and are likely to continue to be highly volatile.**

The trading prices of our Class B common stock have been and are likely to continue to be highly volatile and subject to wide fluctuations. Since our initial public offering, the closing sale price of our Class B common stock on the NASDAQ Global Select Market ranged from \$3.00 to \$26.14 per share through December 31, 2013. Our stock prices may fluctuate in response to a number of events and factors, which may be the result of our business strategy or events beyond our control, including:

developments concerning proprietary rights, including patents, by us or a competitor;

announcements by us or our competitors of significant contracts, acquisitions, financings, commercial relationships, joint ventures or capital commitments;

registration of additional shares of Class B common stock in connection with acquisitions;

actual or anticipated fluctuations in our operating results;

lawsuits initiated against us or lawsuits initiated by us;

announcements of acquisitions or technical innovations;

potential loss or reduced contributions from distribution partners, reseller partners and agencies, or advertisers;

changes in growth or earnings estimates or recommendations by analysts;

changes in the market valuations of similar companies;

changes in our industry and the overall economic environment;

## Edgar Filing: MARCHEX INC - Form 10-K

volume of shares of Class B common stock available for public sale, including upon conversion of Class A common stock or upon exercise of stock options;

Class B common stock repurchases under our previously announced share repurchase program;

sales and purchases of stock by us or by our stockholders, including sales by certain of our executive officers and directors pursuant to written pre-determined selling and purchase plans under Rule 10b5-1 of the Securities Exchange Act of 1934; and

short sales, hedging and other derivative transactions on shares of our Class B common stock.

In addition, the stock market in general, and the NASDAQ Global Select Market and the market for mobile and online commerce companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of the listed companies. These broad

---

**Table of Contents**

market and industry factors may seriously harm the market price of our Class B common stock, regardless of our operating performance. In the past, following periods of volatility in the market, securities class action litigation has often been instituted against these companies.

Litigation against us, whether or not judgment is entered against us, could result in substantial costs and potentially economic loss, and a diversion of our management's attention and resources, any of which could seriously harm our financial condition. Additionally, there can be no assurance that an active trading market of our Class B common stock will be sustained.

**Our executive officer founders control the outcome of stockholder voting, and there may be an adverse effect on the price of our Class B common stock due to the disparate voting rights of our Class A common stock and our Class B common stock.**

As of December 31, 2013, Russell C. Horowitz, Ethan A. Caldwell and Peter Christothoulou, our executive officer founders, beneficially owned 100% of the outstanding shares of our Class A common stock, which shares represented 86% of the combined voting power of all outstanding shares of our capital stock. These executive officer founders together control 87% of the combined voting power of all outstanding shares of our capital stock. The holders of our Class A common stock and Class B common stock have identical rights except that the holders of our Class B common stock are entitled to one vote per share, while holders of our Class A common stock are entitled to twenty-five votes per share on all matters to be voted on by stockholders. This concentration of control could be disadvantageous to our other stockholders with interests different from those of these executive officer founders. This difference in the voting rights of our Class A common stock and Class B common stock could adversely affect the price of our Class B common stock to the extent that investors or any potential future purchaser of our shares of Class B common stock give greater value to the superior voting rights of our Class A common stock. Further, as long as these executive officer founders have a controlling interest, they will continue to be able to elect all or a majority of our board of directors and generally be able to determine the outcome of all corporate actions requiring stockholder approval. As a result, these executive officer founders will be in a position to continue to control all fundamental matters affecting our company, including any merger involving, sale of substantially all of the assets of, or change in control of, our company. The ability of these executive officer founders to control our company may result in our Class B common stock trading at a price lower than the price at which such stock would trade if these executive officer founders did not have a controlling interest in us. This control may deter or prevent a third party from acquiring us which could adversely affect the market price of our Class B common stock.

**Anti-takeover provisions may limit the ability of another party to acquire us, which could cause our stock price to decline.**

Our certificate of incorporation, as amended, our by-laws and Delaware law contain provisions that could discourage, delay or prevent a third party from acquiring us, even if doing so may be beneficial to our stockholders. In addition, these provisions could limit the price investors would be willing to pay in the future for shares of our Class B common stock. The following are examples of such provisions in our certificate of incorporation, as amended, or our by-laws:

the authorized number of our directors can be changed only by a resolution of our board of directors;

advance notice is required for proposals that can be acted upon at stockholder meetings;

there are limitations on who may call stockholder meetings; and

our board of directors is authorized, without prior stockholder approval, to create and issue blank check preferred stock.

We are also subject to Section 203 of the Delaware General Corporation Law, which provides, subject to enumerated exceptions, that if a person acquires 15% or more of our voting stock, the person is an interested

## **Table of Contents**

stockholder and may not engage in business combinations with us for a period of three years from the time the person acquired 15% or more of our voting stock. The application of Section 203 of the Delaware General Corporation Law could have the effect of delaying or preventing a change of control of our company.

### **We may not be able to continue to pay dividends on our common stock in the future which could impair the value of such stock.**

Under Delaware law, dividends to stockholders may be made only from the surplus of a company, or, in certain situations, from the net profits for the current fiscal year or the fiscal year before which the dividend is declared. We have initiated and paid a quarterly dividend on our common stock since November 2006. We accelerated and paid all four of our 2013 quarterly cash dividends on December 31, 2012. In January 2014, our board of directors declared a quarterly dividend in the amount of \$0.02 per share on our Class A and Class B common stock, which was paid on February 18, 2014 to the holders of record as of the close of business on February 7, 2014. There is no assurance that we will be able to pay dividends in the future. Our ability to pay dividends in the future will depend on our financial results, liquidity and financial condition.

### **We will have broad discretion over the use of the net proceeds from any offering and may not use them effectively.**

Our management may have broad discretion to use the net proceeds of any offering for a variety of purposes, including, further development of our products and operations, working capital and general corporate purposes. We may spend or invest these proceeds in a way with which our stockholders disagree. Failure by our management to effectively use these funds could harm our business and financial condition. Until the net proceeds of any offering are used, they may be placed in investments that do not yield a favorable return to our investors, do not produce significant income or lose value.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS.**

None.

## **ITEM 2. PROPERTIES.**

Our headquarters are located in Seattle, Washington and consist of approximately 61,000 square feet of leased office space expiring in March 2018. We also lease additional office space in Las Vegas, Nevada, and New York, New York with lease terms expiring between April 2014 and March 2018. Our information technology systems are hosted and maintained in third party facilities under collocation services agreements. See Item 1 of this Annual Report on Form 10-K under the caption Information Technology and Systems.

We believe that our existing facilities, together with additional space we believe we can lease at reasonable market rates, are adequate for our near term business needs.

## **ITEM 3. LEGAL PROCEEDINGS.**

We are not a party to any material legal proceedings. From time to time, however, we may be subject to legal proceedings and claims in the ordinary course of business, including claims of alleged infringement of intellectual property rights, and a variety of claims arising in connection with our services.

## **ITEM 4. MINE SAFETY DISCLOSURES.**

Not Applicable.

**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.****Market Information**

Our Class B common stock has been traded on the NASDAQ Global Select Market under the symbol MCHX since March 31, 2004 when we completed our initial public offering at a price of \$6.50 per share. Prior to that time, there was no public market for our Class B common stock. The following table sets forth, for the periods indicated, the high and low closing sales prices for Marchex's Class B common stock as reported on the NASDAQ Global Select Market:

	High	Low
<b>Year ended December 31, 2012</b>		
First Quarter	\$ 6.25	\$ 4.03
Second Quarter	\$ 4.47	\$ 3.19
Third Quarter	\$ 4.26	\$ 3.08
Fourth Quarter	\$ 4.46	\$ 3.64
<b>Year ended December 31, 2013</b>		
First Quarter	\$ 4.41	\$ 3.52
Second Quarter	\$ 6.14	\$ 3.72
Third Quarter	\$ 7.75	\$ 5.87
Fourth Quarter	\$ 9.90	\$ 7.15

**Holdings**

As of February 26, 2014, there were 38,670,309 shares of common stock outstanding that were held by 53 stockholders of record. Of these shares:

7,770,215 shares were issued as Class A common stock, and as of this date were held by 3 stockholders of record; and

30,900,094 shares were issued as Class B common stock, and as of this date were held by 50 stockholders of record.

**Dividends**

In November 2006, we initiated a quarterly cash dividend at \$0.02 per share of Class A common stock and Class B common stock. In August 2012, our board of directors approved an increase to the quarterly cash dividend to Class A and Class B common stockholder from \$0.02 per share to \$0.035 per share. In December 2012, our board of directors declared a quarterly dividend for the first, second, third and fourth quarters of 2013 totaling \$0.14 per share on our Class A common stock and Class B common stock which was paid on December 31, 2012 to holders of record as of the close of business on December 18, 2012. The dividend paid totaled approximately \$5.3 million. In January 2014, our board of directors declared a quarterly dividend in the amount of \$0.02 per share on its Class A and Class B common stock, which was paid on February 18, 2014 to the holders of record as of the close of business on February 7, 2014. This quarterly dividend totaled approximately \$771,000. Although we expect that the annual cash dividend, subject to capital availability, will be \$0.08 per common share or approximately \$3.1 million for the foreseeable future, there can be no assurance that we will continue to pay dividends at such a rate or at all.



**Table of Contents****Issuer Purchases of Equity Securities**

During the fourth quarter of 2013, share repurchase activity was as follows:

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares (or approximate dollar value) that may yet be purchased under the plans or programs <sup>(1)</sup>
<b>Class B Common Shares:</b>				
October 1 - October 31, 2013 <sup>(3)</sup>	7,823	\$ 8.36		1,717,381
November 1 - November 30, 2013 <sup>(3)</sup>	8,206	\$ 9.90		1,717,381
December 1 - December 31, 2013 <sup>(2), (3)</sup>	159,050	\$ 8.58		1,717,381
<b>Total Class B Common Shares</b>	<b>175,079</b>	<b>\$ 8.63</b>		<b>1,717,381</b>

- (1) We have established a share repurchase program which authorizes the Company to repurchase up to 13 million shares in the aggregate (less shares previously repurchased under the share repurchase program) of the Company's Class B common stock. No shares will be knowingly purchased from company insiders or their affiliates. The timing and actual number of shares repurchased will depend on a variety of factors including price, corporate and regulatory requirements, capital availability, and other market conditions. This stock repurchase program does not have an expiration date and may be expanded, limited or terminated at any time without prior notice.
- (2) Includes 6,375 shares of restricted equity subject to vesting which were issued to a certain employees. We repurchased shares which were not already vested for \$0.01 share upon termination of employment.
- (3) Includes 7,823, 8,206, and 152,675 shares of the Company's Class B common stock for the periods October 31, 2013, November 30, 2013 and December 31, 2013, respectively, which were repurchased to satisfy the employees' minimum tax withholding obligations in connection with the vesting of restricted stock awards and was based on the fair market value on the vesting date.

**Table of Contents****Stock Performance Graph**

This performance graph shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the Exchange Act) or otherwise subject to the liabilities under that Section and shall not be deemed to be incorporated by reference into any filing of Marchex under the Securities Act of 1933, as amended or the Exchange Act.

The following graph shows a comparison from December 31, 2008 through December 31, 2013 of cumulative total return for our Class B common stock, the NASDAQ Composite Index (the NASDAQ Composite Index) and the RDG Internet Composite Index (the RDG Index). Measurement points are the last trading day of each of the Company's fiscal years ended December 31, 2008 through 2013. The graph assumes that \$100 was invested on December 31, 2008 in the Class B common stock of the Company, the NASDAQ Composite Index and the RDG Internet Composite Index and assumes reinvestment of any dividends. Such returns are based on historical results and are not intended to suggest future performance.

\*\$100 invested on 12/31/08 in stock or index, including reinvestment of dividends.

Fiscal year ending December 31.

	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
Marchex, Inc.	\$ 100	\$ 88.67	\$ 168.99	\$ 111.80	\$ 78.18	\$ 164.54
NASDAQ Composite Index	\$ 100	\$ 144.88	\$ 170.58	\$ 171.30	\$ 199.99	\$ 283.39
RDG Internet Composite Index	\$ 100	\$ 175.07	\$ 202.22	\$ 209.97	\$ 253.14	\$ 344.69

**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA.**

The following selected consolidated financial data should be read in conjunction with Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes appearing elsewhere in this Form 10-K.

The consolidated financial data for the years ended December 31, 2009 and 2010 is derived from our audited consolidated financial statements which are not included in this Form 10-K.

The consolidated statement of operations data for the years ended December 31, 2011, 2012 and 2013, and the consolidated balance sheet data at December 31, 2012 and 2013, are derived from our audited consolidated financial statements appearing elsewhere in this Form 10-K.

The historical results are not necessarily indicative of the results to be expected in any future period.

**Consolidated Statements of Operations Data (in thousands except per share amounts):**

	Year ended December 31,				
	2009	2010	2011	2012	2013
Revenue	\$ 82,898	\$ 85,828	\$ 138,726	\$ 132,794	\$ 152,550
Income (loss) from operations	\$ (3,619)	\$ (4,548)	\$ 5,724	\$ (17,243)	\$ 2,749
Income (loss) from continuing operations	\$ (2,045)	\$ (3,515)	\$ 2,755	\$ (34,258)	\$ 957
Discontinued operations, net of tax	\$ (17)	\$ 472	\$ 204	\$ (938)	\$ 860
Net income (loss)	\$ (2,062)	\$ (3,043)	\$ 2,959	\$ (35,196)	\$ 1,817
Net income (loss) applicable to common stockholders	\$ (2,249)	\$ (3,242)	\$ 2,700	\$ (35,853)	\$ 1,817
Basic and diluted net income (loss) per Class A share applicable to common stockholders:					
Continuing operations applicable to common stockholders	\$ (0.07)	\$ (0.11)	\$ 0.07	\$ (1.03)	\$ 0.03
Discontinued operations, net of tax	\$ (0.00)	\$ 0.01	\$ 0.01	\$ (0.03)	\$ 0.02
Net income (loss) per Class A share applicable to common stockholders	\$ (0.07)	\$ (0.10)	\$ 0.08	\$ (1.06)	\$ 0.05
Basic and diluted net income (loss) per Class B share applicable to common stockholders:					
Continuing operations applicable to common stockholders	\$ (0.07)	\$ (0.11)	\$ 0.07	\$ (1.02)	\$ 0.03
Discontinued operations, net of tax	\$ (0.00)	\$ 0.01	\$ 0.01	\$ (0.03)	\$ 0.02
Net income (loss) per Class B share applicable to common stockholders	\$ (0.07)	\$ (0.10)	\$ 0.08	\$ (1.05)	\$ 0.05
Shares used to calculate basic net income (loss) per share:					
Class A	10,884	10,661	9,928	9,574	8,816
Class B	22,830	21,993	23,358	24,412	26,798
Shares used to calculate diluted net income (loss) per share:					
Class A	10,884	10,661	9,928	9,574	8,816
Class B	33,714	32,654	35,318	33,986	36,999

**Table of Contents****Consolidated Balance Sheet Data (in thousands), except per share data:**

	<b>December 31,</b>				
	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>
Cash and cash equivalents	\$ 33,638	\$ 37,328	\$ 37,443	\$ 15,930	\$ 30,912
Working capital	\$ 41,273	\$ 47,305	\$ 16,168	\$ 21,683	\$ 39,675
Total assets	\$ 159,373	\$ 159,690	\$ 220,058	\$ 149,147	\$ 162,148
Other non-current liabilities	\$ 1,005	\$ 2,076	\$ 2,580	\$ 2,216	\$ 2,095
Total liabilities	\$ 17,948	\$ 19,998	\$ 61,050	\$ 26,212	\$ 27,393
Total stockholders' equity	\$ 141,425	\$ 139,692	\$ 159,008	\$ 122,935	\$ 134,755
Cash dividends declared per common share	\$ 0.08	\$ 0.08	\$ 0.08	\$ 0.25	\$

---

## **Table of Contents**

### **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

*The following discussion should be read in conjunction with the audited consolidated financial statements and the notes to those statements which appear elsewhere in this Annual Report on Form 10-K. This discussion contains forward-looking statements. Please see page 1 on this Annual Report on Form 10-K Forward-Looking Statements and Item 1A of this Annual Report on Form 10-K under the caption Risk Factors for a discussion of the risks, uncertainties and assumptions associated with these statements.*

#### **Overview**

Marchex is a mobile and call advertising technology company. We provide products and services for businesses of all sizes that depend on consumer calls to drive sales. Our technology platform delivers performance-based, pay-for-call advertising across numerous of mobile and online publishers to connect millions of high-intent consumers with businesses over the phone. Our call analytics technology facilitates call quality, analyzes calls in real time and measures the outcomes of calls to close the loop between digital marketing and offline transactions. We help large national brands and small-and medium-sized businesses (SMBs) facilitate efficient and cost-effective marketing campaigns to drive calls and customer leads to their business. We provide a performance-based pay-per-click advertising service that connects advertisers with consumers across our owned and operated web sites as well as third party web sites and we also sell domain names.

Our technology-based products and services enable our customers to connect with consumers across leading third-party mobile and online channels, as well as our proprietary network of locally-focused web sites. We have direct relationships with large national advertisers and advertising agencies which utilize our products and services to plan, execute and measure their call-focused advertising campaigns. We also provide private-label performance marketing solutions for SMBs through a network of large reseller partners, which include Yellow Pages publishers, media and telecommunications companies and vertical marketing service providers. We enable these partners to sell pay-for-call advertising, call-analytics, search engine marketing and other digital marketing services to their millions of small business customers. We execute these campaigns for them using our technology. Our primary products offerings are:

***Marchex Call Marketplace.*** Through the Marchex Call Marketplace, we deliver a variety of call advertising products and services to national advertisers, advertising agencies and small advertiser reseller partners. The Marchex Call Marketplace is a mobile advertising solution focused on delivering customers on a pay-for-call basis. We offer exclusive and preferred ad placements across numerous mobile and online media sources to drive advertisers qualified calls to their businesses. It leverages our Marchex Call Analytics platform to secure call tracking numbers and to provide qualified calls to advertisers that block spam and other telemarketing calls while working to optimize the return on investment for advertisers' marketing investment.

***Marchex Call Analytics.*** Our Marchex Call Analytics technology platform provides data and insights that measure the performance of mobile, online and offline ad campaigns for advertisers and small business resellers. Our analytics technology tracks calls and helps advertisers understand which marketing channels, advertisements, keywords and creatives are driving calls to their business, allowing them to optimize their advertising expenditures across media channels. Call Analytics also includes call recording, call quality filtering and real-time call intelligence to provide rich insights into what is happening during a call and to measure the outcome of calls and return on investment. Advertisers pay us a fee for each call they receive from call-based ads we distribute through our sources of call distribution or for each phone number tracked based on a pre-negotiated rate.

***Local Leads.*** Our Local Leads platform is a white-labeled, full service advertising solution for small business resellers, such as Yellow Pages providers and vertical marketing service providers, to sell call advertising, search marketing and other lead generation products through their existing sales channels to their small business advertisers. These calls and leads are then fulfilled by us across our distribution

---

**Table of Contents**

network, including mobile sources, and leading search engines. The lead services we offer to small business advertisers through our Local Leads platform include products typically available only to national advertisers, including pay-for-call, search marketing and presence management, ad creation and include advanced features such as call tracking, geo-targeting, campaign management, reporting, and analytics. The Local Leads platform is highly scalable and has the capacity to support hundreds of thousands of advertiser accounts. Reseller partners and publishers generally pay us account fees and agency fees for our products in the form of a percentage of the cost of every click or call delivered to their advertisers.

In addition to our call-driven business, we operate the Archeo Domains Marketplace, which enables the buying, selling and development of premium domain names, and includes more than 200,000 of our owned and operated websites. Our portfolio of websites contains more than 75,000 U.S. ZIP code sites, including 90210.com and covering ZIP code areas nationwide. The Archeo domain marketplace also consists of other locally-focused sites such as Yellow.com, OpenList.com and geo-targeted sites. We monetize this portfolio via pay-per-click and banner advertising and also make these domains available for sale to third parties.

We generate two categories of revenue. Call-driven revenue consists of payments from advertisers for pay-for-call marketing services and for use of our Call Analytics technology. Call-driven revenue also consists of payments from our reseller partners for use of our technology platform and marketing services, which they offer to their small business customers, as well as payments from advertisers for cost-per-action services. Archeo revenue includes revenue generated from advertisements on our network of owned and operated websites and third-party distribution, as well as from the sale of domain names in our domain marketplace. During the years ended December 31, 2011, 2012 and 2013, call-driven revenue accounted for approximately 73%, 84%, and 89% of total revenues, respectively. We operate primarily in domestic markets. For detail on revenue by geographical area for the three most recent fiscal years, see *Note 13. Segment Reporting and Geographic Information* of the notes to our consolidated financial statements.

We were incorporated in Delaware on January 17, 2003. Acquisition initiatives have played an important part in our corporate history to date.

We currently have offices in Seattle, Washington; Las Vegas, Nevada; and New York, New York.

***Acquisition***

On April 7, 2011, we acquired 100% of the stock of Jingle Networks, Inc. ( Jingle ) a provider of mobile voice search performance advertising and technology solutions in North America for the following consideration:

Approximately \$15.8 million in cash, net of cash acquired, and 1,019,103 shares of the Company's Class B common stock paid at closing; plus

Future consideration of (i) \$17.6 million, net of certain working capital adjustments on the first anniversary of the closing, and (ii) \$18.0 million on the 18th month anniversary of closing, with the future consideration payable in either cash or shares of the Company's Class B common stock or some combination to be determined by Marchex. In April 2012 and October 2012, the Company paid approximately \$16.9 million and \$17.9 million in cash, net of certain working capital and other adjustments, respectively.

Following the closing, we issued 462,247 shares of restricted stock at an aggregate value of approximately \$3.3 million to employees of Jingle, subject to vesting for up to four years.

The fair value of the shares of Class B common stock issued as part of the consideration paid was valued at \$7.6 million using the Company's closing stock price of \$7.46 per share at the acquisition date.

## **Table of Contents**

### ***Proposed Separation Update***

On November 1, 2012, we announced that our board of directors had authorized us to pursue the separation of our mobile advertising business focused on calls and Archeo, a domain and click-based advertising business. On September 19, 2013, we announced following a strategic review that it would no longer pursue the separation and that Archeo will continue to operate as a division. We will continue to evaluate various strategic alternatives for the Archeo assets.

### ***Consolidated Statements of Operations***

The assets, liabilities and operations of our acquisitions are included in our consolidated financial statements as of the date of the respective acquisitions.

All significant inter-company transactions and balances within Marchex have been eliminated in consolidation. Our purchase accounting resulted in all assets and liabilities from our acquisitions being recorded at their estimated fair values on the respective acquisition dates. All goodwill, intangible assets and liabilities resulting from the acquisitions have been recorded in our consolidated financial statements.

In the third quarter of 2013, we sold certain assets related to our pay-per-click contextual advertising services in which the operating results have been classified and presented as discontinued operations, net of tax (see *Note 14. Discontinued Operations*) as well as revised our segment reporting to reflect the change in segment performance measures for all periods presented (see *Note 13. Segment Reporting and Geographic Information*).

### ***Presentation of Financial Reporting Periods***

The comparative periods presented are for the years ended December 31, 2011, 2012 and 2013.

### ***Revenue***

We currently generate revenue through our call advertising services, pay-per-click advertising, local leads platform which include our call and click services, proprietary web site traffic and domain name sales through our Domains Marketplace.

Our primary sources of revenue are the performance-based advertising services, which include call advertising, pay-per-click services and cost-per-action services. These primary sources amounted to more than 77% of our revenues in all periods presented. Our secondary sources of revenue are our local leads platform which enables partner resellers to sell call advertising and/or search marketing products, campaign management services, and starting in September 2013, domain name sales through our Domains Marketplace. These secondary sources amounted to less than 23% of our revenues in all periods presented. We have no barter transactions.

On September 10, 2013, we launched our Domains Marketplace, which provides domain names available for sale and initiated plans to facilitate the active buying and transacting of domain names. Domain name sales occurring after this launch have been recognized as revenue in the consolidated financial statements. Historically, the sale of domain names were not a core operation and were peripheral to the generation of advertising revenue from domain names held for use, and as such, domain name sales were reported as gains on sales and disposals of intangible assets, net in the consolidated financial statements.

We recognize revenue upon the completion of our performance obligation, provided that: (1) evidence of an arrangement exists; (2) the arrangement fee is fixed and determinable; and (3) collection is reasonably assured.

---

## **Table of Contents**

In certain cases, we record revenue based on available and reported preliminary information from third parties. Collection on the related receivables may vary from reported information based upon third party refinement of the estimated and reported amounts owing that occurs subsequent to period ends.

### ***Performance-Based Advertising Services***

In providing call advertising services and pay-per-click advertising, we generate revenue upon our delivery of qualified and reported phone calls or click-throughs to our advertisers or advertising service providers' listings. These advertisers and advertising service providers pay us a designated transaction fee for each phone call or click-through, which occurs when a user makes a phone call or clicks on any of their advertisement listings after it has been placed by us or by our distribution partners. Each phone call or click-through on an advertisement listing represents a completed transaction. The advertisement listings are displayed within our distribution network, which includes mobile and online search engines and applications, directories, destination sites, shopping engines, third party Internet domains or web sites, our portfolio of owned web sites, other targeted Web-based content and offline sources. We also generate revenue from cost-per-action services, which occurs when a user makes a phone call from our advertiser's listing or is redirected from one of our web sites or a third party web site in our distribution network to an advertiser web site and completes the specified action.

We generate revenue from reseller partners and publishers utilizing our local leads platform to sell call advertising or, search marketing and other lead generation products. We are paid account fees and also agency fees for our products in the form of a percentage of the cost of every call or click delivered to advertisers. The reseller partners or publishers engage the advertisers and are the primary obligor, and we, in certain instances, are only financially liable to the publishers in our capacity as a collection agency for the amount collected from the advertisers. We recognize revenue for these fees under the net revenue recognition method. In limited arrangements resellers pay us a fee for fulfilling an advertiser's campaign in our distribution network and we act as the primary obligor. We recognize revenue for these fees under the gross revenue recognition method.

In providing pay-per-click contextual targeting services, advertisers purchase keywords or keyword strings, based on an amount they choose for a targeted placement on vertically-focused web sites or specific pages of a web site that are specific to their products or services and their marketing objectives. The contextual results distributed by our services are prioritized for users by the amount the advertiser is willing to pay each time a user clicks on the merchant's advertisement and the relevance of the merchant's advertisement, which is dictated by historical click-through rates. Advertisers pay us when a click-through occurs on their advertisement. In July 2013, we sold certain assets related to our pay-per-click contextual advertising services. The results of operations of these certain pay-per-click assets have been presented in the consolidated financial statements as discontinued operations. See *Note 14. Discontinued Operations* for further discussion.

### ***Search Marketing Services and Domains Name Sales***

Advertisers pay us additional fees for services such as campaign management. Advertisers generally pay us on a click-through basis, although in certain cases we receive a fixed fee for delivery of these services. In some cases we also deliver banner campaigns for select advertisers. We may also charge initial set-up, account, service or inclusion fees as part of our services.

Banner advertising revenue may be based on a fixed fee per click and is generated and recognized on click-through activity. In other cases, banner payment terms are volume-based with revenue generated and recognized when impressions are delivered.

Non-refundable account set-up fees are paid by advertisers and are recognized ratably over the longer of the term of the contract or the average expected advertiser relationship period, which generally ranges from twelve months to more than two years. Other account and service fees are recognized in the month or period the account fee or services relate to.

We generate revenue from domain name sales through our Domains Marketplace. Our Domains Marketplace was launched in September 2013 and provides domain names available for sale and initiated plans to facilitate the buying and transacting of domain names. Domain name sales occurring after the launch date are recognized as revenue.



## **Table of Contents**

### ***Industry and Market Factors***

We enter into agreements with various mobile, online and offline distribution partners to provide distribution for pay-for-call and pay-per-click advertisement listings which contain call tracking numbers and/or URL strings of our advertisers. We generally pay distribution partners based on a percentage of revenue or a fixed amount for each phone call or per click-through on these listings. The level of phone calls and click-throughs contributed by our distribution partners has varied, and we expect it will continue to vary, from quarter to quarter and year to year, sometimes significantly. If we do not add new distribution partners, renew our current distribution partner agreements, replace traffic lost from terminated distribution agreements with other sources or if our distribution partners' search businesses do not grow or are adversely affected, our revenue and results of operations may be materially and adversely affected. Our ability to grow will be impacted by our ability to increase our distribution, which impacts the number of mobile and Internet users who have access to our advertisers' listings and the rate at which our advertisers are able to convert calls and clicks from these mobile and Internet users into completed transactions, such as a purchase or sign up. Our ability to grow also depends on our ability to continue to increase the number of advertisers who use our services and the amount these advertisers spend on our services.

We anticipate that these variables will fluctuate in the future, affecting our ability to grow and our financial results. In particular, it is difficult to project the number of phone calls or click-throughs which will be delivered to our advertisers and how much advertisers will spend with us, and it is even more difficult to anticipate the average revenue per phone call or click-through. It is also difficult to anticipate the impact of worldwide economic conditions on advertising budgets.

In addition, we believe we will experience seasonality. Our quarterly results have fluctuated in the past and may fluctuate in the future due to seasonal fluctuations in levels of mobile and Internet usage and seasonal purchasing cycles of many advertisers. Our experience has shown that during the spring and summer months, mobile and Internet usage is lower than during other times of the year and during the latter part of the fourth quarter of the calendar year we generally experience lower call volume and reduced demand for calls. The extent to which usage and call volume may decrease during these off-peak periods is difficult to predict. Prolonged or severe decreases in usage and call volume during these periods may adversely affect our growth rate and results. Additionally, the current business environment has generally resulted in advertisers and reseller partners reducing advertising and marketing services budgets or changing such budgets throughout the year, which we expect will impact our quarterly results of operations in addition to the typical seasonality seen in our industry. Our quarterly results will also be impacted by the timing of domain name sales which were recognized as revenue starting in September 2013 with the launch of our Domains Marketplace.

### **Service Costs**

Our service costs represent the cost of providing our performance-based advertising services and our search marketing services. The service costs that we have incurred in the periods presented primarily include:

user acquisition costs;

amortization of intangible assets;

license and content fees;

credit card processing fees;

network operations;

serving our search results;

Edgar Filing: MARCHEX INC - Form 10-K

telecommunication costs, including the use of phone numbers relating to our call products and services;

maintaining our web sites;

**Table of Contents**

domain name registration renewal fees;

domain name costs;

network fees;

fees paid to outside service providers;

delivering customer service;

depreciation of our web sites, network equipment and internally developed software;

colocation service charges of our network web site equipment;

bandwidth and software license fees;

payroll and related expenses of related personnel; and

stock-based compensation of related personnel.

***User Acquisition Costs***

For the periods presented the largest component of our service costs consist of user acquisition costs that relate primarily to payments made to distribution partners for access to their mobile, online, offline, or other user traffic. We enter into agreements of varying durations with distribution partners that integrate our services into their web sites and indexes. The primary economic structure of the distribution partner agreements is a variable payment based on a specified percentage of revenue. These variable payments are often subject to minimum payment amounts per phone call or click-through. Other payment structures that to a lesser degree exist include:

fixed payments, based on a guaranteed minimum amount of usage delivered;

variable payments based on a specified metric, such as number of paid phone calls or click-throughs; and

a combination arrangement with both fixed and variable amounts that may be paid in advance.

We expense user acquisition costs based on whether the agreement provides for fixed or variable payments. Agreements with fixed payments with minimum guaranteed amounts of usage are expensed as the greater of the pro-rata amount over the term of arrangement or the actual usage delivered to date based on the contractual revenue share. Agreements with variable payments based on a percentage of revenue, number of paid phone calls, click-throughs or other metrics are expensed as incurred based on the volume of the underlying activity or revenue multiplied by the agreed-upon price or rate.

**Sales and Marketing**

Sales and marketing expenses consist primarily of:

payroll and related expenses for personnel engaged in marketing and sales functions;

advertising and promotional expenditures including online and outside marketing activities;

cost of systems used to sell to and serve advertisers; and

stock-based compensation of related personnel.

**Product Development**

Product development costs consist primarily of expenses incurred in the research and development, creation and enhancement of our web sites and services.

## **Table of Contents**

Our research and development expenses include:

payroll and related expenses for personnel;

costs of computer hardware and software;

costs incurred in developing features and functionality of the services we offer; and

stock-based compensation of related personnel.

For the periods presented, substantially all of our product development expenses are research and development.

Product development costs are expensed as incurred or capitalized into property and equipment in accordance with FASB ASC 350. This statement requires that costs incurred in the preliminary project and post-implementation stages of an internal use software project be expensed as incurred and that certain costs incurred in the application development stage of a project be capitalized.

## **General and Administrative**

General and administrative expenses consist primarily of:

payroll and related expenses for executive and administrative personnel;

professional services, including accounting, legal and insurance;

bad debt provisions;

facilities costs;

other general corporate expenses; and

stock-based compensation of related personnel.

## **Stock-Based Compensation**

We measure stock-based compensation cost at the grant date based on the fair value of the award and recognize it as expense, net of estimated forfeitures, over the vesting or service period, as applicable, of the stock award using the straight-line method. Stock-based compensation expense has been included in the same lines as compensation paid to the same employees in the consolidated statement of operations.

## **Amortization of Intangibles from Acquisitions**

Amortization of intangible assets excluding goodwill relates to intangible assets identified in connection with our acquisitions.

The intangible assets have been identified as:

non-competition agreements;

trademarks and Internet domain names;

distributor relationships;

advertising relationships;

patents; and

acquired technology.

These assets are amortized over useful lives ranging from 12 to 84 months.

---

**Table of Contents**

**Provision for Income Taxes**

We utilize the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred 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 on deferred tax assets and liabilities of a change in tax law is recognized in results of operations in the period that includes the enactment date.

Each reporting period we must assess the likelihood that our deferred tax assets will be recovered from existing deferred tax liabilities or future taxable income, and to the extent that realization is not more likely than not, a valuation allowance must be established. The establishment of a valuation allowance and increases to such an allowance may result in either an increase to income tax expense or reduction of income tax benefit in the statement of operations. Although realization is not assured, we believe it is more likely than not, based on operating performance, existing deferred tax liabilities, projections of future taxable income and tax planning strategies, that our net deferred tax assets, excluding certain state and foreign NOL carryforwards, will be realized. In determining that it was more likely than not that we would realize the deferred tax assets, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions and issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets.

As of December 31, 2013, we have net deferred tax assets of \$26.2 million, relating to the impairment of goodwill, amortization of intangibles assets, certain other temporary differences, acquired federal and state net operating loss carryforwards, and research and development credits. At December 31, 2012 and 2013, we have recorded a valuation allowance of \$21.6 million and \$23.0 million, respectively, against our federal net deferred tax assets as we believe it is more likely than not that these benefits will not be realized. The change in the valuation allowance in 2013 was approximately \$1.4 million due to an increase in our deferred tax assets primarily related to the 2012 and 2013 research and development credit and federal and state NOLs recorded during 2013.

Each reporting period we must assess the likelihood that our deferred tax assets will be recovered from existing deferred tax liabilities or future taxable income, and to the extent that realization is not more likely than not, a valuation allowance must be established. The establishment of a valuation allowance and increases to such an allowance may result in either an increase to income tax expense or reduction of income tax benefit in the statement of operations. Although realization is not assured, we believe it is more likely than not, based on operating performance, existing deferred tax liabilities, projections of future taxable income and tax planning strategies, that our net deferred tax assets, excluding certain state and foreign NOL carryforwards, will be realized. In determining that it was more likely than not that we would realize the deferred tax assets, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions and issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets.

The majority of our deferred tax assets are from goodwill and intangible assets recorded in connection with various acquisitions that are tax-deductible over 15 year periods. Based on projections of future taxable income and tax planning strategies, we expect to be able to recover these assets. The amount of the net deferred tax assets considered realizable, however, may be reduced in the near term if our projections of future taxable income are reduced or if we do not perform at the levels we are projecting. This may result in increases to the valuation allowance for deferred tax assets and may increase income tax expense of up to the entire net amount of deferred tax assets.

As of December 31, 2013, based upon both positive and negative evidence available, we have determined it is not more likely than not that certain deferred tax assets primarily relating to NOL carryforwards in certain

## **Table of Contents**

state, city, and foreign jurisdictions will be realizable and accordingly, have recorded a 100% valuation allowance of \$6.0 million against these deferred tax assets. We do not have a history of taxable income in the relevant jurisdictions and the state and foreign NOL carryforwards will more likely than not expire unutilized. Should we determine in the future that we will be able to realize these deferred tax assets, or not be able to realize all or part of our remaining net deferred tax assets recorded as of December 31, 2013, an adjustment to the net deferred tax assets would impact net income or stockholders' equity in the period such determination was made.

As of December 31, 2012 and 2013, we had certain federal NOL carryforwards of \$1.7 million which will begin to expire in 2019. The Tax Reform Act of 1986 limits the use of NOL and tax credit carryforwards in certain situations where changes occur in the stock ownership of a company. We believe that such a change has occurred, and that approximately \$1.7 million of NOL carryforwards is limited such that substantially all of these federal NOL carryforwards will never be available. Accordingly, we have not recorded a deferred tax asset for these NOL s.

In connection with the Jingle acquisition in 2011, we acquired federal NOL carryforwards. Where there is a change in ownership within the meaning of Section 382 of the Internal Revenue Code, the acquired federal net operating loss carryforwards are subject to an annual limitation. We believe that such an ownership change had occurred at Jingle, and that the utilization of the carryforwards is limited such that the majority of the NOL carryforwards will never be utilized. Accordingly, we have not recorded those amounts we believe it will not be able to utilize and has not included those NOL carryforwards in its deferred tax assets. We recorded NOL carryforwards that may be utilized of approximately \$7.0 million in which \$2.6 million was utilized in 2011.

From time to time, various state, federal, and other jurisdictional tax authorities undertake reviews of us and our filings. We believe any adjustments that may ultimately be required as a result of any of these reviews will not be material to the financial statements.

## **Comparison of the year ended December 31, 2012 (2012) to the year ended December 31, 2013 (2013) and comparison of the year ended December 31, 2011 (2011) to the year ended December 31, 2012 (2012).**

## **Segments**

We have organized our operations into two segments: (1) the Call-driven segment which is comprised of our performance-based advertising business focused on driving phone calls; and (2) the Archeo segment which is comprised of our click-based advertising and Internet domain name businesses. In the third quarter of 2013, we changed our segment reporting to reflect the reallocation of our general corporate overhead expenses to the Call-driven segment to reflect changes in how the CODM internally measures segment performance. The tables below reflect these reclassifications to conform to the current presentation.



**Table of Contents**

In July 2013, we sold certain assets related to Archeo's pay per click advertising services. As a result, the operating results related to these certain pay per click assets are shown as discontinued operations, net of tax in the consolidated statements of operations for all periods presented and are excluded from segment reporting. See *Note. 14 Discontinued Operations* for further discussion.

	Years ended December 31,		
	2011	2012	2013
<b>Call-driven</b>			
Revenue	\$ 101,830	\$ 111,886	\$ 135,126
Operating expenses	97,270	106,795	128,829
Segment profit	\$ 4,560	\$ 5,091	\$ 6,297
<b>Archeo</b>			
Revenue	\$ 36,896	\$ 20,908	\$ 17,424
Operating expenses	22,740	12,582	11,705
Gain on sale of intangible assets, net	9,421	6,296	3,774
Segment profit	\$ 23,577	\$ 14,622	\$ 9,493
Reconciliation of segment profit to net income (loss) from continuing operations before provision for income taxes:			
Total segment profit	\$ 28,137	\$ 19,713	\$ 15,790
Less reconciling items:			
Stock based compensation	15,068	15,638	9,237
Impairment of goodwill		15,837	
Amortization of intangible assets from acquisitions	5,455	4,728	2,926
Acquisition and separation related costs	1,890	753	878
Interest expense and other, net	458	449	37
Net income (loss) from continuing operations before provision for income taxes	\$ 5,266	\$ (17,692)	\$ 2,712

	Years ended December 31,		
	2011	2012	2013
<b>Reconciliation of segment revenue to consolidated revenue</b>			
Call-driven	\$ 101,830	\$ 111,886	\$ 135,126
Archeo	36,896	20,908	17,424
Total	\$ 138,726	\$ 132,794	\$ 152,550

**Revenue.**

The following table presents our revenues, by revenue source, for the periods presented:

	Years ended December 31,		
	2011	2012	2013
Partner and Other Revenue Sources	\$ 118,210	\$ 121,904	\$ 141,617
Proprietary Web Site Traffic Sources and Domain Name Revenue	20,516	10,890	10,933

Edgar Filing: MARCHEX INC - Form 10-K

Total Revenue	\$ 138,726	\$ 132,794	\$ 152,550
---------------	------------	------------	------------

---

**Table of Contents****2012 to 2013**

Our partner network revenues are primarily generated using third party distribution networks to deliver the pay-for-call and pay-per-click advertisers listings. The distribution network includes mobile and online search engine applications, directories, destination sites, shopping engines, third party Internet domains or web sites, other targeted Web-based content, mobile carriers, and offline sources. We generate revenue upon delivery of qualified and reported phone calls or click-throughs to our advertisers or to advertising services providers listings. We pay a revenue share to the distribution partners to access their mobile, online, offline or other user traffic. We also generate revenue from cost-per-action services, which occurs when a user makes a phone call from our advertiser s listing or is redirected from one of our web sites or a third party web site in our distribution network to an advertiser web site and completes the specified action. Other revenues include our call provisioning and call tracking services, presence management services, campaign management services and outsourced search marketing platforms. Our proprietary web site traffic revenues are generated from our portfolio of owned web sites which are monetized with pay-for-call or pay-per-click listings that are relevant to the web sites, as well as other forms of advertising, including banner advertising. When an online user navigates to one of our web sites and calls or clicks on a particular listing or completes the specified action, we receive a fee. We also generate revenue from domain name sales. In September 2013, we launched our Domains Marketplace which provides domain names available for sale and initiated plans to facilitate the buying and transacting of domain names. Domain name sales occurring after this launch are recognized as revenue and totaled \$2.5 million for 2013. The corresponding costs related to domain name sales are recorded under service costs. Prior to this, domain name transactions were recognized within gain/loss on sale and disposal of intangible assets. Total domain name transaction amounts for 2011, 2012 and 2013 prior to our Domains Marketplace launch were \$9.5 million, \$6.3 million, and \$3.8 million, respectively.

Revenue increased 15% from \$132.8 million for 2012 compared to \$152.6 million in 2013. The partner and other revenues increased \$19.7 million primarily from our call advertising services. Our call advertising services revenue increases are primarily due to increases in national advertiser budgets and thousands of additional small business accounts utilizing our call analytics platform. This increase was partially offset by a \$4.2 million decrease in revenue from our pay-per-click services primarily due to fewer advertisers and lower advertiser spend amounts.

Our proprietary web site traffic revenues and Domain Name revenues were \$10.9 million for both 2012 and 2013. Our proprietary web site traffic revenues decreased \$2.5 million and were primarily a result of lower revenues from cost-per-actions from resellers related to our local search and directory web sites and lower revenues from our arrangement with an advertiser service provider whereby we receive payment upon click-throughs on pay-per-click listings presented our web sites. This decrease related to our advertiser service provider was principally due to lower click-throughs on pay-per-click listings presented on our Web sites from the advertiser service provider. These decreases were offset by domain name revenues of \$2.5 million that had no comparable revenue in 2012, although domain name transaction amounts recognized as gain/loss on sale of intangible assets prior to our Domains Marketplace launch, totaled \$6.3 million in 2012 and \$3.8 million in 2013.

Our arrangement with AT&T relates to a business unit that is included in YP Holdings, LLC that AT&T sold a majority stake in to a private equity third party in April 2012. Under our primary arrangement with YP, we generate revenues from our local leads platform to sell call advertising and /or search marketing packages through their existing sales channels, which are then fulfilled by us across our distribution network. We are paid account fees and agency fees for our products in the form of a percentage of the cost of every call or click delivered to their advertisers. In the second quarter of 2010, we signed an extension of our arrangement with YP through June 30, 2015 that includes certain provisions for new advertiser accounts and contemplated the migration of several thousand existing advertiser accounts. In July 2013, we amended our arrangement with YP which lowered certain agency fees beginning July 1, 2013 through the end of the term. We also extended a separate pay-for-call relationship through June 2015. To the extent our revenues from large national advertisers grow at a faster rate than from YP small business accounts, our revenues from YP as a percentage of our total may decrease. Additionally, YP s small business account base from their traditional business has declined, and to

---

**Table of Contents**

the extent declines occur in their business or to the extent YP decreases the number of new advertiser accounts with us, it may result in fewer small business accounts and related revenues on our platform. YP accounted for 32%, 28% and 25% of total revenues during 2011, 2012 and 2013, respectively. Our arrangement with ADT Securities, Inc. ( ADT ) and Allstate Insurance Company ( Allstate ) are for call advertising services which accounted for 13% and 12%, respectively, of total revenues during 2013. Our primary arrangement with Allstate is for pay-for-call services within our Call marketplace for 2014 whereby we charge an agreed-upon price for qualified calls or leads from our network. Allstate's budgeted spend amounts are generally higher in the first half of the year compared to the latter part of the year. There can be no assurance that our business with YP, ADT, and Allstate in the future will continue at or near current levels.

**2011 to 2012**

Revenue decreased 4% from \$138.7 million for 2011 compared to \$132.8 million in 2012. The partner and other revenues increased \$3.7 million due almost entirely to increased revenues from our call advertising services and partially attributable to the April 2011 Jingle acquisition. Our call advertising services revenue increases are primarily due to increase in national advertiser budgets and thousands of additional small business accounts utilizing our call analytics platform. This increase was offset by a \$6.7 million decrease in revenue from our pay-per-click services primarily due to fewer advertisers and lower advertiser spend amounts.

Our proprietary web site traffic revenues decreased \$9.6 million and were primarily due to \$8.0 million in lower revenues for cost-per-actions from resellers related to our local search and directory web sites. The remainder of such decrease was largely due to lower revenues from our arrangement with Google whereby we receive payment upon click-throughs on per-per-click listings presented on our web sites. This decrease was principally due to fewer click-throughs to our web sites. In the near term, we expect modestly lower to similar proprietary web site traffic revenues as a result of modestly lower budgets for cost-per-actions from resellers particularly related to our local search and directory web sites.

Our ability to maintain and grow our revenues will depend in part on maintaining and increasing the number of phone calls and click-throughs performed by users of our service through our distribution partners and proprietary web site traffic sources and maintaining and increasing the number and volume of transactions and favorable variable payment terms with advertisers and advertising services providers, which we believe is dependent in part on marketing our web sites and delivering high quality traffic that ultimately results in purchases or conversions for our advertisers and advertising services providers. We may increase our direct monetization of our proprietary web site traffic sources which may not be at the same rate levels as other advertising providers and could adversely affect our revenues and results of operations. Companies distributing advertising through the Internet and mobile sources have experienced, and will likely to continue experience, consolidation. If we do not add new distribution partners, renew our current distribution partner agreements or replace traffic lost from terminated distribution agreements with other sources or if our distribution partners' businesses do not grow or are adversely affected or our distribution partners adversely impact market terms of distribution, our revenue and results of operations may be materially and adversely affected. If revenue grows and the volume of transactions and traffic increases, we will need to expand our network infrastructure. Inefficiencies in our network infrastructure to scale and adapt to higher traffic volumes could materially and adversely affect our revenue and results of operations. In addition, our ability to maintain and grow revenues will also depend on maintaining and growing the number of domain name sales and the average revenue per domain. If we are unable to attract prospective buyers to purchase domains and at the price we value the domains, our revenue and results of operations could be materially and adversely affected.

We anticipate that these variables will fluctuate in the future, affecting our growth rate and our financial results. In particular, it is difficult to project the number of phone calls and click-throughs we will deliver to our advertisers and how much advertisers will spend with us, and it is even more difficult to anticipate the average revenue per phone call or click-through. With the recognition of domain name sales in revenue, it will be difficult to predict the number of domains that may be sold or the average revenue per domain sale. Domains sold have been through negotiated transactions and it may be difficult to determine the value of a domain to a prospective

**Table of Contents**

buyer. It is also difficult to anticipate the impact of worldwide economic conditions on advertising budgets, including due to the economic uncertainty resulting from periodic disruptions in global financial markets.

In addition, we believe we will experience seasonality with our business. Our quarterly results have fluctuated in the past and may fluctuate in the future due to seasonal fluctuations in levels of mobile and Internet usage and seasonal purchasing cycles of many advertisers. Our experience has shown that during the spring and summer months, mobile and Internet usage is generally lower than during other times of the year and during the latter part of the fourth quarter of the calendar year we generally experience lower call volume and reduced demand for calls. The extent to which usage and call volume may decrease during these off-peak periods is difficult to predict. Prolonged or severe decreases in usage and call volume during these periods may adversely affect our growth rate and results. Additionally, the current business environment has generally resulted in many advertisers and reseller partners reducing advertising and marketing services budgets or changing such budgets throughout the year, which we expect will impact our quarterly results of operations in addition to the typical seasonality seen in our industry. Our quarterly results will also be impacted by the timing of domain name sales which were recognized as revenue starting in September 2013 with the launch our Domains Marketplace.

**Expenses**

Expenses were as follows (in thousands):

	Twelve months ended December 31,					
	2011	% revenue	2012	% revenue	2013	% revenue
Service costs	\$ 75,433	54%	\$ 75,920	57%	\$ 91,858	60%
Sales and marketing	14,389	10%	13,057	10%	11,182	7%
Product development	22,603	17%	23,200	17%	27,346	18%
General and administrative	22,653	17%	22,838	17%	19,385	13%
Amortization of intangible assets from acquisitions	5,455	4%	4,728	4%	2,926	2%
Acquisition and separation related costs	1,890	1%	753	1%	878	1%
	\$ 142,423	103%	\$ 140,496	106%	\$ 153,575	101%

We record stock-based compensation expense under the fair value method. Stock-based compensation expense has been included in the same lines as compensation paid to the same employees in the consolidated statement of operations. Stock-based compensation expense was included in the following operating expense categories as follows (in thousands):

	Twelve months ended December 31,		
	2011	2012	2013
Service costs	\$ 1,289	\$ 1,869	\$ 1,180
Sales and marketing	1,471	2,029	645
Product development	1,408	1,038	1,635
General and administrative	10,900	10,702	5,777
Total stock-based compensation	\$ 15,068	\$ 15,638	\$ 9,237

See Note 6 (b). *Stock Option Plan* of the consolidated financial statements as well as our Critical Accounting Policies for additional information about stock-based compensation.

*Service Costs.* Service costs increased 21%, from \$75.9 million in 2012 to \$91.9 million in 2013. The increase was primarily attributable to an increase in distribution partner payments and personnel costs totaling \$17.1 million, partially offset by a decrease in communication and network costs and stock-based compensation.



---

**Table of Contents**

Service costs increased 1%, from \$75.4 million in 2011 to \$75.9 million in 2012. The increase was primarily attributable to an increase in distribution partner payments, communication and network costs and stock-based compensation totaling \$2.6 million and to a lesser extent as a result of the April 2011 Jingle acquisition, partially offset by a decrease in personnel costs, Internet domain amortization, depreciation, facility costs, travel and fees paid to outside service providers.

Service costs represented 60% of revenue in 2013 compared to 57% in 2012 and 54% in 2011. The 2013 increase as a percentage of revenue in service costs compared to 2012 was primarily a result of higher distribution partner payments. The 2012 increase as a percentage of revenue in service costs compared to 2011 was primarily a result of our proprietary web site traffic revenues comprising a lower proportion of revenue compared to 2011. Proprietary web site traffic revenues have a lower service cost as a percentage of revenue relative to our overall service cost percentage.

We expect that user acquisition costs and revenue shares to distribution partners are likely to increase prospectively given the competitive landscape for distribution partners. To the extent that payments to pay-for-call, pay-per-click or cost-per-action distribution partners make up a larger percentage of future operations, or the addition or renewal of existing distribution partner agreements are on terms less favorable to us, we expect that service costs will increase as a percentage of revenue. To the extent of revenue declines in these areas, we expect revenue shares to distribution partners to decrease in absolute dollars. Our proprietary web site traffic revenues have a lower service cost as a percentage of revenue relative to our overall service cost percentage. Our proprietary web site traffic revenues have no corresponding distribution partner payments. To the extent our proprietary web site traffic revenues make up a larger percentage of our future operations, we expect that service costs will decrease as a percentage of revenue. We expect with an increase in the proportion of partner and other revenue sources and additional investment in our network, service costs will increase as a percentage of revenue in the near term. We also expect that in the longer term service costs will increase in absolute dollars as a result of costs associated with the expansion of our operations and network infrastructure as we scale and adapt to increases in the volume of transactions, calls and traffic and invest in our platforms.

*Sales and Marketing.* Sales and marketing expenses decreased 14% from \$13.1 million in 2012 to \$11.2 million in 2013. As a percentage of revenue, sales and marketing expenses were 10% and 7% for 2012 and 2013, respectively. The net decrease in dollars and percentage of revenue were primarily a result of a decrease in stock based compensation related to the acceleration of certain restricted shares as part of a separation agreement in 2012, online and outside marketing activities, and facility costs totaling \$2.3 million offset partially by an increase in personnel costs and depreciation. We expect some volatility in sales and marketing expenses based on the timing of marketing initiatives but expect sales and marketing expenses in the near term to be relatively stable to modestly higher in absolute dollars. We expect that sales and marketing expenses will increase in connection with any revenue increase to the extent that we also increase our marketing activities and correspondingly could increase as a percentage of revenue.

Sales and marketing expenses decreased 9% from \$14.4 million in 2011 to \$13.1 million in 2012. As a percentage of revenue, sales and marketing expenses were 10% for both 2011 and 2012. The net decrease in dollars was related primarily to decreases in personnel and online and outside marketing activities totaling \$2.1 million partially offset by an increase in depreciation and stock-based compensation related to the acceleration of certain restricted shares as part of a separation agreement totaling \$915,000.

*Product Development.* Product development expenses increased 18% from \$23.2 million in 2012 to \$27.3 million in 2013. The net increase in dollars was primarily due to an increase in personnel costs, stock based compensation and fees paid to outside service providers. As a percentage of revenue, product development expenses were 17% and 18% for 2012 and 2013, respectively. The 2013 percentage of revenue was relatively consistent with 2012 percentage of revenue. We expect product development expenditures in the near term to be modestly higher in absolute dollars. In the longer term, we expect that product development expenses will increase in absolute dollars as we increase the number of personnel and consultants to enhance our service offerings and as a result of additional stock-based compensation expense.

---

**Table of Contents**

Product development expenses increased 3% from \$22.6 million in 2011 to \$23.2 million in 2012. The increase in dollars was primarily due to an increase in personnel costs, travel costs and depreciation totaling \$934,000 partly related to the April 2011 Jingle acquisition. This increase was partially offset primarily by a decrease in stock-based compensation. As a percentage of revenue, product development expenses were 17% for both 2011 and 2012.

*General and Administrative.* General and administrative expenses decreased 15%, from \$22.8 million in 2012 to \$19.4 million in 2013. The net decrease was primarily due to decrease in stock based compensation of \$4.9 million offset primarily by an increase in personnel costs, professional fees, bad debt and other operating expenses. As a percentage of revenue, general and administrative expenses were 17% and 13% for 2012 and 2013, respectively, The decrease in percentage of revenue was primarily as a result of a decrease in stock based compensation and higher revenues compared to 2012.

We expect our general and administrative expenses to be relatively stable or modestly higher in the near term. We expect that our general and administrative expenses will increase in the longer term to the extent that we expand our operations and incur additional costs in connection with being a public company, including expenses related to professional fees and insurance, and as a result of stock-based compensation expense. We also expect fluctuations in our general and administrative expenses to the extent the recognition timing of stock-based compensation is impacted by market conditions relating to our stock price.

General and administrative expenses increased 1%, from \$22.7 million in 2011 to \$22.8 million in 2012. General and administrative expenses remained relatively stable compared to 2011. As a percentage of revenue, general and administrative expenses were 17% for both 2011 and 2012.

*Segment Profit.* Call-driven segment profit increased 24% from \$5.1 million in 2012 to \$6.3 million in 2013. The increase in profit was due to higher revenues in 2013 as a result of increases in national advertiser budgets and thousands of additional small business accounts utilizing our call analytics platform and operating expenses as a percentage of revenue remaining similar to 2012.

Call-driven segment profit increased 12% from \$4.6 million in 2011 to \$5.1 million in 2012. The increase in profit was due to higher revenues in 2012 and operating expenses as a percentage of revenue remaining similar to 2011.

Archeo segment profit decreased 35% from \$14.6 million in 2012 to \$9.5 million in 2013. The decrease was primarily due to lower revenues in our pay-per-click services and proprietary web site traffic sources as a result of decreased revenues for cost-per-actions from resellers related to our local search and directory web sites. In September 2013, we launched our Domains Marketplace which provides domain names available for sale and initiated plans to facilitate the buying and transacting of domain names. Domain name sales occurring after this launch are recognized as revenue with corresponding costs under service costs. Prior to the launch, domain name transactions were recognized within gain/loss on sale and disposal of intangible assets. Total contribution from domain name sales included in revenue and corresponding service costs and gain/loss on sale and disposal of intangible assets was \$6.3 million in both periods.

Archeo segment profit decreased 38% from \$23.6 million in 2011 to \$14.6 million in 2012. The decrease was primarily related to \$8.0 million in lower revenues from cost-per-actions from resellers related to our local search and directory web sites and \$8.3 million in lower revenues from our pay-per-click services primarily due to fewer advertisers and lower advertiser spend amounts. The decrease in profit was also attributable to a \$3.1 million decrease in gain on sales and disposals of intangible assets, net related to domain sales. This decrease was offset by lower operating expenses.

*Amortization of Intangible Assets from Acquisitions.* Intangible amortization expense decreased from \$4.7 million in 2012 to \$2.9 million in 2013. The decrease was primarily associated with certain intangible assets related to the April 2011 Jingle acquisition being fully amortized. During 2013, the amortization of intangibles related to service costs and sales and marketing expenses.



---

**Table of Contents**

Intangible amortization expense decreased from \$5.5 million in 2011 to \$4.7 million in 2012. The decrease was associated with certain intangible assets acquired in the Jingle acquisition in April 2011 and other acquisitions prior to 2011 being fully amortized. During 2012, the amortization of intangibles related to service costs, sales and marketing and general and administrative expenses.

Our purchase accounting resulted in all assets and liabilities from our acquisitions being recorded at their estimated fair values on their respective acquisition dates. All goodwill, identifiable intangible assets and liabilities resulting from our acquisitions have been recorded in our financial statements. We may acquire identifiable intangible assets as part of future acquisitions, and if so, we expect that our intangible amortization will increase in absolute dollars.

Events and circumstances considered in determining whether the carrying value of amortizable intangible assets and goodwill may not be recoverable include, but are not limited to: significant changes in performance relative to expected operating results; significant changes in the use of the assets; significant negative industry or economic trends; or a significant decline in our stock price and/or market capitalization for a sustained period of time. If our stock price were to trade below the book value per share for an extended period of time and/or we experience changes in our business, including changes in projected earnings and cash flows, we may have to recognize an impairment of all or some portion of goodwill.

No impairment of our intangible assets have been identified in 2013. The current business environment is subject to evolving market conditions and requires significant management judgment to interpret the potential impact to our assumptions. To the extent that changes in the current business environment impact our ability to achieve levels of forecasted operating results and cash flows, or should other events occur indicating the remaining carrying value of our assets might be impaired, we would test its intangible assets for impairment and may recognize an additional impairment loss to the extent that the carrying amount exceeds such asset's fair value.

*Acquisition and separation related costs.* Acquisition and separation related costs of \$878,000 in 2013 were primarily for professional fees and other procedures associated with our proposed separation of our business into two distinct publicly traded companies. We are no longer pursuing a separation of our business and do not expect any significant additional costs.

Acquisition and separation related costs of \$753,000 in 2012 were primarily for professional fees and other procedures associated with our proposed separation of our business into two distinct publicly traded companies partially offset by a \$132,000 benefit recorded in the first quarter of 2012 related a revision in our original estimates regarding the future obligation related to the Jingle office space.

Acquisition and separation related costs in 2011 of \$1.9 million were primarily for professional fees to perform due diligence, historical audits in connection with regulatory filings and other procedures associated with our acquisition of Jingle in April 2011. Of the \$1.9 million of acquisition related costs, we recognized approximately \$372,000 for the future obligations of non-cancelable lease and other costs related to the Jingle office. The portion related to the non-cancelable lease is based on estimates of vacancy period and sublease income. The actual vacancy periods may differ from these estimates, and sublease income, if any, may not materialize. Accordingly, these estimates may be adjusted in future periods.

*Impairment of goodwill.* We perform our annual impairment testing in accordance with the Accounting Standards Codification 350, *Intangibles Goodwill and Other* on November 30. No impairment has been identified in 2013. In 2012, we recorded a \$15.8 million non-cash impairment charge on goodwill within the Archeo reporting unit, net of \$902,000 classified to discontinued operations as part of the sale of certain pay per click assets in July 2013. During the fourth quarter of 2012, we announced our intention to pursue a spin-off of Archeo and the corresponding organizational changes, resulted in a change to our reporting units for purposes of assessing potential impairment of goodwill. The estimated fair value of the Archeo reporting unit was based on

---

**Table of Contents**

the estimates of future operating results, discounted cash flows and other market-based factors. The goodwill impairment recorded within the Archeo reporting unit resulted from the newly associated amounts of goodwill allocated upon the commencement of the reporting unit designation in the fourth quarter of 2012, and the operating results including lower projected revenue growth rates and profitability levels compared to historical results.

*Gain on sales and disposals of intangible assets, net.* The gain on sales and disposals of intangible assets, net was \$6.3 million in 2012 compared to \$3.8 million in 2013 and was attributable to the sales and disposals of Internet domain names and other intangible assets. The decrease was primarily due to recognition of domain name sales in revenue after the launch of our Domains Marketplace in September 2013. Domains Marketplace provides domain names available for sale and facilitates the buying and transacting of domain names. During 2013, approximately \$2.5 million of domain name sales were recognized as revenue after the launch date and future domain name sales will be recognized as revenue.

The gain on sales and disposals of intangible assets, net was \$9.4 million and \$6.3 million in 2011 and 2012, respectively. The decrease was primarily due to fewer domains sold in 2012 compared to 2011.

*Other income (expense), net.* Other income (expense), net were (\$449,000) and (\$37,000) in 2012 and 2013, respectively. The net decrease in other income (expense), net during 2013 was primarily due to the Jingle deferred acquisition consideration paid in 2012 which resulted in no interest accretion in 2013.

Other income (expense), net were (\$458,000) and (\$449,000) in 2011 and 2012, respectively. The net decrease in other income (expense), net during 2012 was primarily due to a decrease in accretion of interest expense related to the deferred acquisition consideration for the Jingle acquisition offset by a decrease in other income.

*Income Taxes.* The income tax expense in 2013 was \$1.8 million. In 2013, the effective tax rate of 65% differed from the expected effective tax rate of 34% due to state income taxes, non-deductible stock-based compensation related to incentive stock options recorded under the fair-value method, federal research and development credits, increase in valuation allowance and other non-deductible amounts. We recognized approximately \$851,000 of federal research and experimental credits related to 2012 and 2013 during 2013 due to the reinstatement of the federal research and development credit in January 2013 as part of the 2012 American Taxpayer Relief Act. This resulted in an increase in our gross deferred tax assets which was offset by an increase to our valuation allowance of \$651,000 in 2013.

The income tax expense in 2012 was \$16.6 million. In 2012, the effective tax rate of (94%) differed from the expected effective tax rate of 34% due primarily to establishment of a partial valuation allowance on our federal deferred tax assets, non-deductible goodwill impairment and other items such as state income taxes, non-deductible stock-based compensation related to incentive stock options recorded under the fair-value method, non-cash accretion of interest expense, and other non-deductible amounts. At the end of the fourth quarter of 2012, we recognized a partial valuation allowance of \$16.4 million on our federal deferred tax assets. In assessing whether it is more likely than not that our deferred tax assets will be realized, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions, issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets.

The income tax expense in 2011 was \$2.5 million. In 2011, the effective tax rate of 48% differed from the expected effective tax rate of 35% due to state income taxes, non-deductible stock-based compensation related to incentive stock options recorded under the fair-value method, acquisition related costs related to the Jingle acquisition, non-cash accretion of interest expense, and other non-deductible amounts.

**Table of Contents**

During 2011, 2012 and 2013, we recognized excess tax benefits (shortfalls) on stock option exercises, restricted stock vesting, and dividends paid on unvested restricted stock of approximately \$913,000, (\$4.0) million and (\$76,000), respectively, which were recorded to additional paid in capital.

*Discontinued Operations, net of tax.* In July 2013, we sold certain assets related to Archeo's pay per click advertising services. As a result, the operating results related to these certain pay per click assets are shown as discontinued operations. See *Note. 14. Discontinued Operations* for further discussion. Discontinued operations, net of tax in 2011, 2012, and 2013 was an income \$204,000, a loss of (\$938,000) which includes a goodwill impairment of \$902,000, and an income of \$860,000 which includes \$930,000 in gain on sale, net of tax from the sale of certain pay-per-click assets, respectively. The decrease in income from 2011 to 2012 was due primarily to lower revenues each year as a result of fewer advertisers and lower advertiser spend amounts as well as the goodwill impairment in 2012. The increase from 2012 to 2013 was primarily due to the recognition of the gain on sale in 2013.

*Net Income (Loss).* Net loss was \$35.2 million in 2012 compared to net income of \$1.8 million in 2013. The increase in net income in 2013 was primarily a result of non-cash charges related to goodwill impairment and valuation allowance totaling \$33.1 million in 2012, a decrease in stock based compensation and amortization of acquired intangible assets, and an increase in revenue offset by an increase in operating expenses.

Net income was \$3.0 million in 2011 compared to a net loss of \$35.2 million in 2012. The decrease was primarily attributable to the non-cash charges related to the goodwill impairment and valuation allowance totaling \$33.1 and a decrease in revenues and gain on sales and disposals of intangible assets, net partially offset by a decrease in operating expenses.

**Table of Contents****Quarterly Results of Operations (Unaudited)**

The following tables set forth our unaudited quarterly results of operations data for the eight most recent quarters ended December 31, 2013. The information in the tables below should be read in conjunction with our consolidated financial statements and the notes thereto included elsewhere in this report. We have prepared this information on the same basis as the consolidated financial statements and the information includes all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair statement of our financial position and operating results for the quarters or other periods presented. Our quarterly operating results have varied substantially in the past and may vary substantially in the future. You should not draw any conclusions about our future results from the results of operations for any particular quarter or period presented.

(in thousands)	Quarter Ended							
	Mar 31, 2012	June 30, 2012	Sept 30, 2012	Dec 31, 2012	Mar 31, 2013	June 30, 2013	Sept 30, 2013	Dec 31, 2013
<b>Consolidated Statement of Operations:</b>								
Revenue	\$ 33,835	\$ 32,832	\$ 33,691	\$ 32,436	\$ 34,732	\$ 37,578	\$ 40,560	\$ 39,680
Expenses:								
Service costs <sup>(1)</sup>	18,757	18,320	19,744	19,099	20,148	22,584	25,293	23,833
Sales and marketing <sup>(1)</sup>	3,611	4,341	2,542	2,563	2,644	2,905	2,801	2,832
Product development <sup>(1)</sup>	5,977	5,750	5,510	5,963	6,808	6,945	6,833	6,760
General and administrative <sup>(1)</sup>	6,164	5,439	5,678	5,557	4,797	5,527	4,679	4,382
Acquisition and separation related costs	(132)		296	589	345	309	286	(62)
Amortization of intangible assets from acquisitions <sup>(2)</sup>	1,537	1,082	1,055	1,054	1,055	736	709	426
Total operating expenses	35,914	34,932	34,825	34,825	35,797	39,006	40,601	38,171
Impairment of goodwill				(15,837)				
Gain on sales and disposals of intangible assets, net	1,463	3,258	713	862	1,362	1,330	1,047	35
Income (loss) from operations	(616)	1,158	(421)	(17,364)	297	(98)	1,006	1,544
Other income (expense):								
Interest income	3	3	3	5	3	7	3	2
Interest and line of credit expense	(197)	(111)	(111)	(19)	(19)	(19)	(20)	(18)
Other	(3)	(6)	(10)	(6)	(1)		(2)	27
Total other income (expense)	(197)	(114)	(118)	(20)	(17)	(12)	(19)	11
Income (loss) from continuing operations before provision for income taxes	(813)	1,044	(539)	(17,384)	280	(110)	987	1,555
Income tax expense (benefit)	(88)	595	(49)	16,108	165	243	389	958
Net income (loss) from continuing operations	(725)	449	(490)	(33,492)	115	(353)	598	597
Discontinued operations, net of tax	10	(52)	(53)	(843)	(31)		883	8
Net income (loss)	(715)	397	(543)	(34,335)	84	(353)	1,481	605
Dividends paid to participating securities	(73)	(67)	(123)	(394)				
Net income (loss) applicable to common stockholders	\$ (788)	\$ 330	\$ (666)	\$ (34,729)	\$ 84	\$ (353)	\$ 1,481	\$ 605

<sup>(1)</sup> Excludes amortization of intangible assets from acquisitions. Certain reclassifications have been made to prior periods to conform to current period presentation.

## Edgar Filing: MARCHEX INC - Form 10-K

(2) Components of amortization of intangible assets from acquisitions:

Service costs	\$ 1,216	\$ 774	\$ 748	\$ 747	\$ 748	\$ 429	\$ 402	\$ 402
Sales and marketing	307	307	307	307	307	307	307	24
General and administrative	14	1						
Total	\$ 1,537	\$ 1,082	\$ 1,055	\$ 1,054	\$ 1,055	\$ 736	\$ 709	\$ 426

Certain reclassifications have been made to prior periods to conform to current period presentation.

Due to rounding, the sum of quarterly amounts may not equal amounts reported for year-to-date periods.

---

## Table of Contents

### **Liquidity and Capital Resources**

As of December 31, 2012 and 2013, we had cash and cash equivalents of \$15.9 million and \$30.9 million, respectively. As of December 31, 2013, we had current and long term contractual obligations of \$5.4 million and \$9.7 million for rent under our facility operating leases.

Cash provided by operating activities primarily consists of a net income (loss) adjusted for certain non-cash items such as amortization and depreciation, deferred income taxes, stock-based compensation, excess tax benefit related to stock-based compensation, acquisition and separation related costs, accretion of interest, gain on sale of intangible assets, net, gain on sale of discontinued operations, impairment of goodwill and changes in working capital.

Cash provided by operating activities for the year ended December 31, 2013 of approximately \$13.6 million consisted primarily of net income of \$1.8 million adjusted for non-cash items of \$19.6 million, including depreciation, amortization of intangible assets, allowance for doubtful accounts and advertiser credits, stock-based compensation, and deferred income taxes, \$1.5 million of gain on sale of discontinued operations, \$3.8 million gain on sales and disposals of intangible and fixed assets, net and \$2.5 million provided by working capital and other activities.

In July 2013, we sold certain assets related to our pay-per-click services to an unrelated third party. These assets contributed approximately of \$3.2 million of revenue and \$111,000 in operating loss during 2013. We expect the divestiture of these assets will not have a significant impact on working capital and cash generated from operations. See *Note 14. Discontinued Operations* for further discussion.

Cash provided by operating activities for the year ended December 31, 2012 of approximately \$19.9 million consisted primarily of net loss of \$35.2 million adjusted for non-cash items of \$59.2 million, including depreciation, amortization of intangible assets, allowance for doubtful accounts and advertiser credits, stock-based compensation, acquisition related costs, accretion of interest, excess tax benefit related to stock-based compensation, deferred income taxes that includes a \$16.4 million valuation allowance, and impairment of goodwill, gain on sales and disposals of intangible and fixed assets, net of \$6.3 million and \$2.2 million provided by working capital and other activities. Included in the working capital amount is \$881,000 of interest accretion paid as part of the 12-month and 18-month deferred acquisition payments made in April and October 2012, respectively.

With respect to a significant portion of our pay-for call and pay-per-click advertising services, the amount payable to the distribution partners will be calculated at the end of a calendar month, with a payment period following the delivery of the phone calls or click-throughs. These services constituted the majority of revenue in 2011, 2012 and 2013. We generally receive payment from advertisers in close proximity to the timing of the corresponding payments to the distribution partners who provide placement for the listings. In certain cases, payments to distribution partners are paid in advance or are fixed in advance based on a guaranteed minimum amount of usage delivered. We have no corresponding payments to distribution partners related to our proprietary web site traffic revenues.

Nearly all of the reseller partner arrangements are billed on a monthly basis following the month of our phone call or click-through delivery. This payment structure results in our advancement of monies to the distribution partners who have provided the corresponding placements of the listings. For these services, reseller partner payments are generally received two to four weeks following payment to the distribution partners. We expect that in the future periods, if the amounts from our reseller partner arrangements account for a greater percentage of our operating activity, working capital requirements will increase as a result.

We have payment arrangements with reseller partners particularly related to our proprietary web site traffic sources or our local leads and call analytics services, such as YP, SuperMedia Inc., hibu, The Cobalt Group, and Yellow Media Inc., whereby we receive payment between 30 and 60 days following the delivery of services. For the year and as of December 31, 2013 amounts from these partners totaled 41% of revenue and \$15.9 million in

---

**Table of Contents**

accounts receivable. Based on the timing of payments, we generally have this level of amounts in outstanding accounts receivable at any given time from these partners. Our arrangement with AT&T relates to its business unit YP that AT&T sold a majority stake in to a private equity third party in April 2012. In July 2013, we amended our arrangement with YP which lowered certain agency fees beginning July 1, 2013 through the end of the term. We also extended a separate pay-for-call relationship through June 2015. We do not expect the modifications in these agreements to significantly impact our operating results. There can be no assurance that our business with YP in the future will continue at or near current levels. Net accounts receivable balances outstanding at December 31, 2013 from YP totaled \$12.4 million. For the year and as of December 31, 2013 amounts from these partners along with ADT and Allstate totaled 66% of revenue and \$23.8 million in net receivables. There can be no assurances that these partners or other advertisers will not experience financial difficulty, curtail operations, reduce or eliminate spend budgets, delay payments or otherwise forfeit balances owed.

There can be no assurances that these partners or other advertisers will not experience further financial difficulty, curtail operations, reduce or eliminate spend budgets, delay payments or otherwise forfeit balances owed.

In September 2013, we launched our Domains Marketplace which provides domain names available for sale and facilitates the buying and transacting of domain names. Approximately \$2.5 million of domain name sales were recognized as revenue after the launch date and future domain name sales will be recognized as revenue and included in operating activities.

Cash provided by investing activities for the year ended December 31, 2013 of approximately \$1.6 million was primarily attributable to purchases for property and equipment of \$3.0 million, which were more than offset by proceeds from the sales of intangible assets of approximately \$3.8 million and proceeds from sale of discontinued operations of \$1.1 million. Cash provided by investing activities may decrease given the proceeds from sales of intangible assets which comprises domain names is recognized in operating activities with the launch in September 2013 of our Domains Marketplace. Cash used in investing activities for the year ended December 31, 2012 of approximately \$3.3 million was primarily attributable to purchases for property and equipment of \$2.9 million, which were more than offset by proceeds from the sales of intangible assets of approximately \$6.3 million. Cash used in investing activities for the year ended December 31, 2011 of approximately \$10.4 million was primarily attributable to the cash paid at closing of \$15.8 million related to the Jingle acquisition, and purchases for property and equipment of \$4.0 million, which were partially offset by proceeds from the sales of intangible assets of approximately \$9.5 million. In April 2011, we acquired Jingle in which \$15.8 million, net of cash acquired, was paid at closing. The acquisition included deferred acquisition payments, net of certain working capital and other adjustments, totaling \$33.9 million, which were paid in cash in 2012 and are shown as financing activities.

We expect property and equipment purchases will increase as we continue to invest in equipment and software. To the extent our operations increase, we expect to increase expenditures for our systems and personnel. We expect our expenditures for product development initiatives and internally developed software will increase in the longer term in absolute dollars as our development activities accelerate and we increase the number of personnel and consultants to enhance our service offerings.

Cash used in financing activities for the year ended December 31, 2013 was \$261,000 and was primarily comprised of tax withholding payment of approximately \$3.2 million related to certain executive vested restricted stock awards partially offset by proceeds from exercises of stock options of \$2.9 million. Cash used in financing activities for the year ended December 31, 2012 of approximately \$44.7 million was primarily attributable to the cash payments of the 12-month and 18-month deferred acquisition payments related to the April 2011 Jingle acquisition totaling \$33.9 million, which is net of certain working capital and other adjustments. The deferred acquisition payments exclude the interest accretion of \$881,000 that is shown as an operating cash outflow. Other financing activities include the repurchase of 387,000 shares of Class B common stock for treasury stock totaling approximately \$1.7 million and common stock dividend payments of \$9.4

**Table of Contents**

million, partially offset by net proceeds of approximately \$71,000 from the sale of stock through employee stock options and employee stock plan purchases and \$308,000 from excess tax benefit related to stock-based compensation. The dividend payments in 2012 include the December 2012 board of directors' declaration of quarterly dividends for the first, second, third, and fourth quarters of 2013 totaling \$5.3 million, which was paid on December 31, 2012. Cash used in financing activities for the year ended December 31, 2011 of approximately \$6.3 million was primarily attributable to the repurchase of 883,000 shares of Class B common stock for treasury stock totaling approximately \$6.2 million and common stock dividend payments of \$2.9 million, partially offset by net proceeds of approximately \$1.8 million from the sale of stock through employee stock options and employee stock plan purchases and \$1.0 million from excess tax benefit related to stock-based compensation.

The following table summarizes our contractual obligations as of December 31, 2013, and the effect these obligations are expected to have on our liquidity and cash flows in future periods.

In thousands	Total	Less than 1 year	1-3 years	4-5 years	thereafter
<b>Contractual Obligations:</b>					
Operating leases	\$ 9,689	\$ 2,287	\$ 4,492	\$ 2,910	\$
Other contractual obligations	5,458	3,170	2,288		
Total contractual obligations <sup>(1), (2)</sup>	\$ 15,147	\$ 5,457	\$ 6,780	\$ 2,910	\$

(1) In February 2005 we entered into a license agreement with an advertising partner which provides for a contingent royalty based on a discounted rate of 3% (3.75% under certain circumstances) of certain of our gross revenues payable on a quarterly basis through December 2016. The royalty payment is recognized as incurred in service costs and is not included in the above schedule.

(2) Our tax contingencies of approximately \$534,000 are not included due to their uncertainty.

We anticipate that we will need to invest working capital towards the development and expansion of our overall operations. We may also make a significant number of acquisitions, which could result in the reduction of our cash balances or the incurrence of debt. Furthermore, we expect that capital expenditures may increase in future periods, particularly if our operating activity increases.

On April 1, 2008, we entered into a three year credit agreement which provides us with a \$30 million senior secured revolving credit line, which may be used for various corporate purposes including financing permitted acquisitions, subject to compliance with applicable covenants. During the first quarter of 2011, we signed an amendment to the credit agreement which extended the maturity period through to April 1, 2014. During the first quarter of 2014, we signed an amendment to the credit agreement which extended the maturity period through April 1, 2017. As of December 31, 2013, we had \$30 million of availability under the credit agreement.

In November 2006, our board of directors authorized a share repurchase program to repurchase up to 3 million shares of our Class B common stock as well as the initiation of a quarterly cash dividend for the holders of the Class A common stock and Class B common stock. Our board of directors authorized have increases in the share repurchase program to provide for the repurchase of up to 13 million shares in the aggregate (less shares previously purchased under the share repurchase program) of our Class B common stock. Under the share repurchase program, repurchases may take place in the open market and in privately negotiated transactions and at times and in such amounts as we deem appropriate. The timing and actual number of shares repurchased will depend on a variety of factors including price, corporate and regulatory requirements, capital availability, and other market conditions. This share repurchase program does not have an expiration date and may be expanded, limited or terminated at any time without prior notice. During the years ended December 31, 2011, 2012 and 2013, approximately 883,000, 387,000 and 31,000 shares of Class B common stock, respectively, were repurchased under the share purchase program.

The quarterly cash dividend was initiated at \$0.02 per share of Class A common stock and Class B common stock. For 2011, quarterly dividends were paid on February 15, May 16, August 15 and November 15 to Class A and Class B common stockholders of record as of the close of business of February 4, May 6, August 5 and



---

**Table of Contents**

November 5, respectively. Total dividends paid in 2011 were approximately \$2.9 million. For 2012, quarterly dividends were paid on February 15, May 16, August 15, and November 15 to Class A and Class B common stockholders of record as of the close of business of February 4, May 6, August 5 and November 5, respectively and included two additional dividend payments on August 31 and December 31 to holders of record as of the close of business of August 16 and December 18, respectively. In August 2012, the Company's board of directors approved an increase to the Company's quarterly cash dividend on the Company's Class A and Class B common stock, subject to capital availability, from \$0.02 per share to \$0.035 per share. The increase in the dividend raised the annual dividend rate to \$0.14 per share or \$5.3 million. The Company paid the incremental \$0.015 per share dividends totaling \$566,000 on August 31, 2012 to Class A and Class B common stockholders of record as of the close of business on August 16, 2012. In December 2012, the Company's board of directors declared a quarterly dividend for the first, second, third and fourth quarters of 2013 totaling \$0.14 per share on its Class A common stock and Class B common stock, which was paid on December 31, 2012 to the holders of record as of the close of business on December 18, 2012. The dividend paid totaled \$5.3 million. Total dividends paid in 2012 were approximately \$9.4 million, which includes the 2013 dividends accelerated into 2012.

In January 2014, our board of directors declared a quarterly dividend in the amount of \$0.02 per share on its Class A and Class B common stock, which was paid on February 18, 2014 to the holders of record as of the close of business on February 7, 2014. This quarterly dividend totaled approximately \$771,000. Although we expect that the annual cash dividend, subject to capital availability, will be \$0.08 per common share or approximately \$3.1 million for the foreseeable future, there can be no assurance that we will continue to pay dividends at such a rate or at all.

On December 16, 2013 and January 7, 2014, we filed a Registration Statement on Form S-3 (File No. 333-192891) and Amendment, respectively, to sell, from time to time, up to \$50 million of our Class B common stock. We will also sell up to 3.5 million shares of Class B common stock on behalf of selling shareholders in which we will not receive proceeds.

Based on our operating plans we believe that our existing credit availability, resources and cash flow provided by ongoing operations, will be sufficient to fund our operations for at least twelve months. Additional equity and debt financing may be needed to support our acquisition strategy, our long-term obligations and our company's needs. If additional financing is necessary, it may not be available; and if it is available, it may not be possible for us to obtain financing on satisfactory terms. Failure to generate sufficient revenue or raise additional capital could have a material adverse effect on our ability to continue as a going concern and to achieve our intended business objectives.

**Critical Accounting Policies**

The policies below are critical to our business operations and the understanding of our results of operations. In the ordinary course of business, we make a number of estimates and assumptions relating to the reporting of our results.

Our consolidated financial statements have been prepared using accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and the related disclosures of contingent assets and liabilities. We base our estimates on historical experience and on various assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Our critical accounting policies relate to the following matters and are described below:

Revenue;

**Table of Contents**

Goodwill and intangible assets;

Stock-based compensation;

Allowance for doubtful accounts and advertiser credits; and

Provision for income taxes.

***Revenue***

We currently generate revenue through our operating businesses by delivering call and click-based advertising products that enable advertisers of all sizes to reach consumers across online, mobile and offline sources. Our primary source of revenue is performance-based advertising, which includes pay-for-call advertising, pay-per-click advertising, and cost-per-action services. For pay-for-call and pay-per-click advertising, revenue is recognized upon delivery of qualified and reported phone calls or click-throughs to our advertisers or advertising service providers listing which occurs when a mobile, online or offline user makes a phone call or clicks on any of their advertisements after it has been placed by us or by our distribution partners. Each phone call or click-through on an advertisement listing represents a completed transaction. For cost-per-action services, revenue is recognized when a user makes a phone call from our advertiser's listing or is redirected from one of our web sites or a third party web site in our distribution network to an advertiser web site and completes the specified action. In certain cases, we record revenue based on available and reported preliminary information from third parties. Collection on the related receivables may vary from reported information based upon third party refinement of the estimated and reported amounts owing that occurs subsequent to period ends.

We have entered into agreements with various distribution partners in order to expand our distribution network, which includes mobile and online search engines and applications, directories, shopping engines, third party Internet domains or web sites, other targeted Web-based content, offline sources, and our portfolio of owned web sites, on which we include our advertisers' listings. We generally pay distribution partners based on a specified percentage of revenue or a fixed amount per phone call or click-through on these listings. We act as the primary obligor in these transactions, and we are responsible for providing customer and administrative services to the advertiser. In accordance with FASB ASC 605, the revenue derived from advertisers who receive paid introductions through us as supplied by distribution partners is reported gross based upon the amounts received from the advertiser. We also recognize revenue for certain agency contracts with advertisers under the net revenue recognition method. Under these specific agreements, we purchase listings on behalf of advertisers from search engines and directories. We are paid account fees and also agency fees based on the total amount of the purchase made on behalf of these advertisers. Under these agreements, our advertisers are primarily responsible for choosing the publisher and determining pricing, and the Company, in certain instances, is only financially liable to the publisher for the amount collected from our advertisers. This creates a sequential liability for media purchases made on behalf of advertisers. In certain instances, the web publishers engage the advertisers directly and we are paid an agency fee based on the total amount of the purchase made by the advertiser. In limited arrangements resellers pay us a fee for fulfilling an advertiser's campaign in our distribution network and we act as the primary obligor. We recognize revenue for these fees under the gross revenue recognition method.

On September 10, 2013, we launched our Domains Marketplace, which provides domain names available for sale and initiated plans to facilitate the active buying and transacting of domain names. Domain name sales occurring after this launch have been recognized as revenue in the consolidated financial statements. Historically, the sale of domain names were not a core operation and were peripheral to the generation of advertising revenue from domain names held for use and as such domain name sales were reported as gains on sales and disposals of intangible assets, net in the consolidated financial statements.

We apply FASB ASC 605 to account for revenue arrangements with multiple deliverables. FASB ASC 605 addresses certain aspects of accounting by a vendor for arrangements under which the vendor will perform multiple revenue-generating activities. When an arrangement involves multiple elements, the entire fee from the

---

## **Table of Contents**

arrangement is allocated to each respective element based on its relative selling price and recognized when revenue recognition criteria for each element are met. The relative selling price for each element is determined using a hierarchy of (1) company specific objective evidence, then (2) third party evidence, then (3) best estimate of selling price.

### ***Goodwill and Intangible Assets***

Goodwill represents the excess of the purchase price over the fair value of identifiable assets acquired and liabilities assumed in business combinations accounted for under the purchase method.

We apply the provisions of FASB ASC 350 *Goodwill and Intangible Assets* acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of FASB ASC 350. FASB ASC 350 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with FASB ASC 360.

Goodwill is tested annually for impairment and is tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. The provisions of the accounting standard for goodwill and other intangible assets allow us to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Events and circumstances considered in determining whether the carrying value of goodwill may not be recoverable include, but are not limited to: significant changes in performance relative to expected operating results; significant changes in the use of the assets; significant negative industry or economic trends; and a significant decline in the Company's stock price and/or market capitalization for a sustained period of time. If our stock price were to trade below book value per share for an extended period of time and/or we continue to experience adverse effects of a continued downward trend in the overall economic environment, changes in the business itself, including changes in projected earnings and cash flows, we may have to recognize an impairment of all or some portion of our goodwill. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. If the fair value is lower than the carrying value, a material impairment charge may be reported in our financial results. We exercise judgment in the assessment of the related useful lives of intangible assets, the fair values and the recoverability. In certain instances, the fair value is determined in part based on cash flow forecasts and discount rate estimates. We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. To the extent such evaluation indicates that the useful lives of intangible assets are different than originally estimated, the amortization period is reduced or extended and, accordingly, amortization expense is increased or decreased. Recoverability of assets held and used is measured by a comparison of the carrying amount of an asset group to estimated undiscounted future cash flows expected to be generated by the asset group. If such asset group is considered to be impaired, the impairment is to be recognized by the amount by which the carrying amount of the assets exceeds fair value. Assets to be disposed of are separately presented on the balance sheet and reported at the lower of their carrying amount or fair value less costs to sell, and are no longer depreciated. We cannot accurately predict the amount and timing of any impairment of goodwill or other intangible assets. Should the value of goodwill or other intangible assets become impaired, we would record the appropriate charge, which could have an adverse effect on our financial condition and results of operations.

The current business environment is subject to evolving market conditions and requires significant management judgment to interpret the potential impact to our assumptions. To the extent that changes in the current business environment impact our ability to achieve levels of forecasted operating results and cash flows, or should other events occur indicating the remaining carrying value of our assets might be impaired, we would test its goodwill and intangible assets for impairment and may recognize an additional impairment loss to the extent that the carrying amount exceeds such asset's fair value. We will continue to monitor our financial performance, stock price and other factors in order to determine if there are any indicators of impairment prior to our annual impairment evaluation in the fourth quarter.

---

## **Table of Contents**

Any future additional impairment charges or changes to the estimated amortization periods could have a material adverse effect on our financial results.

### ***Stock-Based Compensation***

FASB ASC 718 requires the measurement and recognition of compensation for all stock-based awards made to employees, non-employees and directors including stock options, restricted stock issuances, and restricted stock units based on estimated fair values. Under the fair value recognition provisions, we recognize stock-based compensation net of an estimated forfeiture rate, and therefore only recognize compensation cost for those shares expected to vest over the requisite service period.

We generally use the Black-Scholes option pricing model as our method of valuation for stock-based awards with time-based vesting. Our determination of the fair value of stock-based awards on the date of grant using an option pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to the expected life of the award, our expected stock price, volatility over the term of the award and actual and projected exercise behaviors. For stock-based awards with time-based vesting, we are required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. We estimate the forfeiture rate based on historical experience of our stock-based awards that are granted, exercised and cancelled. If our actual forfeiture rate is materially different from our estimate, the stock-based compensation expense could be significantly different from what we have recorded in the current period.

During 2012 and 2013, we issued equity awards of stock options, restricted stock awards, and restricted stock units that have vesting based on a combination of certain service and market conditions. For equity awards with vesting based on a combination of certain service and market conditions, we factor an estimated probability of achieving certain service and market conditions and recognize compensation cost over the requisite service period of the award. We used a binomial lattice model to determine the fair value for each tranche and a Monte Carlo simulation to determine the derived service period for each tranche.

Although the fair value of stock-based awards is determined in accordance with FASB ASC 718, the assumptions used in calculating fair value of stock-based awards, the use of the Black-Scholes option pricing model, and the use of the binomial lattice model and a Monte Carlo simulation are highly subjective, and other reasonable assumptions could provide differing results. As a result, if factors change and we use different assumptions, our stock-based compensation expense could be materially different in the future. See *Note 6(b). Stock Option Plan* in the consolidated financial statements for additional information.

FASB ASC 718 requires the benefits of tax deductions in excess of the stock-based compensation cost to be classified as financing cash inflows. In addition, a tax benefit and a credit to additional paid-in capital for the excess deductions is not recognized until that deduction reduces taxes payable. For the year ended December 31, 2013, we incurred an excess tax benefit which was not recorded because we are in a cumulative loss carryforward position for income taxes.

### ***Allowance for Doubtful Accounts and Advertiser Credits***

Accounts receivable balances are presented net of allowance for doubtful accounts and advertiser credits. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our accounts receivable. We determine our allowance based on analysis of historical bad debts, advertiser concentrations, advertiser creditworthiness and current economic trends. We review the allowance for collectability on a quarterly basis. Account balances are written off against the allowance after all reasonable means of collection have been exhausted and the potential recovery is considered remote. If the financial condition of our advertisers were to deteriorate, resulting in an impairment of their ability to make payments, or if we underestimated the allowances required, additional allowances may be required which would result in increased general and administrative expenses in the period such determination was made.

---

**Table of Contents**

We determine our allowance for advertiser credits and adjustments based upon our analysis of historical credits. Material differences may result in the amount and timing of our revenue for any period if our management made different judgments and estimates.

***Provision for Income Taxes***

We utilize the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred 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 on deferred tax assets and liabilities of a change in tax law is recognized in results of operations in the period that includes the enactment date.

Each reporting period we must assess the likelihood that our deferred tax assets will be recovered from existing deferred tax liabilities or future taxable income, and to the extent that realization is not more likely than not, a valuation allowance must be established. The establishment of a valuation allowance and increases to such an allowance may result in either an increase to income tax expense or reduction of income tax benefit in the statement of operations. Although realization is not assured, we believe it is more likely than not, based on operating performance, existing deferred tax liabilities, projections of future taxable income and tax planning strategies, that our net deferred tax assets, excluding certain state and foreign NOL carryforwards, will be realized. In determining that it was more likely than not that we would realize the deferred tax assets, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions and issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets.

As of December 31, 2013, we have net deferred tax assets of \$26.2 million, relating to the impairment of goodwill, amortization of intangibles assets, certain other temporary differences, acquired federal and state net operating loss carryforwards, and research and development credits. At December 31, 2012 and 2013, we have recorded a valuation allowance of \$21.6 million and \$23.0 million, respectively, against our federal net deferred tax assets as we believe it is more likely than not that these benefits will not be realized. The change in the valuation allowance in 2013 was approximately \$1.4 million due to an increase in our gross deferred tax assets primarily related to the 2012 and 2013 research and development credit and federal and state NOLs recorded during 2013.

Each reporting period we must assess the likelihood that our deferred tax assets will be recovered from existing deferred tax liabilities or future taxable income, and to the extent that realization is not more likely than not, a valuation allowance must be established. The establishment of a valuation allowance and increases to such an allowance may result in either an increase to income tax expense or reduction of income tax benefit in the statement of operations. Although realization is not assured, we believe it is more likely than not, based on operating performance, existing deferred tax liabilities, projections of future taxable income and tax planning strategies, that our net deferred tax assets, excluding certain state and foreign NOL carryforwards, will be realized. In determining that it was more likely than not that we would realize the deferred tax assets, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions and issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets.

The majority of our deferred tax assets are from goodwill and intangible assets recorded in connection with various acquisitions that are tax-deductible over 15 year periods. Based on projections of future taxable income and tax planning strategies, we expect to be able to recover these assets. The amount of the net deferred tax assets considered realizable, however, may be reduced in the near term if our projections of future taxable income are reduced or if we do not perform at the levels we are projecting. This may result in increases to the valuation

---

**Table of Contents**

allowance for deferred tax assets and may increase income tax expense of up to the entire net amount of deferred tax assets.

As of December 31, 2013, based upon both positive and negative evidence available, we have determined it is not more likely than not that certain deferred tax assets primarily relating to NOL carryforwards in certain state, city, and foreign jurisdictions will be realizable and accordingly, have recorded a 100% valuation allowance of \$6.0 million against these deferred tax assets. We do not have a history of taxable income in the relevant jurisdictions and the state and foreign NOL carryforwards will more likely than not expire unutilized. Should we determine in the future that we will be able to realize these deferred tax assets, or not be able to realize all or part of our remaining net deferred tax assets recorded as of December 31, 2013, an adjustment to the net deferred tax assets would impact net income or stockholders' equity in the period such determination was made.

As of December 31, 2012 and 2013, we had certain federal NOL carryforwards of \$1.7 million which will begin to expire in 2019. The Tax Reform Act of 1986 limits the use of NOL and tax credit carryforwards in certain situations where changes occur in the stock ownership of a company. We believe that such a change has occurred, and that approximately \$1.7 million of NOL carryforwards is limited such that substantially all of these federal NOL carryforwards will never be available. Accordingly, we have not recorded a deferred tax asset for these NOL s.

In connection with the Jingle acquisition in 2011, we acquired federal NOL carryforwards. Where there is a change in ownership within the meaning of Section 382 of the Internal Revenue Code, the acquired federal net operating loss carryforwards are subject to an annual limitation. We believe that such an ownership change had occurred at Jingle, and that the utilization of the carryforwards is limited such that the majority of the NOL carryforwards will never be utilized. Accordingly, we have not recorded those amounts we believe it will not be able to utilize and has not included those NOL carryforwards in its deferred tax assets. We recorded NOL carryforwards that may be utilized of approximately \$7.0 million in which \$2.6 million was utilized in 2011.

From time to time, various state, federal, and other jurisdictional tax authorities undertake reviews of us and our filings. We believe any adjustments that may ultimately be required as a result of any of these reviews will not be material to the financial statements.

FASB ASC 740 clarifies the accounting for uncertainty in income taxes recognized in the financial statements. This pronouncement prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in the our tax return. FASB ASC 740 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure requirements for uncertain tax positions.

**Accounting Standards Issued Not Yet Adopted**

In July 2013, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists ( ASU 2013-11)*. The amendments in this update require an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The assessment of whether a deferred tax asset is available is based on the unrecognized tax benefit and deferred tax asset that exist at the reporting date and should be made presuming

**Table of Contents**

disallowance of the tax position at the reporting date. The amendments in this update do not require new recurring disclosures. ASU 2013-11 is effective for annual and interim periods beginning after December 15, 2013 and early adoption is permitted. We do not expect this update to have a material impact on its consolidated financial statements.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Our exposure to market risk is limited to interest income sensitivity, which is affected by changes in the general level of U.S. interest rates, particularly because the majority of our investments are in short-term, money market funds. We place our investments with high-quality financial institutions. During the years ended December 31, 2012 and 2013, the effects of changes in interest rates on the fair market value of our investments and our earnings were not material. Further, we believe that the impact on the fair market value of our investments and our earnings from a hypothetical 10% change in interest rates would not be significant. We do not have any material foreign currency or other derivative financial instruments.

Our existing credit facility bears interest at a rate which will be, at our option, either: (i) the applicable margin rate (depending on our leverage) plus the one-month LIBOR rate reset daily, or (ii) the applicable margin rate plus the 1, 2, 3, or 6-month LIBOR rate. This facility is exposed to market rate fluctuations and may impact the interest paid on any borrowings under the credit facility. Currently, we have no borrowings under this facility; however, an increase in interest rates would impact interest expense on future borrowings.

**Table of Contents**

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.  
INDEX TO FINANCIAL STATEMENTS**

	<b>Page</b>
<b>Marchex, Inc.</b>	
<u>Reports of Independent Registered Public Accounting Firm</u>	74
<u>Consolidated Balance Sheets as of December 31, 2012 and 2013</u>	75
<u>Consolidated Statements of Operations for the years ended December 31, 2011, 2012 and 2013</u>	76
<u>Consolidated Statements of Stockholders' Equity for the years ended December 31, 2011, 2012 and 2013</u>	77
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2011, 2012 and 2013</u>	78
<u>Notes to Consolidated Financial Statements</u>	79



**Table of Contents**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders

Marchex, Inc.:

We have audited the accompanying consolidated balance sheets of Marchex, Inc. and subsidiaries as of December 31, 2012 and 2013, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Marchex, Inc. and subsidiaries as of December 31, 2012 and 2013, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 3, 2014 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Seattle, Washington

March 3, 2014

---

**Table of Contents**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders

Marchex, Inc.:

We have audited Marchex, Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Marchex, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Marchex, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Marchex, Inc. and subsidiaries as of December 31, 2012 and 2013, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013, and our report dated March 3, 2014 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Seattle, Washington

March 3, 2014

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Consolidated Balance Sheets****(in thousands, except per share amounts)**

	<b>As of December 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 15,930	\$ 30,912
Accounts receivable, net	25,988	30,005
Prepaid expenses and other current assets	2,667	2,943
Refundable taxes	264	97
Deferred tax assets	830	1,016
<b>Total current assets</b>	<b>45,679</b>	<b>64,973</b>
Property and equipment, net	6,005	5,440
Deferred tax assets	27,677	25,138
Intangible and other assets, net	611	484
Goodwill	65,815	65,679
Intangible assets from acquisitions, net	3,360	434
<b>Total assets</b>	<b>\$ 149,147</b>	<b>\$ 162,148</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 12,378	\$ 15,922
Accrued expenses and other current liabilities	9,609	7,988
Deferred revenue	2,009	1,388
<b>Total current liabilities</b>	<b>23,996</b>	<b>25,298</b>
Other non-current liabilities	2,216	2,095
<b>Total liabilities</b>	<b>26,212</b>	<b>27,393</b>
Commitments and contingencies		
Stockholders equity:		
Common stock, \$.01 par value. Authorized 137,500 shares;		
Class A: 12,500 shares authorized; 9,832 and 9,570 shares issued and outstanding, respectively, at December 31, 2012; 8,032 and 7,770 shares issued and outstanding, respectively, at December 31, 2013	98	80
Class B: 125,000 shares authorized; 28,380 and 27,978 shares issued and outstanding, respectively, at December 31, 2012, including 2,433 of restricted stock at December 31, 2012; and 30,879 and 30,720 shares issued and outstanding, respectively, at December 31, 2013, including of 1,884 restricted stock at December 31, 2013	284	309
Treasury stock: 402 and 159 shares of Class B stock at December 31, 2012 and 2013, respectively	(13)	(2)
Additional paid-in capital	295,532	305,517
Accumulated deficit	(172,966)	(171,149)
<b>Total stockholders equity</b>	<b>122,935</b>	<b>134,755</b>
<b>Total liabilities and stockholders equity</b>	<b>\$ 149,147</b>	<b>\$ 162,148</b>

See accompanying notes to consolidated financial statements.



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Consolidated Statements of Operations****(in thousands, except per share amounts)**

	Years ended December 31,		
	2011	2012	2013
Revenue	\$ 138,726	\$ 132,794	\$ 152,550
Expenses:			
Service costs <sup>(1)</sup>	75,433	75,920	91,858
Sales and marketing <sup>(1)</sup>	14,389	13,057	11,182
Product development <sup>(1)</sup>	22,603	23,200	27,346
General and administrative <sup>(1)</sup>	22,653	22,838	19,385
Amortization of intangible assets from acquisitions <sup>(2)</sup>	5,455	4,728	2,926
Acquisition and separation related costs	1,890	753	878
Total operating expenses	142,423	140,496	153,575
Impairment of goodwill		(15,837)	
Gain on sales and disposals of intangible assets, net	9,421	6,296	3,774
Income (loss) from operations	5,724	(17,243)	2,749
Other income (expense):			
Interest income	141	14	15
Interest and line of credit expense	(604)	(438)	(76)
Other	5	(25)	24
Total other income (expense)	(458)	(449)	(37)
Income (loss) from continuing operations before provision for income taxes	5,266	(17,692)	2,712
Income tax expense	2,511	16,566	1,755
Net income (loss) from continuing operations	2,755	(34,258)	957
Discontinued operations:			
Income (loss) from discontinued operations, net of tax	204	(938)	(70)
Gain on sale of discontinued operations, net of tax			930
Discontinued operations, net of tax	204	(938)	860
Net income (loss)	2,959	(35,196)	1,817
Dividends paid to participating securities	(259)	(657)	
Net income (loss) applicable to common stockholders	\$ 2,700	\$ (35,853)	\$ 1,817
Basic and diluted net income (loss) per Class A share applicable to common stockholders:			
Continuing operations	\$ 0.07	\$ (1.03)	\$ 0.03
Discontinued operations, net of tax	\$ 0.01	\$ (0.03)	\$ 0.02
Basic and diluted net income (loss) per Class A share applicable to common stockholders	\$ 0.08	\$ (1.06)	\$ 0.05
Basic and diluted net income (loss) per Class B share applicable to common stockholders:			
Continuing operations	\$ 0.07	\$ (1.02)	\$ 0.03
Discontinued operations, net of tax	\$ 0.01	\$ (0.03)	\$ 0.02
Basic and diluted net income (loss) per Class B share applicable to common stockholders	\$ 0.08	\$ (1.05)	\$ 0.05
Dividends paid per share	\$ 0.08	\$ 0.25	\$
Shares used to calculate basic net income (loss) per share applicable to common stockholders:			
Class A	9,928	9,574	8,816
Class B	23,358	24,412	26,798

## Edgar Filing: MARCHEX INC - Form 10-K

Shares used to calculate diluted net income (loss) per share applicable to common stockholders:

Class A	9,928	9,574	8,816
Class B	35,318	33,986	36,999

(1) Excludes amortization of intangible assets from acquisitions.

(2) Components of amortization of intangible assets from acquisitions:

Service costs	\$ 4,515	\$ 3,484	\$ 1,981
Sales and marketing	897	1,228	945
General and administrative	43	16	

Total	\$ 5,455	\$ 4,728	\$ 2,926
-------	----------	----------	----------

See accompanying notes to consolidated financial statements.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Consolidated Statements of Stockholders Equity**

(in thousands)

	Class A common stock		Class B common stock		Treasury stock		Additional paid-in capital	Accumulated deficit	Total stockholders equity
	Shares	Amount	Shares	Amount	Shares	Amount			
Balances at December 31, 2010	10,238	\$ 105	25,480	\$ 255	(223)	\$ (1,360)	\$ 281,421	\$ (140,729)	\$ 139,692
Issuance of common stock upon exercise of stock options			411	4			1,753		1,757
Income tax benefit of option exercises and restricted stock vesting, net							913		913
Issuance of common stock under employee stock purchase plan			4				26		26
Issuance of common stock in connection with acquisition			1,019	10			7,593		7,603
Issuance of restricted stock to employees			1,103	11					11
Issuance of restricted stock to employees as part of acquisitions			462	5					5
Repurchase of Class B common stock					(883)	(6,159)			(6,159)
Conversion of Class A common stock to Class B common stock	(606)	(6)	606	6					
Repurchase of unvested restricted stock					(62)	(1)			(1)
Stock compensation from options and restricted stock, net of estimated forfeitures							15,140		15,140
Retirement of treasury stock loss			(1,011)	(10)	1,011	6,453	(6,443)		
Net Income								2,959	2,959
Common stock cash dividends							(2,938)		(2,938)
Balances at December 31, 2011	9,632	\$ 99	28,074	\$ 281	(157)	\$ (1,067)	\$ 297,465	\$ (137,770)	\$ 159,008
Issuance of common stock upon exercise of stock options			6				27		27
Income tax shortfall of option exercises and restricted stock vesting, net							(4,006)		(4,006)
Issuance of common stock under employee stock purchase plan			10				36		36
Issuance of restricted stock to employees			1,484	15					15
Tax withholding related to restricted stock awards			(7)		(384)	(4)	(1,607)		(1,611)
Repurchase of Class B common stock					(387)	(1,651)			(1,651)
Conversion of Class A common stock to Class B common stock	(62)	(1)	62	1					
Repurchase of unvested restricted stock					(723)	(7)			(7)
Stock compensation from options and restricted stock, net of estimated forfeitures							15,696		15,696
Retirement of treasury stock			(1,249)	(13)	1,249	2,716	(2,703)		
Net loss								(35,196)	(35,196)
Common stock cash dividends							(9,376)		(9,376)
Balances at December 31, 2012	9,570	\$ 98	28,380	\$ 284	(402)	\$ (13)	\$ 295,532	\$ (172,966)	\$ 122,935
Issuance of common stock upon exercise of stock options			560	6			2,925		2,931
Issuance of common stock upon vesting of restricted stock units			71						
							(384)		(384)

Edgar Filing: MARCHEX INC - Form 10-K

Income tax shortfall of option exercises, restricted stock vesting and other, net										
Issuance of common stock under employee stock purchase plan			12				72			72
Issuance of restricted stock to employees			735	7						7
Tax withholding related to restricted stock awards					(220)	(2)	(1,764)			(1,766)
Repurchase of Class B common stock					(31)	(119)				(119)
Conversion of Class A common stock to Class B common stock	(1,800)	(18)	1,800	18						
Repurchase of unvested restricted stock					(185)	(2)				(2)
Stock compensation from options and restricted stock, net of estimated forfeitures							9,264			9,264
Retirement of treasury stock			(679)	(6)	679	134	(128)			
Net income									1,817	1,817
Balances at December 31, 2013	7,770	\$ 80	30,879	\$ 309	(159)	\$ (2)	\$ 305,517	\$ (171,149)	\$	134,755

See accompanying notes to consolidated financial statements.



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Consolidated Statements of Cash Flows**

(in thousands)

	Years ended December 31,		
	2011	2012	2013
Cash flows from operating activities:			
Net income (loss)	\$ 2,959	\$ (35,196)	\$ 1,817
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Amortization and depreciation	9,473	8,457	6,683
Accretion of interest expense	519	362	
Acquisition and separation related costs	372	(132)	(62)
Leasehold improvement incentive	204		
Impairment of goodwill		16,739	
(Gain) loss on sales of fixed assets, net	(4)		7
Gain on sale of discontinued operations			(1,492)
Gain on sales and disposals of intangible assets, net	(9,421)	(6,296)	(3,774)
Allowance for doubtful accounts and advertiser credits	1,203	1,780	1,722
Stock-based compensation	15,143	15,696	9,264
Deferred income taxes	1,895	16,586	1,968
Excess tax benefit related to stock-based compensation	(1,032)	(308)	
Change in certain assets and liabilities, net of acquisition:			
Accounts receivable, net	(6,965)	2,948	(5,732)
Refundable taxes, net	4,006	(100)	167
Prepaid expenses and other current assets	(1,618)	1,884	(338)
Accounts payable	(1,542)	(550)	3,513
Accrued expenses and other current liabilities	1,195	(1,704)	(39)
Deferred revenue	210	79	(49)
Other non-current liabilities	185	(344)	(59)
Net cash provided by operating activities	16,782	19,901	13,596
Cash flows from investing activities:			
Purchases of property and equipment	(3,971)	(2,879)	(3,041)
Cash paid for acquisitions, net of cash acquired	(15,801)		
Proceeds from sales of property and equipment	9		9
Proceeds from sales of intangible assets	9,474	6,319	3,775
Purchases of intangibles and changes in other non-current assets	(103)	(120)	(154)
Proceeds from sale of discontinued operations			1,058
Net cash provided by (used in) investing activities	(10,392)	3,320	1,647
Cash flows from financing activities:			
Excess tax benefit related to stock-based compensation	1,032	308	
Tax withholding related to restricted stock awards		(226)	(3,150)
Repurchase of Class B common stock for treasury stock	(6,159)	(1,651)	(119)
Common stock dividends payments	(2,938)	(9,376)	
Proceeds from exercises of stock option	1,754	27	2,931
Proceeds from issuance of restricted stock to employees, net of repurchases of forfeited unvested restricted stock	10	8	5
Deferred acquisition payments		(33,860)	
Proceeds from employee stock purchase plan	26	36	72
Net cash used in financing activities	(6,275)	(44,734)	(261)

Edgar Filing: MARCHEX INC - Form 10-K

Net increase (decrease) in cash and cash equivalents	115	(21,513)	14,982
Cash and cash equivalents at beginning of period	37,328	37,443	15,930
Cash and cash equivalents at end of period	\$ 37,443	\$ 15,930	\$ 30,912
Supplemental disclosure of cash flow information:			
Cash received during the period for income taxes, net of payments	(2,994)	117	19
Cash paid during the period for interest accretion on deferred payment		881	
Cash paid (received) during the period for interest, net	(63)	(62)	(80)
Supplemental disclosure of non-cash investing and financing activities:			
Fair value of Class B common stock issued in connection with acquisition	7,603		
Deferred payments related to acquisition	34,695	835	
Property and equipment acquired in accounts payable and accrued expenses	121	239	167
Tax withholding related to restricted stock awards in accrued expenses		1,384	

See accompanying notes to consolidated financial statements.

---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**(1) Description of Business and Summary of Significant Accounting Policies and Practices**

***(a) Description of Business and Basis of Presentation***

Marchex, Inc. (the Company) was incorporated in the state of Delaware on January 17, 2003. The Company is a mobile and call advertising technology company. The Company provides products and services for businesses of all sizes that depend on consumer phone calls to drive sales. The Company's technology platform delivers performance-based, pay-for-call advertising across numerous mobile and online publishers to connect high-intent consumers with businesses over the phone while its technology facilitates call quality, analyzes calls in real time and measures the outcomes of calls. The Company through its Archeo division enables the buying, selling and development of domain names. The Company also provides performance-based online advertising that connects advertisers with consumers across our owned web sites as well as third party web sites.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Acquisitions are included in the Company's consolidated financial statements as of and from the date of acquisition. The Company's purchase accounting resulted in all assets and liabilities of acquired businesses being recorded at their estimated fair values on the acquisition dates. All inter-company transactions and balances have been eliminated in consolidation. Certain reclassifications have been made to the consolidated financial statements in the prior periods to conform to the current period presentation.

In July 2013, the Company sold certain assets related to Archeo's pay per click advertising services. As a result, the operating results related to these certain pay per click assets are shown as discontinued operations in the consolidated statements of operations for all periods presented (see *Note 15. Discontinued Operations*). Unless otherwise indicated, information presented in the notes to the financial statements relates only to the Company's continuing operations.

*Acquisition*

On April 7, 2011, the Company acquired 100% of the stock of Jingle Networks, Inc. (Jingle), a provider of mobile voice search performance advertising and technology solutions in North America. See *Note 9. Acquisition* for further discussion.

*Proposed Separation Update*

On November 1, 2012, the Company announced that its board of directors had authorized the Company to pursue the separation of its mobile advertising business focused on calls and Archeo, its domain and click-based advertising business. On September 19, 2013, the Company announced following a strategic review that it would no longer pursue the separation and that Archeo will continue to operate as a division of the Company. The Company will continue to evaluate various strategic alternatives for the Archeo assets.

***(b) Cash and Cash Equivalents***

The Company considers all highly liquid investments with an original maturity of three months or less at the date of purchase to be cash equivalents. Cash equivalents consist primarily of money market funds.

***(c) Fair Value of Financial Instruments***

The Company had the following financial instruments as of December 31, 2012 and 2013: cash and cash equivalents, accounts receivable, refundable taxes, accounts payable and accrued liabilities. The carrying value of cash and cash equivalents, accounts receivable, refundable taxes, accounts payable and accrued liabilities approximates their fair value based on the liquidity of these financial instruments or based on their short-term nature.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****(d) Accounts Receivable**

Accounts receivable are recorded at the invoiced amount and do not bear interest. Accounts receivable balances are presented net of allowance for doubtful accounts and allowance for advertiser credits.

*Allowance for Doubtful Accounts*

The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in existing accounts receivable. The Company determines the allowance based on analysis of historical bad debts, advertiser concentrations, advertiser credit-worthiness and current economic trends. Past due balances over 90 days and specific other balances are reviewed individually for collectibility. The Company reviews the allowance for collectibility quarterly. Account balances are written off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

The allowance for doubtful account activity for the periods indicated is as follows (in thousands):

	<b>Balance at beginning of period</b>	<b>Charged to costs and expenses</b>	<b>Write-offs, net of recoveries</b>	<b>Balance at end of period</b>
December 31, 2011	457	453	117	793
December 31, 2012	793	594	810	577
December 31, 2013	577	772	728	621

*Allowance for Advertiser Credits*

The allowance for advertiser credits is the Company's best estimate of the amount of expected future reductions in advertisers' payment obligations related to delivered services. The Company determines the allowance for advertiser credits and adjustments based on analysis of historical credits.

The allowance for advertiser credits activity for the periods indicated is as follows (in thousands):

	<b>Balance at beginning of period</b>	<b>Additions charged against revenue</b>	<b>Credits processed</b>	<b>Balance at end of period</b>
December 31, 2011	639	690	856	473
December 31, 2012	473	1,186	1,074	585
December 31, 2013	585	994	870	709

**(e) Property and Equipment**

Property and equipment are stated at cost. Depreciation on computers and other related equipment, purchased and internally developed software, and furniture and fixtures is calculated on the straight-line method over the estimated useful lives of the assets, generally averaging three years. Leasehold improvements are amortized straight-line over the shorter of the lease term or estimated useful lives of the assets ranging from three to eight years.

**(f) Goodwill**

## Edgar Filing: MARCHEX INC - Form 10-K

Goodwill represents the excess of the purchase price over the fair value of identifiable assets acquired and liabilities assumed in business combinations accounted for under the purchase method.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The Company applies the provisions of FASB ASC 350 *Goodwill and Intangible Assets*. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of FASB ASC 350. FASB ASC 350 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with FASB ASC 360.

**(g) Impairment or Disposal of Long-Lived Assets**

The Company reviews its long-lived assets for impairment in accordance with FASB ASC 360 whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds fair value. Assets to be disposed of would be separately presented on the balance sheet and reported at the lower of their carrying amount or fair value less costs to sell, and no longer depreciated.

**(h) Revenue Recognition**

The following table presents our revenues, by revenue source, for the periods presented (in thousands):

	Years ended December 31,		
	2011	2012	2013
Partner and Other Revenue Sources	\$ 118,210	\$ 121,904	\$ 141,617
Proprietary Web site Traffic Sources and Domain Name Revenue	20,516	10,890	10,933
<b>Total Revenue</b>	<b>\$ 138,726</b>	<b>\$ 132,794</b>	<b>\$ 152,550</b>

The Company's partner network revenues are primarily generated using third party distribution networks to deliver advertisers' listings. The distribution network includes mobile and online search engines and applications, directories, destination sites, shopping engines, third party Internet domains or web sites, other targeted Web-based content, mobile carriers and other offline sources. The Company generates revenue upon delivery of qualified and reported phone calls or click-throughs to our advertisers or to advertising services providers' listings. The Company pays a revenue share to the distribution partners to access their mobile, online, offline and other user traffic. Other revenues include the Company's call provisioning and call tracking services, presence management services, and campaign management services.

The Company's proprietary web site traffic revenues are generated from the Company's portfolio of owned web sites which are monetized with pay-for-call or pay-per-click listings that are relevant to the web sites, as well as other forms of advertising, including banner advertising and sponsorships. When an online user navigates to one of the Company's owned and operated web sites and calls or clicks on a particular listing or completes the specified action, the Company receives a fee. Other proprietary web site traffic revenues include domain name sales, which have been recognized as revenue since the launch of its Domains Marketplace in September 2013.

The Company's primary sources of revenue are the performance-based advertising services, which include call advertising, pay-per-click services, and cost-per-action services. These primary sources amounted to greater than 77% of revenue for the years ended December 31, 2011, 2012 and 2013. The secondary sources of revenue are the Local Leads platform which enables partner resellers to sell call advertising and/or search marketing

---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

products, campaign management services, and starting in September 2013, domain name sales through our Domains Marketplace. These secondary sources amounted to less than 23% of revenue for the years ended December 31, 2011, 2012 and 2013. The Company has no barter transactions.

The Company recognizes revenue upon the completion of its performance obligation, provided that: (1) evidence of an arrangement exists; (2) the arrangement fee is fixed and determinable; and (3) collection is reasonably assured.

In certain cases, the Company records revenue based on available and reported preliminary information from third parties. Collection on the related receivables may vary from reported information based upon third party refinement of the estimated and reported amounts owing that occurs subsequent to period ends.

In providing call advertising services and pay-per-click advertising, the Company generates revenue upon delivery of qualified and reported phone calls or click-throughs to advertisers or advertising service providers' listings. These advertisers and advertising service providers pay the Company a designated transaction fee for each phone call or click-through, which occurs when an online user makes a phone call or clicks on any of their advertisement listings after it has been placed by the Company or by the Company's distribution partners. Each phone call or click-through on an advertisement listing represents a completed transaction. The advertisement listings are displayed within the Company's distribution network, which includes mobile and online search engines and applications, directories, destination sites, shopping engines, third party Internet domains or web sites, the Company's portfolio of owned web sites and other targeted Web-based content and offline sources. The Company also generates revenue from cost-per-action services, which occurs when a user makes a phone call from our advertiser's listing or is redirected from one of the Company's web sites or a third party web site in our distribution network to an advertiser web site and completes the specified action.

The Company generates revenue from reseller partners and publishers utilizing the Company's Local Leads platform to sell call advertising, search marketing and other lead generation products. The Company is paid account fees and also agency fees for the Company's products in the form of a percentage of the cost of every call or click delivered to advertisers. The reseller partners or publishers engage the advertisers and are the primary obligor, and the Company, in certain instances, is only financially liable to the publishers in the Company's capacity as a collection agency for the amount collected from the advertisers. The Company recognizes revenue for these fees under the net revenue recognition method. In limited arrangements resellers pay the Company a fee for fulfilling an advertiser's campaign in its distribution network and the Company acts as the primary obligor. The Company recognizes revenue for these fees under the gross revenue recognition method.

On September 10, 2013, we launched our Domains Marketplace, which provides domain names available for sale and initiated plans to facilitate the active buying and transacting of domain names. Domain name sales occurring after this launch have been recognized as revenue in the consolidated financial statements. Historically, the sale of domain names were not a core operation of the Company and were peripheral to the generation of advertising revenue from domain names held for use, and as such, domain name sales were reported as gains on sales and disposals of intangible assets, net in the consolidated financial statements.

In providing pay-per-click contextual targeting services, advertisers purchase keywords or keyword strings, based on an amount they choose for a targeted placement on vertically-focused web sites or specific pages of a web site that are specific to their products or services and their marketing objectives. The contextual results distributed by our services are prioritized for users by the amount the advertiser is willing to pay each time a user clicks on the advertisement and the relevance of the advertisement, which is dictated by historical click-through rates. Advertisers pay the Company when a click-through occurs on their advertisement. In July 2013, the Company sold certain assets related to its pay-per-click contextual advertising services. The results of operations

---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

of these certain pay-per-click assets have been presented in the consolidated financial statements as discontinued operations. *See Note 14. Discontinued Operations* for further discussion.

Advertisers pay the Company additional fees for services such as campaign management. Advertisers generally pay the Company on a click-through basis, although in certain cases the Company receives a fixed fee for delivery of these services. In some cases we also deliver banner campaigns for select advertisers. Banner advertising revenue may be based on a fixed fee per click and is generated and recognized on click-through activity. In other cases, banner payment terms are volume-based with revenue generated and recognized when impressions are delivered.

The Company enters into agreements with various distribution partners to provide distribution for pay-for-call and pay-per-click advertisement listings which contain call tracking numbers and/or URL strings of our advertisers. The Company generally pays distribution partners based on a percentage of revenue or a fixed amount per phone call or click-through on these listings. The Company acts as the primary obligor with the advertiser for revenue call or click-through transactions and is responsible for the fulfillment of services.

In accordance with FASB ASC 605, the revenue derived from advertisers is reported gross based upon the amounts received from the advertiser. The Company also recognizes revenue for certain agency contracts with advertisers under the net revenue recognition method. Under these specific agreements, the Company purchases listings on behalf of advertisers from mobile sources, search engines and applications, directories, other Web-based content providers and offline sources. The Company is paid account fees and also agency fees based on the total amount of the purchase made on behalf of these advertisers. Under these agreements, the advertisers are primarily responsible for choosing the publisher and determining pricing, and the Company, in certain instances, is only financially liable to the publisher for the amount collected from our advertisers. This creates a sequential liability for media purchases made on behalf of advertisers. In certain instances, the web publishers engage the advertisers directly and the Company is paid an agency fee based on the total amount of the purchase made by the advertiser. In other arrangements resellers pay us a fee for fulfilling an advertiser's campaign in our distribution network and we act as the primary obligor. We recognize revenue for these fees under the gross revenue recognition method.

The Company applies FASB ASC 605 to account for revenue arrangements with multiple deliverables. FASB ASC 605 addresses certain aspects of accounting by a vendor for arrangements under which the vendor will perform multiple revenue-generating activities. When an arrangement involves multiple elements, the entire fee from the arrangement is allocated to each respective element based on its relative selling price and recognized when the revenue recognition criteria, as described above, for each element are met. The relative selling price for each element is determined using a hierarchy of (1) company specific objective evidence, then (2) third party evidence, then (3) best estimate of selling price.

***(i) Service Costs***

The largest component of the Company's service costs consist of user acquisition costs that relate primarily to payments made to distribution partners for access to their mobile, online, and offline user traffic. The Company enters into agreements of varying durations with distribution partners that integrate the Company's services into their web sites and indexes. The primary payment structure of the distribution partner agreements is a variable payment based on a specified percentage of revenue. These variable payments are often subject to minimum payment amounts per phone call or click-through. Other payment structures that to a lesser degree exist include: 1) fixed payments, based on a guaranteed minimum amount of usage delivered, 2) variable payments based on a specified metric, such as number of paid click-throughs, and 3) a combination arrangement with both fixed and variable amounts that may be paid in advance.

The Company expenses user acquisition costs based on whether the agreement provides for fixed or variable payments. Agreements with fixed payments with minimum guaranteed amounts of usage are expensed as the



---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

greater of the pro-rata amount over the term of arrangement or the actual usage delivered to date based on the contractual revenue share. Agreements with variable payments based on a percentage of revenue, number of paid phone calls or click-throughs or other metrics are expensed as incurred based on the volume of the underlying activity or revenue multiplied by the agreed-upon price or rate.

Service costs also include network operations and customer service costs that consist primarily of costs associated with providing performance-based advertising and search marketing services, maintaining the Company's web sites, credit card processing fees, network costs and fees paid to outside service providers that provide the Company's paid listings and customer services. Customer service and other costs associated with serving the Company's search results and maintaining the Company's web sites include depreciation of web sites, network equipment and internally developed software, colocation charges of the Company's network web site equipment, bandwidth, software license fees, salaries of related personnel, stock-based compensation and amortization of intangible assets. Other service costs include license fees, domain name costs, the amortization of the purchase cost of domain names, the costs incurred for the renewal of the domain name registration and telecommunication costs, including the use of telephone numbers for providing call-based advertising services.

***(j) Advertising Expenses***

Advertising costs are expensed as incurred and includes mobile and Internet-based advertising, sponsorships, and trade shows. Such costs are included in sales and marketing. The amounts for mobile, online and related outside marketing activities were approximately \$3.2 million, \$1.8 million and \$1.0 million for the years ended December 31, 2011, 2012 and 2013, respectively.

***(k) Other Intangible Assets and Product Development***

The Company capitalizes costs incurred to acquire domain names or URLs, which include the initial registration fees, and amortizes the costs over the expected useful life of the domain names on a straight-line basis. The expected useful lives range from 12 to 84 months. As of December 31, 2012, the net carrying value of Internet domains names related to domain names held for use. On September 10, 2013, the Company launched its Domains Marketplace, which provides domain names available for sale and initiated plans to facilitate the active buying and transacting of domain names. The net carrying value of Internet domain names as of December 31, 2013 related to both domain names held for use and available for sale. In order to maintain the rights to each domain name acquired, the Company pays periodic registration fees, which generally cover a minimum period of 12 months. The Company records registration renewal fees of domain name intangible assets as a prepaid expense and recognizes the cost over the renewal period. Product development costs consist primarily of expenses incurred by the Company in the research and development, creation, and enhancement of the Company's Internet sites and services. Research and development costs are expensed as incurred and include compensation and related expenses, costs of computer hardware and software, and costs incurred in developing features and functionality of the services. For the periods presented, substantially all of the product development expenses are research and development.

Product development costs are expensed as incurred or capitalized into property and equipment in accordance with FASB ASC 350. FASB ASC 350 requires that cost incurred in the preliminary project and post-implementation stages of an internal use software project be expensed as incurred and that certain costs incurred in the application development stage of a project be capitalized.

***(l) Income Taxes***

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred 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 on deferred tax assets and liabilities of a change in tax laws or rates is recognized in results of operations in the period that includes the enactment date. A valuation allowance is recorded for deferred tax assets when it is more likely than not that such deferred tax assets will not be realized.

**(m) Stock-Based Compensation**

The Company measures stock-based compensation cost at the grant date based on the fair value of the award and recognize it as expense, net of estimated forfeitures, over the vesting or service period, as applicable, of the stock award using the straight-line method.

**(n) Use of Estimates**

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. The Company has used estimates related to several financial statement amounts, including revenues, allowance for doubtful accounts, allowance for advertiser credits, useful lives for property and equipment, intangible assets, the fair-value of the Company's common stock and stock option awards, the impairment of goodwill and intangible assets and a valuation allowance for deferred tax assets. Actual results could differ from those estimates.

In certain cases, the Company records revenue based on available and reported preliminary information from third parties. Collection on the related receivables may vary from reported information based upon third party refinement of the estimated and reported amounts owing that occurs subsequent to period ends.

**(o) Concentrations**

The Company maintains substantially all of its cash and cash equivalents with one financial institution and are all considered at Level 1 fair value with observable inputs that reflect quoted prices for identical assets or liabilities in active markets.

A significant majority of the Company's revenue earned from advertisers is generated through arrangements with distribution partners. The Company may not be successful in renewing any of these agreements, or if they are renewed, they may not be on terms as favorable as current arrangements. The Company may not be successful in entering into agreements with new distribution partners or advertisers on commercially acceptable terms. In addition, several of these distribution partners or advertisers may be considered potential competitors.

There were no distribution partners representing more than 10% of consolidated revenue for the years ended December 31, 2011 and 2012, and one distribution partner was paid less than 15% of consolidated revenue for the year ended December 31, 2013.

The advertisers representing more than 10% of consolidated revenue are as follows (in percentages):

	Years ended December 31,		
	2011	2012	2013
Advertiser A	32%	28%	25%
Advertiser B	*	*	13%
Advertiser C	*	*	12%



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

Advertiser A is also a distribution partner.

The outstanding receivable balance for each advertiser representing more than 10% of consolidated accounts receivable is as follows (in percentages):

	At December 31,	
	2012	2013
Advertiser A	36%	41%
Advertiser B	11%	14%
Advertiser C	*	13%

\* Less than 10%.

**(q) Net Income (Loss) Per Share**

The Company computes net income (loss) per share of Class A and Class B common stock using the two class method. Under the provisions of the two class method, basic net income (loss) per share is computed by dividing net income (loss) applicable to common stockholders by the weighted average number of common shares outstanding during the year. Diluted net income (loss) per share is computed by dividing net income (loss) applicable to common stockholder by the weighted average number of common and dilutive common equivalent shares outstanding during the period. The computation of the diluted net income (loss) per share of Class B common stock assumes the conversion of Class A common stock to Class B common stock, while the diluted net income (loss) per share of Class A common stock does not assume the conversion of those shares.

In accordance with the two class method, the undistributed earnings (losses) for each year are allocated based on the contractual participation rights of the Class A and Class B common shares and the restricted shares as if the earnings for the year had been distributed. Considering the terms of the Company's charter which provides that, if and when dividends are declared on our common stock in accordance with Delaware General Corporation Law, equivalent dividends shall be paid with respect to the shares of Class A common stock and Class B common stock and that both classes of common stock have identical dividend rights and would share equally in the Company's net assets in the event of liquidation, the Company has allocated undistributed earnings (losses) on a proportionate basis. Additionally, the Company has paid dividends equally to both classes of common stock and the unvested restricted shares since it initiated a quarterly cash dividend in November 2006.

Instruments granted in unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents, whether paid or unpaid, are participating securities prior to vesting. As such, the Company's restricted stock awards are considered participating securities for purposes of calculating earnings per share. Under the two class method, dividends paid on unvested restricted stock are allocated to these participating securities and therefore impacts the calculation of amounts allocated to common stock.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The following table calculates net income (loss) to net income (loss) applicable to common stockholders used to compare basic net income (loss) per share for the period ended (in thousands, except per share amounts):

	Twelve months ended December 31,					
	2011		2012		2013	
	Class A	Class B	Class A	Class B	Class A	Class B
Basic net income (loss) per share:						
Numerator:						
Net income (loss) from continuing operations	\$ 744	\$ 2,011	\$ (9,900)	\$ (24,358)	\$ 222	\$ 735
Dividends paid to participating securities		(259)		(657)		
Net income (loss) from continuing operations applicable to common stockholders	\$ 744	\$ 1,752	\$ (9,900)	\$ (25,015)	\$ 222	\$ 735
Discontinued operations, net of tax	55	149	(264)	(674)	199	661
Net income (loss) applicable to common stockholders	\$ 799	\$ 1,901	\$ (10,164)	\$ (25,689)	\$ 421	\$ 1,396
Denominator:						
Weighted average number of shares outstanding used to calculate basic net income (loss) per share	9,928	23,358	9,574	24,412	8,816	26,798
Basic net income (loss) per share:						
Net income (loss) from continuing operations applicable to common stockholders	\$ 0.07	\$ 0.07	\$ (1.03)	\$ (1.02)	\$ 0.03	\$ 0.03
Discontinued operations, net of tax	0.01	0.01	(0.03)	(0.03)	0.02	0.02
Basic net income (loss) per share applicable to common stockholders	\$ 0.08	\$ 0.08	\$ (1.06)	\$ (1.05)	\$ 0.05	\$ 0.05

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The following table calculates net income (loss) to diluted net income (loss) applicable to common stockholders used to compute diluted net income (loss) per share for the periods ended (in thousands, except per share amounts):

	Twelve months ended December 31,					
	2011		2012		2013	
	Class A	Class B	Class A	Class B	Class A	Class B
<b>Diluted net income (loss) per share:</b>						
<b>Numerator:</b>						
Net income (loss) from continuing operations	\$ 745	\$ 2,010	\$ (9,900)	\$ (24,358)	\$ 217	\$ 740
Dividends paid to participating securities		(259)		(657)		
Reallocation of net income (loss) for Class A shares as a result of conversion of Class A to Class B shares		745		(9,900)		217
Net income (loss) from continuing operations applicable to common stockholders	\$ 745	\$ 2,496	\$ (9,900)	\$ (34,915)	\$ 217	\$ 957
Discontinued operations, net of tax	54	150	(264)	(674)	195	665
Reallocation of discontinued operations for Class A shares as a result of conversion of Class A to Class B share		54		(264)		195
Diluted discontinued operations, net of tax	\$ 54	\$ 204	\$ (264)	\$ (938)	\$ 195	\$ 860
Net income (loss) applicable to common stockholders	\$ 799	\$ 2,700	\$ (10,164)	\$ (35,853)	\$ 412	\$ 1,817
<b>Weighted average number of shares outstanding used to calculate basic net income (loss) per share</b>						
Weighted average stock options and common shares subject to repurchase or cancellation		2,032				1,385
Conversion of Class A to Class B common shares outstanding		9,928		9,574		8,816
Weighted average number of shares outstanding used to calculate diluted net income (loss) per share	9,928	35,318	9,574	33,986	8,816	36,999
<b>Diluted net income (loss) per share:</b>						
Net income (loss) from continuing operations applicable to common stockholders	\$ 0.07	\$ 0.07	\$ (1.03)	\$ (1.02)	\$ 0.03	\$ 0.03
Discontinued operations, net of tax	0.01	0.01	(0.03)	(0.03)	0.02	0.02
Diluted net income (loss) per share applicable to common stockholders	\$ 0.08	\$ 0.08	\$ (1.06)	\$ (1.05)	\$ 0.05	\$ 0.05

The computation of diluted net income (loss) per share excludes the following because their effect would be anti-dilutive (in thousands):

For the years ended December 31, 2011, 2012 and 2013, outstanding options to acquire 4,792, 7,029, and 4,565 shares, respectively, of Class B common stock.



---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

For the years ended December 31, 2011, 2012, and 2013, 134, 2,433 and 174 shares, respectively, of unvested Class B restricted common shares issued to employees and in connection with acquisitions. These shares were for future services that vest over periods ranging from two to six years.

For the year ended December 31, 2012 and 2013, 131 and 43 restricted stock units with vesting based on meeting certain service and market conditions, respectively.

For the year ended December 31, 2011, 5,987 shares of Class B common stock that may be issued in lieu of cash for the deferred payments related to the acquisition of Jingle using the if converted method. See *Note 9. Acquisition* for further discussion.

**(r) Guarantees**

FASB ASC 460 provides accounting guidance surrounding liability recognition and disclosure requirements related to guarantees. In the ordinary course of business, the Company is not subject to potential obligations under guarantees that fall within the scope of FASB ASC 460 except for standard indemnification provisions that are contained within many of the Company's advertiser and distribution partner agreements, and give rise only to the disclosure requirements prescribed by FASB ASC 460.

In certain agreements, the Company has agreed to indemnification provisions of varying scope and terms with advertisers, vendors and other parties with respect to certain matters, including, but not limited to, losses arising out of the Company's breach of agreements or representations and warranties made by the Company, services to be provided by the Company and intellectual property infringement claims made by third parties. As a result of these provisions, the Company may from time to time provide certain levels of financial support to contract parties to seek to minimize the impact of any associated litigation in which they may be involved. To date, there have been no known events or circumstances that have resulted in any material costs related to these indemnification provisions and no liabilities therefore have been recorded in the accompanying consolidated financial statements. However, the maximum potential amount of the future payments we could be required to make under these indemnification provisions could be material.

**(s) Deferred Acquisition Payment**

The Company's deferred acquisition payments represent consideration payable related to a business combination. Both deferred acquisition payments were paid in cash in April 2012 and October 2012.

**(t) Accounting Standards Issued Not Yet Adopted**

In July 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* (ASU 2013-11). The amendments in this update require an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The assessment of whether a deferred tax asset is available is based on the unrecognized tax benefit and deferred tax asset that exist at the reporting date and should be made presuming



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

disallowance of the tax position at the reporting date. The amendments in this update do not require new recurring disclosures. ASU 2013-11 is effective for annual and interim periods beginning after December 15, 2013 and early adoption is permitted. The Company does not expect this update to have a material impact on its consolidated financial statements.

**(2) Property and Equipment**

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

	<b>Years ended December 31,</b>	
	<b>2012 <sup>(1)</sup></b>	<b>2013 <sup>(1)</sup></b>
Computer and other related equipment	\$ 15,842	\$ 17,794
Purchased and internally developed software	7,452	7,672
Furniture and fixtures	1,242	1,319
Leasehold improvements	1,809	1,829
	\$ 26,345	\$ 28,614
Less: accumulated depreciation and amortization	(20,340)	(23,174)
<b>Property and equipment, net</b>	<b>\$ 6,005</b>	<b>\$ 5,440</b>

(1) Includes the original cost and accumulated depreciation of fully-depreciated fixed assets which were \$15.8 million and \$17.4 million at December 31, 2012 and 2013, respectively.

The Company has capitalized certain costs of internally developed software for internal use. The estimated useful life of costs capitalized is evaluated for each specific project. Amortization begins in the period in which the software is ready for its intended use. The Company has not capitalized any internally developed software costs during 2011, 2012 and 2013.

Depreciation and amortization expense incurred by the Company was approximately \$2.8 million, \$3.2 million and \$3.4 million for the years ended December 31, 2011, 2012 and 2013, respectively.

**(3) Credit Agreement**

In April 2008, the Company entered into a credit agreement providing for a senior secured \$30 million revolving credit facility ( Credit Agreement ). The Credit Agreement, as amended in 2011, matures and all outstanding borrowings are due in April 2014. Interest on outstanding balances under the Credit Agreement will accrue at LIBOR plus an applicable margin rate, as determined under the agreement and has an unused commitment fee. The Credit Agreement contains certain customary representations and warranties, financial covenants, events of default and is secured by substantially all of the assets of the Company. During the years ended December 31, 2012 and 2013, the Company had no borrowings under the Credit Agreement. During the first quarter of 2014, the Company signed an amendment to the Credit Agreement which extends the maturity period to April 1, 2017.

**(4) Commitments**

The Company has commitments for future payments related to office facilities leases and other contractual obligations. The Company leases its office facilities under operating lease agreements expiring through 2018. The Company recognizes rent expense under such agreements on a straight-line basis over the lease term with any lease incentive amortized as a reduction of rent expense over the lease term. The Company also has other contractual obligations expiring over varying time periods through 2016. Other contractual obligations primarily relate to minimum

contractual payments due to distribution partners and other outside service providers.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

Future minimum payments are approximately as follows (in thousands):

	<b>Facilities operating leases</b>	<b>Other contractual obligations</b>	<b>Total</b>
2014	2,287	3,170	5,457
2015	2,225	1,403	3,628
2016	2,267	885	3,152
2017	2,333		2,333
2018 and after	577		577
Total minimum payments	\$ 9,689	\$ 5,458	\$ 15,147

Rent expense incurred by the Company was approximately \$2.1 million, \$2.0 million and \$1.9 million for the years ended December 31, 2011, 2012 and 2013, respectively.

**(5) Income Taxes**

The components of income (loss) from continuing operations before provision for income taxes consist of the following (in thousands):

	<b>Years ended December 31,</b>		
	<b>2011</b>	<b>2012</b>	<b>2013</b>
United States	\$ 5,513	\$ (17,696)	\$ 2,710
Foreign	(247)	4	2
Income (loss) before provision for income taxes	\$ 5,266	\$ (17,692)	\$ 2,712

The provision (benefit) for income taxes from continuing operations for the Company consists of the following (in thousands):

	<b>Years ended December 31,</b>		
	<b>2011</b>	<b>2012</b>	<b>2013</b>
Current provision (benefit)			
Federal	\$ (340)	\$ (69)	\$ (11)
State	16	63	34
Foreign		2	
Deferred provision			
Federal	1,884	4,139	874
State			
Tax expense (benefit) of equity adjustment for stock option exercises and restricted stock vesting	824	(4,227)	(76)
Valuation allowance		16,400	651
Other	127	258	283
Total income tax expense	\$ 2,511	\$ 16,566	\$ 1,755



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

Income tax expense from continuing operations differed from the amounts computed by applying the U.S. federal income tax rates of 34% for 2011, 2012, and 2013, respectively, to income (loss) before provision for income taxes as a result of the following (in thousands):

	Years ended December 31,		
	2011	2012	2013
Income tax expense (benefit) at U.S. statutory rate	\$ 1,790	\$ (6,016)	\$ 922
State taxes, net of valuation allowance	42	40	17
Non-deductible stock compensation	652	589	571
Non-deductible goodwill impairment		3,534	
Effect of rate change on deferred items		1,289	
Valuation allowance		16,400	651
Effect of non-U.S. operations, net of valuation allowance	84		
Research tax credits	(722)	(242)	(851)
Other non-deductible expenses	665	972	445
 Total income tax expense	 \$ 2,511	 \$ 16,566	 \$ 1,755

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below (in thousands):

	As of December 31,	
	2012	2013
Deferred tax assets:		
Accrued liabilities not currently deductible	\$ 1,685	\$ 1,631
Intangible assets-excess of financial statement over tax amortization	15,333	14,208
Goodwill recognized on financial statements in excess of tax amortization	18,976	15,420
Stock-based compensation	4,834	5,158
Federal net operating losses and AMT credit carryforwards	3,519	3,897
State and city net operating loss carryforwards	5,074	5,883
Research & experimental tax credit carryforwards	1,478	2,613
Other	329	582
 Gross deferred tax assets	 51,228	 49,392
Valuation allowance	(21,575)	(23,034)
 Net deferred tax assets	 29,653	 26,358
Deferred tax liabilities:		
Excess of tax over financial statement depreciation	1,146	204
 Total deferred tax liabilities	 1,146	 204
 Net deferred tax assets	 \$ 28,507	 \$ 26,154

The Company recognized approximately \$1.2 million and \$1.5 million in federal NOL carryforwards for 2012 and 2013, respectively, and which will expire in 2032 and 2033, respectively. The Company also has research and development credits of \$2.6 million available to reduce

## Edgar Filing: MARCHEX INC - Form 10-K

income taxes, if any, which will expire in 2029 through 2032, if not utilized. The 2012 Taxpayer Relief Act was signed into law on January 2, 2013 which extends the research tax credit for two years to December 31, 2013 and is retroactive to January 1, 2012. The Company recognized a tax benefit of \$398,000 and \$453,000 for qualifying amounts incurred in 2012 and 2013, respectively, in 2013 when the law was enacted. The Company also increased its valuation allowance in 2013 by \$651,000 primarily as a result of the tax benefit from the federal research and development credit.

---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

The Company has recorded a deferred tax asset for stock-based compensation recorded on unexercised non-qualified stock options and certain restricted shares. The ultimate realization of this asset is dependent upon the fair value of the Company's stock when the options are exercised and when restricted shares vest, and generation of sufficient taxable income to realize the benefit of the related tax deduction.

At December 31, 2012 and 2013, the Company recorded a valuation allowance of \$21.6 million and \$23.0 million, respectively, against its federal, state, city and foreign net deferred tax assets, as it believes it is more likely than not that these benefits will not be realized. The change in the valuation allowance in 2013 was approximately \$1.4 million.

The Company regularly reviews deferred tax assets to assess whether it is more likely than not that the deferred tax assets will be realized and, if necessary, establishes a valuation allowance for portions of such assets to reduce the carrying value. At the end of the fourth quarter of 2012, the Company recognized a partial valuation allowance of \$16.4 million on its federal deferred tax assets. In assessing whether it is more likely than not that the Company's deferred tax assets will be realized, factors considered included: historical taxable income, historical trends related to advertiser usage rates, projected revenues and expenses, macroeconomic conditions, issues facing our industry, existing contracts, our ability to project future results and any appreciation of our other assets. During the fourth quarter of 2012, the Company incurred a \$15.8 million goodwill impairment loss, which excludes \$902,000 related to discontinued operations, within its Archeo reporting unit due in part to lower projected revenue growth rates and profitability levels within Archeo compared to historical results.

The majority of the deferred tax assets have arisen due to deductions taken in the financial statements related to the impairment of goodwill and the amortization of intangible assets recorded in connection with various acquisitions that are tax-deductible over 15 year periods. Consequently, based on projections of future taxable income and tax planning strategies, the Company expects to be able to recover a portion of these assets. Although realization is not assured, the Company believes it is more likely than not, based on its operating performance, existing deferred tax liabilities, projections of future taxable income and tax planning strategies, that the Company's net deferred tax assets, excluding certain state and foreign net operating loss carryforwards, will be realized. The amount of the net deferred tax assets considered realizable, however, could be reduced in the near term if the Company's projections of future taxable income are reduced or if the Company does not perform at the levels it is projecting. This could result in increases to the valuation allowance for deferred tax assets and a corresponding increase to income tax expense of up to the entire net amount of deferred tax assets.

At December 31, 2012 and 2013, the Company has certain tax effected state, city, and foreign net operating loss (NOL) carryforwards of approximately \$5.1 million and \$6.0 million, respectively. The Company does not have a history of taxable income in the relevant jurisdictions and the state, city, and foreign net operating loss carryforwards will more likely than not expire unutilized. Therefore, the Company has recorded a 100% valuation allowance on the state, city, and foreign net operating loss carryforwards as of December 31, 2012 and 2013.

In connection with the Jingle acquisition in 2011, the Company acquired federal NOL carryforwards. Where there is a change in ownership within the meaning of Section 382 of the Internal Revenue Code, the acquired federal net operating loss carryforwards are subject to an annual limitation. The Company believes that such an ownership change had occurred at Jingle, and that the utilization of the carryforwards is limited such that the majority of the NOL carryforwards will never be available. Accordingly, the Company recorded approximately \$7.0 million of NOL carryforwards, which will begin to expire in 2026. The Company utilized \$2.6 million in 2011.

In addition, at December 31, 2012 and 2013, the Company had certain federal net operating loss carryforwards of approximately \$1.7 million which begin to expire in 2019. The Tax Reform Act of 1986 limits

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

the use of NOL and tax credit carryforwards in certain situations where changes occur in the stock ownership of a company. The Company believes that such a change has occurred related to these specific NOL carryforwards, and that the utilization of the approximately \$1.7 million in carryforwards is limited such that substantially all of these NOL carryforwards will never be utilized. Accordingly, the Company has not included these federal NOL carryforwards in its deferred tax assets.

During the years ended December 31, 2011, 2012 and 2013, the Company recognized excess tax benefits (shortfall) on stock option exercises, restricted stock vesting, and dividends paid on unvested restricted stock of approximately \$913,000, (\$4.0) million, and (\$76,000), respectively, which were recorded to additional paid in capital.

The tax benefit realized for the tax deductions from option exercises and restricted stock vesting totaled \$2.5 million, for the year ended December 31, 2011 and \$0 for both the years ended December 31, 2012, and 2013.

From time to time, various state, federal and other jurisdictional tax authorities undertake audits of the Company and its filings. In evaluating the exposure associated with various tax filing positions, the Company on occasion accrues charges for uncertain positions. The Company adjusts these contingencies in light of changing facts and circumstances, such as the outcome of tax audits. Audits of the Company's federal tax returns for 2005 through 2009, comprising approximately \$463,000 of uncertain tax positions, were settled in 2011. Resolution of uncertain tax positions will impact our effective tax rate when settled. The Company does not have any significant interest or penalty accruals. The provision for income taxes includes the impact of contingency provisions and changes to contingencies that are considered appropriate.

The following table summarizes the activity related to the Company's tax contingencies from January 1, 2011 to December 31, 2013 (in thousands):

Gross tax contingencies January 1, 2011	\$ 546
Gross increases to tax positions associated with prior periods	\$ 66
Gross increases to current period tax positions	\$ 156
Gross decreases to tax positions associated with prior periods	\$ (362)
Settlements	\$ (101)
Lapse of statute of limitations	\$
Gross tax contingencies December 31, 2011	\$ 305
Gross increases to tax positions associated with prior periods	\$ 28
Gross increases to current period tax positions	\$
Gross decreases to tax positions associated with prior periods	\$ (83)
Settlements	\$
Lapse of statute of limitations	\$
Gross tax contingencies December 31, 2012	\$ 250
Gross increases to tax positions associated with prior periods	\$
Gross increases to current period tax positions	\$ 284
Gross decreases to tax positions associated with prior periods	\$
Settlements	\$
Lapse of statute of limitations	\$
Gross tax contingencies December 31, 2013	\$ 534





---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

The Company files U.S. federal, certain U.S. states, and certain foreign tax returns. Generally, U.S. federal, U.S. state, and foreign tax returns filed for years after 2009 are within the statute of limitations and are under examination or may be subject to examination.

**(6) Stockholders' Equity**

***(a) Common Stock and Authorized Capital***

The authorized capital stock of the Company consisted of 1,000,000 shares of undesignated preferred stock and 125,000,000 shares of Class B common stock. The Company's board of directors has the authority to issue up to 1,000,000 shares of preferred stock, \$0.01 par value in one or more series and has the authority to designate rights, privileges and restrictions of each such series, including dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences and the number of shares constituting any series.

The Company has two classes of authorized common stock: Class A common stock and Class B common stock. Except with respect to voting rights, the Class A and Class B shares have identical rights. Each share of Class A common stock is entitled to twenty-five votes per share, and each share of Class B common stock is entitled to one vote per share. Each share of Class A common stock is convertible at the holder's option into one share of Class B common stock.

In accordance with the stockholders' agreement signed by Class A and the founding Class B common stockholders, the following provisions survived the Company's initial public offering: Class A stockholders other than Russell C. Horowitz may only sell, assign or transfer their Class A stock to existing Class A stockholders or to the Company and in the event of transfers of Class A stock not expressly permitted by the stockholders' agreement, such shares of Class A stock shall be converted into shares of Class B common stock.

In November 2006, the Company's board of directors authorized a share repurchase program for the Company to repurchase up to 3 million shares of the Company's Class B common stock as well as the initiation of a quarterly cash dividend for the holders of the Class A and Class B common stock. The Company's board of directors has authorized increases to the share repurchase up to 13 million in the aggregate (less shares previously repurchased under the share repurchase program) of the Company's Class B common stock. The timing and actual number of shares repurchased will depend on a variety of factors including price, corporate and regulatory requirements, capital availability, and other market conditions. This stock repurchase program does not have an expiration date and may be expanded, limited or terminated at any time without prior notice. During the years ended December 31, 2011, 2012 and 2013, the Company repurchased approximately 883,000, 387,000, and 31,000 shares, respectively, of Class B common stock for \$6.2 million, \$1.7 million, and \$119,000, respectively, under this repurchase program.

During the years ended December 31, 2012 and 2013, the Company's board of directors authorized the retirement of 1.2 million and 679,000 shares, respectively, of the Company's Class B common stock, all of which had been repurchased by the Company and had been classified as treasury stock on the consolidated balance sheet before retirement.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

During 2011 and 2012, the Company's board of directors declared the following quarterly dividends on the Company's Class A common stock and Class B common stock:

<b>Approval Date</b>	<b>Per share dividend</b>	<b>Date of record</b>	<b>Total amount (in thousands)</b>	<b>Payment date</b>
January 2011	\$ 0.02	February 4, 2011	\$ 712	February 15, 2011
April 2011	\$ 0.02	May 6, 2011	\$ 743	May 16, 2011
July 2011	\$ 0.02	August 5, 2011	\$ 738	August 15, 2011
October 2011	\$ 0.02	November 5, 2011	\$ 745	November 15, 2011
January 2012	\$ 0.02	February 3, 2012	\$ 751	February 15, 2012
April 2012	\$ 0.02	May 4, 2012	\$ 743	May 15, 2012
July 2012	\$ 0.02	August 3, 2012	\$ 755	August 15, 2012
August 2012	\$ 0.015	August 16, 2012	\$ 566	August 31, 2012
October 2012	\$ 0.035	November 2, 2012	\$ 1,300	November 15, 2012
December 2012	\$ 0.14	December 18, 2012	\$ 5,300	December 31, 2012

In August 2012, the Company's board of directors approved an increase to the Company's quarterly cash dividend on the Company's Class A and Class B common stock from \$0.02 per share to \$0.035 per share. The Company paid the incremental \$0.015 per share dividends on August 31, 2012 to Class A and Class B common stockholders of record as of the close of business on August 16, 2012. The Company paid approximately \$566,000 for these incremental dividends.

In December 2012, the Company's board of directors declared a quarterly dividend for the first, second, third and fourth quarters of 2013 totaling \$0.14 per share on its Class A common stock and Class B common stock, which was paid on December 31, 2012 to the holders of record as of the close of business on December 18, 2012. The dividend paid totaled \$5.3 million.

In January 2014, the Company's board of directors declared a quarterly dividend in the amount of \$0.02 per share on its Class A and Class B common stock, which was paid on February 18, 2014 to the holders of record as of the close of business on February 7, 2014. This quarterly dividend totaled approximately \$771,000.

**(b) Stock Option Plan**

The Company's stock incentive plan (the 2003 Plan) allows for grants of both stock option and restricted stock awards to employees, officers, non-employee directors, and consultants and such options may be designated as incentive or non-qualified stock options at the discretion of the Plan's Administrative Committee. In May 2010, the Company's Board of Directors approved an amendment to the Company's 2003 Amended and Restated Stock Incentive Plan (the Plan) which provides for the grant of restricted stock units to eligible participants under the Plan. The Plan authorizes grants of options to purchase up to 4,000,000 shares of authorized but unissued Class B common stock and provides for the total number of shares of Class B common stock for which options designated as incentive stock options may be granted shall not exceed 8,000,000 shares. Annual increases are to be added on the first day of each fiscal year beginning on January 1, 2004 equal to 5% of the outstanding common stock (including for this purpose any shares of common stock issuable upon conversion of any outstanding capital stock of the Company). As a result of this provision, the authorized number of shares available under this Plan was increased by 1,774,752 to 17,676,347 on January 1, 2011 and by 1,877,411 to 19,553,758 on January 1, 2012.

In April 2012, the Company's Board of Directors approved the establishment of the Marchex 2012 Stock Incentive Plan (the 2012 Plan). After December 31, 2012, no further awards will be made under the 2003 Plan.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The 2012 Plan authorizes up to 3,500,000 shares of Class B common stock that may be issued with respect to awards granted under the Plan, and provides that the total number of shares of Class B common stock for which options designated as incentive stock options may be granted shall not exceed 3,500,000 shares. Annual increases to each of these share limits are to be added on the first day of each fiscal year beginning on January 1, 2013 equal to 5% of the outstanding common stock (including for this purpose any shares of common stock issuable upon conversion of any outstanding capital stock of the Company) or in the case of incentive stock options, if lesser of 2,000,000 shares of Class B common stock or such number as determined by the Company's Board of Directors. As a result of this provision, the authorized number of shares available under the 2012 Plan was increased by 1,877,388 to 5,377,388 in January 1, 2013 and by 1,924,511 to 7,301,899 on January 1, 2014. The Company may issue new shares or reissue treasury shares for stock option exercises and restricted stock grants. Generally, stock options have 10-year terms and vest 25% each year either annually or quarterly, over a 4 year period.

The Company did not grant any options with exercise prices less than the then current market value during 2011, 2012 and 2013.

The Company measures stock-based compensation cost at the grant date based on the fair value of the award and recognizes it as expense, net of estimated forfeitures, over the vesting or service period, as applicable, of the stock award using the straight-line method.

Stock-based compensation expense has been included in the same lines as compensation paid to the same employees in the consolidated statement of operations. Stock-based compensation expense was included in the following operating expense categories as follows (in thousands):

	<b>Twelve months ended December 31,</b>		
	<b>2011</b>	<b>2012</b>	<b>2013</b>
Service costs	\$ 1,289	\$ 1,869	\$ 1,180
Sales and marketing	1,471	2,029	645
Product development	1,408	1,038	1,635
General and administrative	10,900	10,702	5,777
<b>Total stock-based compensation</b>	<b>\$ 15,068</b>	<b>\$ 15,638</b>	<b>\$ 9,237</b>
Income tax benefit related to stock-based compensation included in net income (loss) from continuing operations	\$ 5,023	\$ 4,728	\$ 2,575

FASB ASC 718 requires the benefits of tax deductions in excess of the stock-based compensation cost to be classified as financing cash inflows and is shown as "Excess tax benefit related to stock-based compensation" on the consolidated statement of cash flows. In addition, a tax benefit and a credit to additional paid-in capital for the excess deductions is not recognized until that deduction reduces taxes payable. For the year ended December 31, 2013, we incurred an excess tax benefit of \$3.0 million which was not recorded because the Company is in a cumulative loss carryforward position for income taxes.

The Company uses the Black-Scholes option pricing model to estimate the per share fair value of stock option grants with time-based vesting. The Black-Scholes model relies on a number of key assumptions to calculate estimated fair values. For years ended December 31, 2011, 2012 and 2013, the expected life of each award granted was determined based on historical experience with similar awards, giving consideration to contractual terms, anticipated exercise patterns, vesting schedules and forfeitures. Expected volatility is based on historical volatility levels of the Company's Class B common stock and the expected volatility of companies in similar industries that have similar vesting and contractual terms. The risk-free interest rate is based on the

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

implied yield currently available on U.S. Treasury issues with terms approximately equal to the expected life of the option. The Company uses an expected annual dividend yield in consideration of the Company's common stock dividend payments.

The following weighted average assumptions were used in determining the fair value of time-vested stock option grants for the periods presented:

	Years ended December 31,					
	2011		2012		2013	
Expected life (in years)	4.0	6.25	4.0	6.25	4.0	6.25
Risk-free interest rate	0.60% to 1.77%		0.47% to 0.78%		0.57% to 2.10%	
Expected volatility	68% to 71%		65% to 70%		54% to 64%	
Weighted average expected volatility	70%		67%		57%	
Expected dividend yield	0.91%		1.33% to 3.11%		0.87% to 2.33%	

During 2011, 2012, and 2013, the Company issued equity awards which include stock options, restricted stock awards, and restricted stock units that have vesting based on a combination of certain service and market conditions. The compensation costs and derived service periods for stock option grants with vesting based on a combination of service and market conditions are estimated using the binomial lattice model to determine the fair value for each tranche and a Monte Carlo simulation to determine the derived service period for each tranche. The risk-free interest rate is based on the 10 year bond rate as of the valuation date based on the contractual life of the option.

The following weighted average assumptions were used in determining the fair value for option grants with vesting based on a combination of certain service and market conditions for the periods presented:

	Years ended December 31,					
	2011		2012		2013	
Expected life (in years)	1.97	4.54	1.50	5.74	1.18	2.28
Risk-free interest rate	1.94%		1.81%		2.89%	
Expected volatility	57%		60%		61%	
Weighted average expected volatility	57%		60%		61%	
Expected dividend yield	1.26%		3.17%		0.89%	

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

Stock option, restricted stock award and restricted stock unit activity during the period indicated is as follows:

	Options and Restricted Stock available for grant	Number of options outstanding	Weighted average exercise price of options	Weighted average remaining contractual term (in years)	Aggregate intrinsic value (in thousands)
Balance at December 31, 2010	1,924,766	6,410,589	\$ 8.48	7.20	
Increase to option pool January 1, 2011	1,774,752				
Options granted <sup>(1)</sup>	(1,735,950)	1,735,950	7.28		
Restricted stock granted	(1,603,899)				
Restricted stock forfeited	62,125				
Options exercised		(410,662)	4.28		
Options expired	277,775	(277,775)	14.47		
Options forfeited	254,318	(254,318)	6.70		
Balance at December 31, 2011	953,887	7,203,784	\$ 8.24	6.81	
Increase to option pool January 1, 2012	1,877,411				
Options granted <sup>(1)</sup>	(915,500)	915,500	4.13		
Restricted stock granted	(1,343,250)				
Restricted stock forfeited	723,232				
Options exercised		(6,556)	4.13		
Options expired	407,505	(407,505)	11.04		
Options forfeited	675,863	(675,863)	7.04		
Balance at December 31, 2012	2,379,148	7,029,360	\$ 7.67	6.28	\$ 506
Increase to option pool January 1, 2013	1,877,388				
Options granted <sup>(1)</sup>	(2,305,422)	2,305,422	5.91		
Restricted stock granted	(1,528,224)				
Restricted stock forfeited	212,711				
Options exercised		(560,496)	5.23		
Options expired	718,889	(718,889)	6.93		
Options forfeited	347,684	(347,684)	5.67		
Balance at December 31, 2013	1,702,174	7,707,713	\$ 7.48	6.99	\$ 17,148
Options exercisable at December 31, 2013 <sup>(2)</sup>		4,343,185	\$ 8.72	5.41	\$ 7,575

(1) Includes 313,400, 202,000, and 173,750 stock options issued in 2011, 2012 and 2013, respectively, which have vesting based on a combination of certain service and market conditions.

(2) Includes 828,125 stock options which have vested based on meeting a combination of certain service and market conditions.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The following table summarizes information concerning currently outstanding and exercisable options at December 31, 2013:

Range of exercise prices per share	Options Outstanding			Options Exercisable		
	Number Outstanding	Average remaining contractual life (in years)	Weighted Average Exercise price per share	Number exercisable	Weighted average exercise price per share	
\$ 3.18 \$ 4.06	530,425	8.51	\$ 3.82	118,729	\$ 3.63	
\$ 4.10 \$ 4.20	889,426	9.20	4.20	16,911	4.17	
\$ 4.22 \$ 4.63	1,010,625	7.08	4.53	686,035	4.59	
\$ 4.64 \$ 5.47	872,554	6.49	4.99	781,003	4.99	
\$ 5.48 \$ 6.00	192,500	8.43	5.80	48,000	5.61	
\$ 6.01 \$ 6.35	833,200	8.03	6.33	431,547	6.35	
\$ 6.38 \$ 8.77	1,276,210	7.73	8.10	693,706	8.58	
\$ 8.80 \$10.19	847,087	8.04	9.27	311,568	9.73	
\$10.33 \$12.93	771,286	3.04	11.85	771,286	11.85	
\$13.29 \$24.54	484,400	1.95	19.02	484,400	19.02	
	7,707,713	6.98	\$ 7.48	4,343,185	\$ 8.72	

Information related to stock compensation activity during the period indicated is as follows:

	Years ended December 31,		
	2011	2012	2013
Weighted average fair value of options granted	\$ 3.54	\$ 1.78	\$ 2.56
Intrinsic value of options exercised (in thousands)	\$ 1,885	\$ 7	\$ 1,463
Total grant date fair value of restricted stock vested (in thousands)	\$ 4,056	\$ 22,015	\$ 5,751

At December 31, 2013, there was \$8.5 million of stock option compensation expense related to non-vested awards not yet recognized, which is expected to be recognized over a weighted average period of 2.0 years.

During the years ended December 31, 2011, 2012 and 2013 gross proceeds recognized from the exercise of stock options was approximately \$1.8 million, \$27,000 and \$2.9 million, respectively. The net excess tax benefit (shortfall) on stock option exercises, restricted stock vesting, and dividends paid on unvested restricted stock during the years ended December 31, 2011, 2012 and 2013, of approximately \$913,000, (\$4.0) million and (\$76,000), respectively, were recorded to additional paid in capital.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

Restricted stock awards and restricted stock unit activity for the years ended December 31, 2011, 2012 and 2013 is summarized as follows:

	Shares/ Units	Weighted Average Grant Date Fair Value
Unvested at December 31, 2010	3,468,750	\$ 8.13
Granted <sup>(1)</sup>	1,603,899	7.20
Vested	(721,500)	5.63
Forfeited	(62,125)	6.42
Unvested at December 31, 2011	4,289,024	8.23
Granted <sup>(2)</sup>	1,343,250	3.79
Vested	(2,323,431)	9.47
Forfeited	(745,332)	7.08
Unvested at December 31, 2012	2,563,511	5.12
Granted <sup>(2)</sup>	1,528,224	5.43
Vested	(1,169,581)	4.92
Forfeited	(212,711)	4.77
Unvested at December 31, 2013	2,709,443	5.41

(1) Includes 104,100 restricted stock units issued in 2011 which entitle the holder to receive one share of the Company's Class B common stock upon satisfaction of certain service and market conditions.

(2) Includes 202,000 and 173,750 restricted stock awards issued in 2012 and 2013, which vest upon satisfaction of certain service and market conditions. The Company issues restricted stock awards and restricted stock units to employees for future services and in connection with acquisitions. Restricted stock awards and restricted stock unit grants are generally measured at fair value on the date of grant based on the number of awards granted and the quoted price of the Company's common stock. Restricted shares issued are accounted for under FASB ASC 718 using the straight-line method net of estimated forfeitures.

As of December 31, 2013, there was \$12.6 million of total restricted stock compensation expense related to non-vested awards not yet recognized, which is expected to be recognized over a weighted average period of 1.9 years.

In the second quarter of 2012, vesting of approximately 195,000 restricted shares were fully accelerated in connection with a separation agreement. In the fourth quarter of 2012, 1,050,000 restricted shares that would otherwise have vested on January 1, 2013 were vested on December 31, 2012.

During 2012 and 2013, the Company repurchased 391,000 and 220,000 shares, respectively, from certain executives for minimum withholding taxes on 1,255,000 and 1,031,000 restricted stock award vests, respectively. The number of shares repurchased was based on the value on the vesting date of the restricted stock awards equivalent to the value of the executives' minimum withholding taxes of \$1.6 million and \$1.8 million for 2012 and 2013, respectively. The Company then remitted cash to the appropriate taxing authorities. The payments are reflected as a financing activity within the consolidated statement of cash flows when paid. The payments had the effect of share repurchases by the Company as they reduced the number of shares that would have otherwise been issued on the vesting date and were recorded as a reduction of additional paid in capital.





---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

***(c) Employee Stock Purchase Plan***

On February 15, 2004, the Company's board of directors and stockholders approved the 2004 Employee Stock Purchase Plan ( 2004 ESPP ), which became effective on March 30, 2004. The Company authorized an aggregate of 300,000 shares of Class B common stock for issuance under the plan to participating employees.

In December 2005, the compensation committee of the Company's board of directors amended the 2004 ESPP to provide that effective January 1, 2006 eligible participants may purchase the Company's Class B common stock under the purchase plan at a price equal to 95% of the fair value on the last day of an offering period. During the year ended December 31, 2011, 3,637 shares were purchased at prices ranging from \$5.94 to \$8.44 per share. During the year ended December 31, 2012, 9,817 shares were purchased at prices ranging from \$3.43 to \$4.24 per share. During the year ended December 31, 2013, 11,511 shares were purchased at prices ranging from \$4.00 to \$8.22 per share. The 2004 ESPP, as amended, expired on December 31, 2013.

On March 8, 2013, the Company's board of directors adopted and in May 2013 the stockholders approved the 2014 Employee Stock Purchase Plan ( 2014 ESPP ), which became effective on January 1, 2014. The Company authorized an aggregate of 225,000 shares of Class B common stock for issuance under the plan to participating employees. The 2014 ESPP provided eligible employees the opportunity to purchase the Company's Class B common stock at a price equal to 95% of the closing price on the last business day of each purchase periods. The 2014 ESPP permits eligible employees to purchase amounts up to 15% of their compensation in purchase period, and no employee is permitted to purchase stock worth more than \$25,000 in any calendar year, valued as of the first day of each purchase period.

**(7) Contingencies**

The Company is involved in legal and administrative proceedings and claims of various types from time to time. While any litigation contains an element of uncertainty, the Company is not aware of any legal proceedings or claims which are pending that the Company believes, based on current knowledge, will have, individually or taken together, a material adverse effect on the Company's financial condition or results of operations or liquidity.

In some agreements to which we are a party, we have agreed to indemnification provisions of varying scope and terms with advertisers, vendors and other parties with respect to certain matters, including, but not limited to, losses arising out of the Company's breach of agreements or representations and warranties made by the Company, services to be provided by the Company and intellectual property infringement claims made by third parties. As a result of these provisions, we may from time to time provide certain levels of financial support to our contract parties to seek to minimize the impact of any associated litigation in which they may be involved. To date, there have been no known events or circumstances that have resulted in any material costs related to these indemnification provisions and no liabilities therefore have been recorded in the accompanying consolidated financial statements. However, the maximum potential amount of the future payments we could be required to make under these indemnification provisions could be material.

**(8) 401(k) Savings Plan**

The Company has a Retirement/Savings Plan (401(k) Plan) under Section 401(k) of the Internal Revenue Code which covers those employees that meet eligibility requirements. Eligible employees may contribute up to the Internal Revenue Code prescribed maximum amounts. During 2011, the Company elected to match a portion of the employee contributions up to a defined maximum. No cash matching contributions were made in 2011. In 2012 and 2013, cash contributions were made in the amount of \$67,000 and \$186,000, respectively.

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****(9) Acquisition**

On April 7, 2011, the Company acquired 100% of the stock of Jingle, a provider of mobile voice search performance advertising and technology solutions in North America for the following consideration:

Approximately \$15.8 million in cash, net of cash acquired, and 1,019,103 shares of the Company's Class B common stock paid at closing; and

Future consideration of (i) \$17.6 million, net of certain working capital adjustments, on the first annual anniversary of the closing, and (ii) \$18.0 million on the 18th month anniversary of closing, with the future consideration payable in either cash or shares of the Company's Class B common stock or some combination to be determined by the Company. In April 2012 and October 2012, the Company paid approximately \$16.9 million and \$17.9 million in cash, net of certain working capital and other adjustments, respectively.

Following the closing, the Company issued 462,247 shares of restricted stock at an aggregate value of approximately \$3.3 million to employees of Jingle, subject to vesting for up to four years.

The Company accounted for the Jingle acquisition as a business combination. As a result of the acquisition, the Company added additional sources of mobile distribution to its call advertising network. The Company has progressed in its integration of Jingle's operations, including sales activities, and accordingly, revenues and earnings of the acquired operations are not readily separable.

The fair value of the shares of Class B common stock issued as part of the consideration paid was valued at \$7.6 million using the Company's closing stock price of \$7.46 per share at the acquisition date. Acquisition related costs of approximately \$1.9 million for 2011 were primarily for professional fees to perform due diligence, historical audits and other procedures associated with the acquisition. Of the \$1.9 million of acquisition related costs in 2011, we recognized approximately \$372,000 for the future obligations of non-cancelable lease and other costs related to the Jingle office. The portion related to the non-cancelable lease is based on estimates of vacancy period and sublease income. In March 2012, the Company arranged for the future sublease of the Jingle office space and revised its original estimates which resulted in a \$132,000 benefit recorded in acquisition and separation related costs in the consolidated statements of operations. The actual vacancy periods may differ from these estimates, and sublease income, if any, may not materialize. Accordingly, these estimates may be adjusted in future periods.

In connection with the acquisition, the Company acquired federal net operating loss carryforwards ( NOL ). Where there is a change in ownership within the meaning of Section 382 of the Internal Revenue Code, the acquired federal net operating loss carryforwards are subject to an annual limitation. The Company believes that such an ownership change had occurred at Jingle, and that the utilization of the carryforwards is limited such that the majority of the NOL carryforwards will never be utilized. Accordingly, the Company recorded approximately \$7.0 million of NOL carryforwards. In 2011, the Company utilized approximately \$2.6 million.

A summary of the consideration for the acquisition is as follows (in thousands):

Cash	\$ 16,563
Stock issued	7,603
Future consideration paid	34,695

Total

\$ 58,861

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

The following summarizes the allocation of the fair value of the assets acquired and the liabilities assumed at December 31, 2011 (in thousands):

Cash acquired	\$ 761
Accounts receivable	4,740
Deferred tax assets	2,538
Other current assets	62
Property and equipment	206
Other non-current assets	148
Intangible assets	11,966
Goodwill	47,290
<b>Total assets acquired</b>	<b>67,711</b>
Current liabilities	(5,512)
Deferred tax liabilities	(3,246)
Other non-current liabilities	(92)
<b>Total liabilities assumed</b>	<b>(8,850)</b>
<b>Net assets acquired</b>	<b>\$ 58,861</b>

The acquired intangible assets of approximately \$12.0 million consist primarily of customer and partner relationships, technology, trademarks and patents which will be amortized over 12 to 36 months (weighted average of 2.4 years) using the straight line method. The goodwill and acquired intangible assets will not be deductible for federal tax purposes.

The following unaudited pro forma financial information summarizes the combined results of operations of the Company and Jingle and is based on the historical results of operations of the Company and Jingle. The pro forma information reflects the results of operations of the Company as if the acquisition of Jingle had taken place on January 1, 2010. The unaudited pro forma financial information for the year ended December 31, 2011 combine the historical results of operations for the Company for the year ended December 31, 2011 and Jingle's historical results of operations during the pre-acquisition period from January 1, 2011 to April 7, 2011. The results of operations for Jingle for the year ended December 31, 2012 and 2013 are incorporated in the results of operations for the Company for the year ended December 31, 2012. The pro forma information includes adjustments for amortization of intangible assets, intercompany activity and accretion of interest expense related to the future consideration. The unaudited pro forma financial information is provided for information purposes only and is not necessarily indicative of the combined results that would have occurred had the acquisition taken place on the dates indicated, nor is it necessarily indicative of results that may occur in the future.

(in thousands)

	<b>2011</b>
Revenue	\$ 144,517
Net income (loss) from continuing operations	1,626
Net income (loss) applicable to common stockholders	1,570

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****(10) Intangible Assets from Acquisitions**

Intangible assets from acquisitions consisted of the following (in thousands):

	As of December 31, 2012		
	Gross Carrying Amount (1)	Accumulated Amortization (1)	Net
Advertiser relationship	\$ 3,070	\$ (2,125)	\$ 945
Distribution partner relationship	4,830	(2,787)	2,043
Acquired technology	2,760	(2,388)	372
	\$ 10,660	\$ (7,300)	\$ 3,360

	As of December 31, 2013		
	Gross Carrying Amount (1)	Accumulated Amortization (1)	Net
Distribution partner relationship	4,830	(4,396)	434
	\$ 4,830	\$ (4,396)	\$ 434

(1) Excludes the original cost and accumulated amortization of fully-amortized intangible assets which were \$82.1 million and \$87.7 million at December 31, 2012 and 2013, respectively.

Amortizable intangible assets are amortized on a straight-line basis over their useful lives. Advertiser relationships, distribution partner relationships and acquired technology have weighted average useful life from date of purchase of 2.5 years, 3.0 years, and 2.0 years, respectively. Aggregate amortization expense incurred by the Company for the years ended December 31, 2011, 2012 and 2013, was approximately \$5.5 million, \$4.7 million and \$2.9 million, respectively. Based upon the current amount of acquired intangible assets subject to amortization, the estimated amortization expense for the next four years is as follows: \$434,000 in 2014 and \$0 thereafter.

**(11) Goodwill**

Changes in the carrying amount of goodwill for the years ended December 31, 2012 and 2013 are as follows (in thousands):

	Call Driven	Archeo	Total
Balance as of December 31, 2011			82,644
Jingle acquisition			(53)
Other			(37)
Goodwill allocation between segments	63,305	19,249	
Impairment		(16,739)	(16,739)

Edgar Filing: MARCHEX INC - Form 10-K

Balance as of December 31, 2012	63,305	2,510	65,815
Sales of certain pay-per-click advertising assets		(136)	(136)
Balance as of December 31, 2013	\$ 63,305	\$ 2,374	\$ 65,679

In 2012, the decrease in goodwill was primarily related to the impairment loss recognized during the fourth quarter within the Archeo segment as discussed further below. During the fourth quarter of 2012, the Company announced its intention to pursue a spin-off of Archeo and the corresponding organizational changes resulted in a change to the Company's reportable operating segments and reporting units for purposes of assessing potential

---

**Table of Contents**

**MARCHEX, INC. AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

impairment of goodwill. The Company's reporting units are consistent with its reportable operating segments identified in *Note 13 Segment Reporting and Geographic Information*. Prior to the fourth quarter of 2012, the Company operated in a single operating segment consisting of a single reporting unit. In connection with the change in reportable operating segments and reporting units, the Company allocated approximately \$19.2 million and \$63.3 million of goodwill to its Archeo and Call-driven segments, respectively.

In 2013, the decrease in goodwill of \$136,000 related to the sale of certain assets related to the Company's pay-per-click advertising services in July 2013. See *Note 14. Discontinued Operations* for further discussion.

Goodwill at December 31, 2011 is net of the 2008 impairment charge of \$169.3 million. Goodwill at December 31, 2012 is net of the accumulated impairment charges from 2008 and 2012 of \$186.0 million.

The Company reviews goodwill for impairment annually on November 30 and whenever events or changes in circumstances indicate the carrying value of goodwill may not be recoverable. When evaluating goodwill for impairment, we may first perform a qualitative assessment to determine if the fair value of the reporting unit is more likely than not greater than its carrying amount. The Company performed this qualitative assessment in the fourth quarter of 2013 and determined that the fair value of each reporting unit is more likely than not greater than the carrying amount.

In 2012, the Company initiated its annual goodwill impairment analysis in the fourth quarter and concluded that the fair value was below the carrying value for the Archeo reporting unit and recognized an impairment loss of \$16.7 million including \$902,000 related to discontinued operations. The estimated fair value of the Archeo reporting unit was based on estimates of future operating results, discounted cash flows and other market-based factors. The goodwill impairment recorded within the Archeo reporting unit resulted from the newly associated amounts of goodwill allocated upon the commencement of the reporting unit designation in the fourth quarter, and the operating results including lower projected revenue growth rates and profitability levels compared to historical results. The lower projected operating results reflect changes in assumptions related to organic revenue growth rates, market trends, business mix, cost structure, and other expectations about the anticipated short-term and long-term operating results of the Archeo reporting unit.

The testing of goodwill and other intangible assets for impairment requires the Company to make significant estimates about its future performance and cash flows, as well as other assumptions. These estimates can be affected by numerous factors, including changes in economic, industry or market conditions, changes in business operations, changes in competition or changes in the share price of the Company's common stock and market capitalization. Significant and sustained declines in the Company's stock price and market capitalization, a significant decline in its expected future cash flows or a significant adverse change in the Company's business climate, among other factors, could result in the need to perform an impairment analysis in future interim periods. The Company cannot accurately predict the amount and timing of any future impairment of goodwill or other intangible assets. Should the value of goodwill or other intangible assets become impaired, the Company would record an impairment charge, which could have an adverse effect on its financial condition and results of operations.

The current business environment is subject to evolving market conditions and requires significant management judgment to interpret the potential impact to our assumptions. To the extent that changes in the current business environment impact the Company's ability to achieve levels of forecasted operating results and cash flows, or should other events occur indicating the remaining carrying value of its assets might be impaired, the Company would test its goodwill and intangible assets for impairment and may recognize an additional impairment loss.



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****(12) Intangible and other assets, net**

Intangible and other assets, net consisted of the following (in thousands):

	As of December 31,	
	2012	2013
Internet domain names	\$ 14,910	\$ 14,514
Less accumulated amortization	(14,590)	(14,376)
<b>Internet domain names, net</b>	<b>320</b>	<b>138</b>
Other assets:		
Registration fees, net	9	12
Other	282	334
<b>Total intangibles and other assets, net</b>	<b>\$ 611</b>	<b>\$ 484</b>

The Company capitalizes costs incurred to acquire domain names or URLs, which include the initial registration fees, to other intangible assets which excludes intangible assets acquired through business combinations. The capitalized costs are amortized over the expected useful life of the domain names on a straight-line basis.

As of December 31, 2012, the net carrying value of Internet domains names related to domain names held for use. On September 10, 2013, the Company launched its Domains Marketplace, which provides domain names available for sale and initiated plans to facilitate the active buying and transacting of domain names. Domain name sales occurring after this launch have been recognized as revenue in the consolidated financial statements. The net carrying value of Internet domain names as of December 31, 2013 related to both domain names held for use and available for sale.

The Company also capitalizes costs incurred to renew or extend the term of the domain names or URLs to prepaid expenses and other current assets or registration fees, net. The capitalized costs are amortized over the renewal or extended period on a straight-line basis. The total amount of costs incurred for the year ended December 31, 2013 to renew or extend the term for domain names was \$2.7 million. The weighted average renewal period for registration fees as of December 31, 2013 was approximately 1.0 year.

Amortization expense for Internet domain names for the years ended December 31, 2011, 2012 and 2013, was approximately \$1.2 million, \$520,000 and \$336,000 respectively.

Based upon the current amount of domains subject to amortization, the estimated expense for the next five years is as follows: \$138,000 in 2014 and \$0 thereafter.

**(13) Segment Reporting and Geographic Information**

Operating segments are revenue-producing components of the enterprise for which separate financial information is produced internally for the Company's management. During the fourth quarter of 2012, the Company changed its internal reporting available to its chief operating decision maker ( CODM ) for evaluating segment performance and allocating resources due to its intention to spin off Archeo and revised segment disclosures accordingly. The reporting disaggregates the Company's operations into the Call-driven and Archeo segments, and represented a change in the Company's reportable operating segments. Prior to the fourth quarter of 2012, the Company operated in a single operating segment.



**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

In July 2013, the Company sold certain assets related to Archeo's pay-per-click advertising services. As a result, the operating results related to these certain pay per click assets are shown as discontinued operations, net of tax in the consolidated statements of operations for all periods presented and are excluded from segment reporting. See *Note. 14. Discontinued Operations* for further discussion. In September 2013, the Company announced it will no longer pursue the spinoff of Archeo and will operate Archeo as a distinct division and changed its segment reporting to reflect the reallocation of its general corporate overhead expenses to the Call-driven segment. The Company revised its segment reporting to reflect changes in how the CODM internally measures segment performance. The tables below reflect these reclassifications to conform to the current presentation.

The Company's Call-driven segment comprises its performance-based advertising business focused on driving phone calls. The Archeo segment comprises the Company's click-based advertising and Internet domain name businesses. Segment expenses include both direct costs incurred by the segment businesses as well as an allocation of certain shared and indirect costs. Segment expenses exclude the following: stock-based compensation, amortization of intangible assets from acquisitions, acquisition and separation related costs, and other income (expense).

A measure of segment assets is not currently provided to the Company's CODM and has therefore not been disclosed. The change in the Company's operating segments during the fourth quarter of 2012 also resulted in a change in the Company's reporting units for purposes of assessment potential impairment of goodwill. Goodwill was reallocated to the Company's two reporting units based on their respective fair values and the Company recognized an impairment of goodwill of \$15.8 million related to its Archeo segment. The carrying amount of goodwill by operating segment at December 31, 2013 was approximately \$63.3 million and \$2.4 million for Call-driven and Archeo, respectively.

Selected segment information (in thousands):

	Year ended December 31, 2013		
	Call-driven	Archeo	Total
Revenue	\$ 135,126	\$ 17,424	\$ 152,550
Operating expenses	128,829	11,705	140,534
Gain on sales of intangible assets		3,774	3,774
Segment profit	\$ 6,297	\$ 9,493	\$ 15,790
Less reconciling items:			
Stock based compensation			9,237
Amortization of intangible assets from acquisitions			2,926
Acquisition and separation related costs			878
Interest expense and other, net			37
Income from continuing operations before provision for income taxes			\$ 2,712

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)**

	Year ended December 31, 2012		
	Call-driven	Archeo	Total
Revenue	\$ 111,886	\$ 20,908	\$ 132,794
Operating expenses	106,795	12,582	119,377
Gain on sales of intangible assets		6,296	6,296
Segment profit	\$ 5,091	\$ 14,622	\$ 19,713
Less reconciling items:			
Stock based compensation			15,638
Impairment of goodwill			15,837
Amortization of intangible assets from acquisitions			4,728
Acquisition and separation related costs			753
Interest expense and other, net			449
Loss from continuing operations before provision for income taxes			\$ (17,692)

	Year ended December 31, 2011		
	Call-driven	Archeo	Total
Revenue	\$ 101,830	\$ 36,896	\$ 138,726
Operating expenses	97,270	22,740	120,010
Gain on sales of intangible assets		9,421	9,421
Segment profit	\$ 4,560	\$ 23,577	\$ 28,137
Less reconciling items:			
Stock based compensation			15,068
Amortization of intangible assets from acquisitions			5,455
Acquisition and separation related costs			1,890
Interest expense and other, net			458
Income from continuing operations before provision for income taxes			\$ 5,266

Revenues from advertisers by geographical areas are tracked on the basis of the location of the advertiser. The vast majority of the Company's revenue and accounts receivable are derived from domestic sales to advertisers engaged in various mobile, online and other activities.

Revenues by geographic region are as follows (in percentages):

	Years ended December 31,		
	2011	2012	2013
United States	94%	94%	95%
Canada	6%	6%	5%
Other countries	*	*	*
	100%	100%	100%

\* Less than 1% of revenue

**Table of Contents****MARCHEX, INC. AND SUBSIDIARIES****Notes to Consolidated Financial Statements (Continued)****(14) Discontinued Operations**

On July 19, 2013, we completed the sale of certain pay-per-click advertising services to an unrelated third party. Accordingly, we have presented the results of operations of these certain pay-per-click assets in the consolidated financial statements as discontinued operations, net of tax, for the current and all historical periods. The operating results for the discontinued operations were as follows (in thousands):

	Years ended December 31,		
	2011	2012	2013
Revenue	\$ 8,000	\$ 5,512	\$ 3,185
Income (loss) before provision for income taxes	306	(947)	(111)
Income tax expense (benefit)	102	(9)	(41)
Income (loss) from discontinued operations, net of tax	\$ 204	\$ (938)	\$ (70)
Gain on sale of discontinued operations			1,492
Income tax expense (benefit)			562
Gain on sale of discontinued operations, net of tax	\$	\$	\$ 930
Discontinued operations, net of tax	\$ 204	\$ (938)	860

The net cash proceeds from the sale were approximately \$1.1 million. The net carrying value of liabilities assumed net of goodwill associated with the component sold was approximately \$435,000 as of July 19, 2013, resulting in a net gain of \$1.5 million from the sale. The sale includes contingent earn-out consideration payments that depend upon the achievement of certain thresholds and will be recognized as income when received.

---

**Table of Contents**

**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**

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our chief executive officer and our chief financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). Based on this evaluation, our chief executive officer and our chief financial officer have concluded that, as of the date of the evaluation, our disclosure controls and procedures were effective.

**Management's Report on Internal Control Over Financial Reporting**

*(a) Management's report on internal control over financial reporting*

Management of Marchex, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in the Securities Exchange Act of 1934 Rule 13a-15(f). Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2013 as required by the Securities Exchange Act of 1934 Rule 13a-15(c). In making this assessment, we used the criteria set forth in the framework in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in Internal Control-Integrated Framework (1992), our management concluded that our internal control over financial reporting was effective as of December 31, 2013.

*(b) Report of the registered public accounting firm*

The report of KPMG LLP, the Company's independent registered public accounting firm, on the effectiveness of the Company's internal control over financial reporting is included in this Annual Report on Form 10-K.

*(c) Changes in Internal Control over Financial Reporting*

During the quarter ended December 31, 2013, no change was made to our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Limitations on the Effectiveness of Controls**

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, cannot provide absolute assurance of achieving the desired control objectives.

In addition, because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

**ITEM 9B. OTHER INFORMATION.**

None.

**Table of Contents**

**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.**

The information required by this item is incorporated herein by reference to the Company's definitive proxy statement relating to the 2014 annual meeting of stockholders (the 2014 Proxy Statement), which the Company intends to file with the Securities and Exchange Commission within 120 days of the Company's fiscal year ended December 31, 2013.

Our Code of Ethics for our Chief Executive Officer, Chief Financial Officer and Senior Financial Officers is available on our web site, [www.marchex.com](http://www.marchex.com), by clicking "Investors" and then "Corporate Governance".

**ITEM 11. EXECUTIVE COMPENSATION.**

The information required under this item may be found in the 2014 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 under this item may be found in the 2014 Proxy Statement and is incorporated herein by reference.

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

The information required under this item may be found in the 2014 Proxy Statement and is incorporated herein by reference.

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES.**

The information required under this item may be found in the 2014 Proxy Statement and is incorporated herein by reference.



**Table of Contents**

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES.**

1. The following financial statements are included in Part II, Item 8 of this Form 10-K:

Reports of Independent Registered Public Accounting Firm;

Consolidated Balance Sheets as of December 31, 2012 and 2013;

Consolidated Statements of Operations for the years ended December 31, 2011, 2012 and 2013;

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2011, 2012 and 2013;

Consolidated Statements of Cash Flow for the years ended December 31, 2011, 2012 and 2013; and

Notes to Consolidated Financial Statements.

2. Financial Statement Schedules

Financial statement schedules are omitted because they are not required or are not applicable, or the required information is provided in the consolidated financial statements or notes described in Item 15 (a) (1) above.

3. We have filed, or incorporated into this Form 10-K by reference, the exhibits listed on the accompanying Exhibit Index immediately following the signature page of this Form 10-K.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized in the City of Seattle, State of Washington on March 3, 2014.

MARCHEX, INC.

By: /s/ MICHAEL M. MILLER  
Michael M. Miller

**Senior VP Accounting and Corporate Controller**

**(Principal Accounting Officer)**

**POWER OF ATTORNEY**

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Russell C. Horowitz and Michael A. Arends, jointly and severally, as his or her attorneys-in-fact, each with the full power of substitution, for him or her, in any and all capacities, to sign any amendment to this Annual Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting to said attorneys-in-fact, 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 to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact or any of them, or their or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Annual Report on Form 10-K has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Signature	Date
/s/ RUSSELL C. HOROWITZ	March 3, 2014
<b>Russell C. Horowitz</b>	
<b>Chairman and Chief Executive Officer</b>	
<b>(Principal Executive Officer)</b>	
/s/ MICHAEL A. ARENDS	March 3, 2014
<b>Michael A. Arends</b>	
<b>Chief Financial Officer</b>	
<b>(Principal Financial Officer)</b>	
/s/ DENNIS CLINE	March 3, 2014
<b>Dennis Cline</b>	
<b>Director</b>	
/s/ ANNE DEVEREUX MILLS	March 3, 2014

**Anne Devereux Mills**

**Director**

**Table of Contents**

<b>Signature</b>	<b>Date</b>
/s/ NICOLAS J. HANAUER	March 3, 2014
<b>Nicolas J. Hanauer</b>	
<b>Vice Chairman and Director</b>	
/s/ M. WAYNE WISEHART	March 3, 2014
<b>M. Wayne Wishart</b>	
<b>Director</b>	

**Table of Contents****EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Description of Document</b>
2.1	Agreement and Plan of Merger, dated as of February 19, 2003, by and among the Registrant, Marchex Acquisition Corporation, eFamily.com, Inc., the Shareholders of eFamily.com, Inc., ah-ha.com, Inc. and Paul J. Brockbank, as Stockholder Representative (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on December 11, 2003 and incorporated herein by reference).
2.2	Agreement and Plan of Merger, dated as of October 1, 2003, by and among the Registrant, Sitewise Acquisition Corporation, TrafficLeader, Inc., the Shareholders of TrafficLeader, Inc. and Gerald Wiant, as Shareholder Representative (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on December 11, 2003 and incorporated herein by reference).
2.3	Agreement and Plan of Merger, dated as of July 21, 2004, by and among the Registrant, Project TPS, Inc., goClick.com, Inc. and the Sole Stockholder of goClick.com, Inc. (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2009 filed with the SEC on March 10, 2010 and incorporated herein by reference).
2.4	Asset Purchase Agreement, dated as of November 19, 2004, by and among the Registrant, Name Development Ltd. and the Sole Stockholder of Name Development Ltd. (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-121213) filed with the SEC on December 13, 2004 and incorporated herein by reference).
2.5	Asset Purchase Agreement, dated as of April 26, 2005, by and among the Registrant, Pike Street Industries, Inc. and the holders of all the issued and outstanding capital stock of Pike Street Industries, Inc. (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC on March 14, 2011 and incorporated herein by reference).
2.6	Agreement and Plan of Merger, dated as of July 27, 2005, by and among the Registrant, Einstein Holdings I, Inc., Einstein Holdings 2, LLC, IndustryBrains, Inc., the primary shareholders of IndustryBrains, Inc. and with respect to Articles II, VII and XII only, Eric Matlick as shareholder representative (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC on March 14, 2011 and incorporated herein by reference).
2.7	Asset Purchase Agreement, dated as of May 1, 2006, by and among the Registrant, MDNH, Inc., AreaConnect LLC and the holder of all of the issued and outstanding ownership interests of AreaConnect LLC (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 12, 2012 and incorporated herein by reference).
2.8	Asset Purchase Agreement, dated as of May 26, 2006, by and among the Registrant, MDNH, Inc., OpenList, Inc., Brian Harriman, the stockholders of OpenList, Inc., and with respect to the Articles VI and XI only, Brad Gerstner as stockholder representative (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 12, 2012 and incorporated herein by reference).
2.9	Agreement and Plan of Merger, dated as of August 9, 2007, by and among Registrant, VoiceStar, Inc., and the Shareholders of VoiceStar, Inc. (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the SEC on March 12, 2013 and incorporated herein by reference).

**Table of Contents**

<b>Exhibit Number</b>	<b>Description of Document</b>
+2.10	Agreement and Plan of Merger, dated as of April 7, 2011, by and among the Registrant, Marchex Acquisition Corporation, Jingle Networks, Inc. and with respect to Articles II, V and VIII only, Chip Hazard as the Stockholder Representative (Filed with the Registrant's Amendment No. 1 to the Registration Statement on Form S-3 (No. 333-174016) filed with the SEC on June 29, 2011 and incorporated herein by reference).
3.1	Certificate of Incorporation of the Registrant (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on December 11, 2003 and incorporated herein by reference).
3.2	Amended and Restated Certificate of Incorporation of the Registrant (Filed with the Registrant's Amendment No. 2 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on March 19, 2004 and incorporated herein by reference).
3.3	By-laws of the Registrant (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on December 11, 2003 and incorporated herein by reference).
3.4	Amended and Restated By-Laws of the Registrant . (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the SEC on March 12, 2013 and incorporated herein by reference).
4.1	Specimen stock certificate representing shares of Class B Common Stock of the Registrant (Filed with the Registrant's Amendment No. 3 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on March 30, 2004 and incorporated herein by reference).
*10.1	Amended and Restated 2003 Stock Incentive Plan (Filed with the Registrant's Amendment No. 2 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on March 19, 2004 and incorporated herein by reference).
*10.2	Executive Employment Agreement, dated as of January 17, 2003, by and between Russell C. Horowitz and the Registrant (Filed with the Registrant's Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on December 11, 2003 and incorporated herein by reference).
*10.3	Executive Employment Agreement, dated as of May 1, 2003, by and between Michael A. Arends and the Registrant (Filed with the Registrant's Amendment No. 1 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on February 19, 2004 and incorporated herein by reference).
*10.4	2004 Employee Stock Purchase Plan (Filed with the Registrant's Amendment No. 1 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on February 19, 2004 and incorporated herein by reference).
10.5	Representative Director and Officer Indemnification Agreement, dated as of February 4, 2004, by and between Russell C. Horowitz and the Registrant (Filed with the Registrant's Amendment No. 2 to the Registration Statement on Form SB-2 (No. 333-111096) filed with the SEC on March 19, 2004 and incorporated herein by reference).
+10.6	License Agreement, effective February 14, 2005, by and between Overture Services, Inc. and Registrant (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC on March 14, 2011 and incorporated herein by reference).
*10.7	2004 Employee Stock Purchase Plan, as amended on December 8, 2005 (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC on March 14, 2011 and incorporated herein by reference).

**Table of Contents**

<b>Exhibit Number</b>	<b>Description of Document</b>
*10.8	Marchex, Inc. Annual Incentive Plan. (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 12, 2012 and incorporated herein by reference).
*10.9	Form of Restricted Stock Agreement (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the SEC on March 12, 2013 and incorporated herein by reference).
*10.10	Form of Retention Agreement. (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 12, 2012 and incorporated herein by reference).
+10.11	Master Services and License Agreement dated as of October 1, 2007, by and between MDNH, Inc. and YellowPages.com LLC (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the SEC on March 12, 2013 and incorporated herein by reference).
+10.12	Credit Agreement dated as of April 1, 2008, by and between the Registrant, the several banks and other financial institutions or entities from time to time parties to the agreement, and U.S. Bank National Association, as administrative agent.
*10.13	Form of Retention Agreement Amendment (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.14	Revised Form of Retention Agreement (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.15	Form of Restricted Stock Agreement Amendment (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.16	First Amendment to Executive Employment Agreement effective as of May 8, 2009, by and between Michael A. Arends and the Registrant (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.17	Revised Form of Executive Restricted Stock Agreement (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.18	Form of Director Restricted Stock Agreement (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
10.19	Amended and Restated Lease effective as of June 5, 2009, between 520 Pike Street, Inc. and the Registrant (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 7, 2009 and incorporated herein by reference).
*10.20	Form of Executive Officer Stock Option Agreement (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on November 9, 2009 and incorporated herein by reference).
+10.21	Amendment No. 1 to Master Services and License Agreement effective as of April 30, 2010, by the between MDNH, Inc. and YellowPages.com LLC d/b/a AT&T Interactive and related Project Addendum No. 1, effective as of January 1, 2009, as amended (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).

**Table of Contents**

Exhibit Number	Description of Document
*10.22	Form of Notice of Grant of Executive Officer Stock Option (Performance-Based) (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.23	Form of Notice of Grant of Executive Officer Stock Option (Time-Based) (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.24	Form of Notice of Grant of Executive Officer Restricted Stock Units (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.25	Form of Executive Officer Restricted Stock Agreement (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.26	Form of Executive Officer Restricted Stock Units Agreement (2003 Amended and Restated Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
+10.27	Amendments No. 1, 2 and 3 to YAHOO! Publisher Network Service Order, effective as of September 25, 2007, August 1, 2008 and June 1, 2010 respectively, by and between Yahoo! Inc., as successor in interest to Overture Services, Inc., and Yahoo! Sarl, as successor in interest to Overture Search Services (Ireland) Limited, MDNH, Inc. and MDNH International Ltd. (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.28	Amendment to the Marchex, Inc. 2003 Amended and Restated Stock Incentive Plan (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 6, 2010 and incorporated herein by reference).
*10.29	Marchex, Inc. Amended and Restated Annual Incentive Plan (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed with the SEC on March 14, 2011 and incorporated herein by reference).
10.30	First Amendment to the Credit Agreement made and entered into as of March 1, 2011, by and among the Registrant, the several banks and other financial institutions or entities from time to time parties to the agreement, and U.S. Bank National Association, as administrative agent (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 12, 2012 and incorporated herein by reference).
*10.31	Marchex, Inc. 2012 Stock Incentive Plan (Filed as Appendix A to the Registrant's Definitive Proxy Statement on Form 14A filed with the SEC on April 9, 2012 and incorporated herein by reference).
*10.32	Marchex, Inc. 2004 Employee Stock Purchase Plan, as amended on December 20, 2012 (Filed with the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012 filed with the SEC on March 12, 2013 and incorporated herein by reference).
*10.33	Marchex, Inc. 2014 Employee Stock Purchase Plan, as amended on December 20, 2012 (Filed the as Appendix A to the Registrant's Definitive Proxy Statement on Form 14A filed with the SEC on April 3, 2013 and incorporated herein by reference).
*10.34	Form of Incentive Stock Option Notice and Agreement (2012 Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2013 and incorporated herein by reference).



**Table of Contents**

Exhibit Number	Description of Document
*10.35	Form of Nonstatutory Stock Option Notice and Agreement (2012 Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2013 and incorporated herein by reference).
*10.36	Form of Restricted Stock Agreement (2012 Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2013 and incorporated herein by reference).
*10.37	Form of Restricted Stock Units Notice and Agreement (2012 Stock Incentive Plan) (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2013 and incorporated herein by reference).
(+)10.38	Amendment No. 1 to Master Services and License Agreement, effective as of July 1, 2013, by and between Marchex Sales LLC, a Delaware limited liability company, and YellowPages.com LLC, a Delaware limited liability company (Filed with the Registrant's Quarterly Report on Form 10-Q filed with the SEC on November 12, 2013 and incorporated herein by reference).
*10.39	Form of Indemnity Agreement (Section 16 Executive Officers and Directors) (Filed with the Registrant's Current Report on Form 8-K filed with the SEC on May 7, 2013 and incorporated herein by reference).
10.40	Second Amendment to the Credit Agreement made and entered into as of February 24, 2014, by and among the Registrant, the several banks and other financial institutions or entities from time to time parties to the agreement, and U.S. Bank National Association, as administrative agent.
21.1	Subsidiaries of the Registrant.
23.1	Consent of Independent Registered Public Accounting Firm.
24.1	Power of Attorney (incorporated herein by reference to the signature page of the Annual Report on Form 10-K)
31(i)	Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31(ii)	Certification of Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE	XBRL Taxonomy Presentation Linkbase Document.

\* Management contract or compensatory plan or arrangement.

(+) Certain information in this agreement has been omitted and filed separately with the Securities and Exchange Commission. Confidential treatment has been granted with respect to the omitted portions.

Filed herewith.

Furnished herewith.

Refiled herewith pursuant to Regulation S-K Item 10.