MARCHEX INC
Form 10-Q
November 07, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016

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	35-2194038
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

520 Pike Street, Suite 2000

Seattle, Washington 98101

(Address of principal executive offices)

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

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

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

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

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

Class	Outstanding at November 3, 2016
Class A common stock, par value $.01 per share	5,056,136
Class B common stock, par value $.01 per share	38,102,444

Marchex, Inc.

Form 10-Q

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Part I—Financial Information

Item 1. Condensed Consolidated Financial Statements

MARCHEX, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(in thousands)

(unaudited)

	December 31, 2015	September 30, 2016
Assets		
Current assets:		
Cash and cash equivalents	$109,155	$105,275
Accounts receivable, net	24,621	21,579
Prepaid expenses and other current assets	1,784	1,995
Refundable taxes	127	117
Total current assets	135,687	128,966
Property and equipment, net	5,778	3,913
Intangible and other assets, net	222	220
Goodwill	63,305	—
Total assets	$204,992	$133,099
Liabilities and Stockholders’ Equity		
Current liabilities:		
Accounts payable	$9,460	$7,960
Accrued expenses and other current liabilities	6,712	8,300
Deferred revenue	692	362
Total current liabilities	16,864	16,622
Other non-current liabilities	662	266
Total liabilities	17,526	16,888
Stockholders’ equity:		
Class A common stock	55	55
Class B common stock	368	381
Treasury stock	(238)	(2)
Additional paid-in capital	350,799	357,617
Accumulated deficit	(163,518)	(241,840)
Total stockholders’ equity	187,466	116,211
Total liabilities and stockholders’ equity	$204,992	$133,099

See accompanying Notes to Condensed Consolidated Financial Statements.

MARCHEX, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations

(in thousands, except per share amounts)

(unaudited)

	Nine Months Ended		Three Months Ended	
	September 30,		September 30,	
	2015	2016	2015	2016
Revenue	$108,113	$101,146	$36,852	$30,749
Expenses:				
Service costs	59,166	60,964	20,003	18,505
Sales and marketing	11,969	16,733	4,266	5,562
Product development	23,608	21,859	7,769	6,832
General and administrative	14,925	15,815	4,721	5,320
Acquisition and disposition related costs	199	662	81	354
Total operating expenses	109,867	116,033	36,840	36,573
Impairment of goodwill	—	(63,305)	—	—
Income (loss) from operations	(1,754)	(78,192)	12	(5,824)
Other expense:				
Interest and line of credit expense	(48)	(41)	(11)	(3)
Other, net	(4)	(49)	(1)	(12)
Total other expense	(52)	(90)	(12)	(15)
Income (loss) from continuing operations before provision for income taxes	(1,806)	(78,282)	0	(5,839)
Income tax expense	11	40	191	15
Net loss from continuing operations	(1,817)	(78,322)	(191)	(5,854)
Discontinued operations:				
Income from discontinued operations, net of tax	5,084	—	37	—
Gain on sale of discontinued operations, net of tax	22,195	—	163	—
Discontinued operations, net of tax	27,279	—	200	—
Net income (loss)	25,462	(78,322)	9	(5,854)
Dividends paid to participating securities	(37)	—	—	—
Net income (loss) applicable to common stockholders	$25,425	$(78,322)	$9	$(5,854)
Basic and diluted net income (loss) per Class A and Class B share applicable to common stockholders:				
Continuing operations	$(0.04)	$(1.88)	$(0.00)	$(0.14)
Discontinued operations, net of tax	0.66	—	0.00	—
Basic and diluted net income (loss) per Class A and Class B share applicable to common stockholders	$0.62	$(1.88)	$0.00	$(0.14)
Dividends paid per share	$0.04	$—	$—	$—
Shares used to calculate basic net income (loss) per share applicable to common stockholders:				

Class A	5,233	5,233	5,233	5,233
Class B	35,980	36,372	36,120	36,639
Shares used to calculate diluted net income (loss) per share applicable to common stockholders:				
Class A	5,233	5,233	5,233	5,233
Class B	41,213	41,605	41,353	41,872

See accompanying Notes to Condensed Consolidated Financial Statements.

MARCHEX, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2016
Cash flows from operating activities:		
Net income (loss)	$25,462	$(78,322)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization and depreciation	2,735	2,457
Impairment of goodwill	—	63,305
Allowance for doubtful accounts and advertiser credits	678	1,429
Loss on disposal of fixed assets	—	3
Gain on sale of discontinued operations	(22,195)	—
Stock-based compensation	7,809	7,246
Change in certain assets and liabilities:		
Accounts receivable, net	(599)	1,612
Refundable taxes	(4)	10
Prepaid expenses, other current assets and other assets	484	(223)
Accounts payable	(1,472)	(1,477)
Accrued expenses and other current liabilities	230	1,812
Deferred revenue	(789)	(329)
Other non-current liabilities	(339)	(396)
Net cash provided by (used in) operating activities	12,000	(2,873)
Cash flows from investing activities:		
Proceeds from sale of discontinued operations, net of costs	25,249	—
Cash paid for sale of Archeo assets	—	(224)
Purchases of property and equipment	(3,623)	(594)
Purchases of intangible assets and changes in other non-current assets	(46)	(11)
Net cash provided by (used in) investing activities	21,580	(829)
Cash flows from financing activities:		
Tax withholding related to restricted stock awards	(74)	(154)
Common stock dividend payments	(1,685)	—
Repurchase of Class B common stock	(3,201)	(365)
Proceeds from exercises of stock options, issuance and vesting of restricted stock and employee stock purchase plan, net	284	341
Net cash used in financing activities	(4,676)	(178)
Net increase (decrease) in cash and cash equivalents	28,904	(3,880)
Cash and cash equivalents at beginning of period	80,032	109,155
Cash and cash equivalents at end of period	$108,936	$105,275

See accompanying Notes to Condensed Consolidated Financial Statements.

MARCHEX, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(unaudited)

(1) 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 advertising analytics company that helps connect online behavior to real-world, offline actions. The Company provides products and services for businesses of all sizes that depend on consumer phone calls to drive sales. The Company’s technology can facilitate call quality, analyze calls in real time and measure the outcomes of calls while its technology platform delivers performance-based, pay-for-call advertising across numerous mobile and online publishers to connect consumers with businesses over the phone.

The accompanying unaudited condensed consolidated financial statements of Marchex, Inc. and its wholly-owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016, or for any other period. The balance sheet at December 31, 2015 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. These condensed consolidated financial statements and notes should be read in conjunction with the Company’s audited consolidated financial statements and accompanying notes included in the Annual Report on Form 10-K for the year ended December 31, 2015 filed with the SEC.

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated in consolidation.

In April 2015, the Company sold certain assets related to Archeo’s domain operations, including the bulk of its domain name portfolio. The operating results related to this April 2015 disposition are shown as discontinued operations in the condensed consolidated statements of operations in 2015. In December 2015, the Company sold the remaining Archeo operations which did not meet the criteria for discontinued operations, and as a result the operating results are reflected in continuing operations in 2015. See Note 12. Discontinued Operations, Dispositions, and Other of the Notes to Condensed Consolidated Financial Statements for further discussion. Unless otherwise indicated, information presented in the Notes to Condensed Consolidated Financial Statements relates only to the Company’s continuing operations.

(2) Significant Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles ("GAAP") in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These judgments are difficult as matters that are inherently uncertain directly impact their valuation and accounting. Actual results may vary from management's estimates and assumptions.

Recent Accounting Pronouncement(s) Not Yet Effective

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which amends the existing accounting standards for revenue recognition. ASU 2014-09 requires an entity to recognize the amount of revenue to which it expects to be entitled when products or services are transferred to customers. In July 2015, the FASB voted to approve a one-year delay of the effective date. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within those annual periods. ASU 2014-09 may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. In 2016, the FASB issued additional guidance to clarify the implementation guidance. The Company is currently in the process of evaluating the impact of adoption of ASU 2014-09 on its consolidated financial statements.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, Income Taxes (Topic 740), Balance Sheet Classification of Deferred Taxes (ASU 2015-17), an ASU amending the accounting for income taxes and requiring all deferred tax assets and liabilities to be classified as non-current on the consolidated balance sheet. The ASU is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. The ASU may be adopted either prospectively or retrospectively. The Company does not expect adoption of ASU 2015-17 to have a material impact on its consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 Leases (Topic 842), an ASU requiring the recognition of lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU is effective for reporting periods beginning after December 15, 2018, with early adoption permitted. The ASU must be adopted retrospectively. The Company is currently in the process of evaluating the impact of adoption of ASU 2016-02 on its consolidated financial statements.

In March 2016, the FASB amended the existing accounting standards for stock-based compensation, with Accounting Standards Update No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). The amendments impact several aspects of accounting for share-based payment transactions, including the income tax consequences, forfeitures, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The ASU is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. If early adoption is elected, all amendments must be adopted in the same period. The manner of application varies by the various provisions of the guidance, with certain provisions applied on a retrospective or modified retrospective approach, while others are applied prospectively. The Company is currently evaluating the impact of these amendments and the transition alternatives on its consolidated financial statements.

In June 2016, the FASB issued Accounting Standards Update No. 2016-13, Financial Instruments — Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments (ASU 2016-13), an ASU amending the impairment model for most financial assets and certain other instruments. The ASU is effective for reporting periods beginning after December 15, 2019, with early adoption permitted after December 15, 2018. The ASU must be adopted using a modified-retrospective approach. The Company does not expect adoption of ASU 2016-13 to have a material impact on its consolidated financial statements.

(3) Stock-based Compensation Plans

The Company grants stock-based awards, including stock options, restricted stock awards, and restricted stock units. 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-based award, using the straight-line method under FASB ASC 718. Stock-based compensation expense was included in the following operating expense categories as follows (in thousands):

	Nine months ended		Three months ended	
	September 30,		September 30,	
	2015	2016	2015	2016
Service costs	$1,046	$565	$273	$160
Sales and marketing	893	1,321	339	353

Product development	1,843	1,367	620	206
General and administrative	4,027	3,993	1,119	1,060
Total stock-based compensation	$7,809	$7,246	$2,351	$1,779

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 the quarters ended September 30, 2015 and 2016, 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 implied yield currently available on U.S. Treasury issues with terms approximately equal to the expected life of the option. The Company used an expected annual dividend yield in consideration of the Company's common stock dividend payments during the first half of 2015. The Company discontinued paying dividends on its common stock after the second quarter of 2015.

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

	Nine months ended September 30,		Three months ended September 30,	
	2015	2016	2015	2016
Expected life (in years)	4.0-6.25	4.0-6.25	4.0-6.25	4.0
Risk-free interest rate	1.13%-1.56%	0.86%-1.15%	1.15%-1.56%	1.01%
Expected volatility	59%-65%	57%-58%	59%-65%	57%
Expected dividend yield	0%-0.36%	0%	0%	0%

Stock option activity during the nine months ended September 30, 2016 is summarized as follows:

	Shares	Weighted average exercise price	Weighted average remaining contractual term (in years)
Balance at December 31, 2015	8,937,281	$ 6.97	6.33
Options granted	1,669,000	4.20	
Options forfeited	(734,562)	5.51	
Options expired	(620,500)	12.58	
Options exercised	(60,303)	4.01	
Balance at September 30, 2016	9,190,916	$ 6.22	5.91

Restricted stock awards and restricted stock units 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 stock units entitle the holder to receive one share of the Company's Class B common stock upon satisfaction of certain service conditions.

Restricted stock awards and restricted stock unit activity during the nine months ended September 30, 2016 is summarized as follows:

	Shares/ Units	Weighted average grant date fair value

Unvested balance at December 31, 2015	2,222,080	$	4.86
Granted	2,196,406		4.24
Vested	(813,592)		5.16
Forfeited	(649,771)		5.08
Unvested balance at September 30, 2016	2,955,123	$	4.26

In the nine months ended September 30, 2015 and 2016, the Company repurchased approximately 15,000 and 45,000 shares, respectively, from certain executives for minimum withholding taxes on approximately 55,000 and 146,000 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 $74,000 and $154,000, respectively, which was remitted in 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.

In May 2016, approximately 27,000 stock options and 33,000 restricted stock awards were fully accelerated and the period to exercise any outstanding vested stock options was modified to extend through the 10-year anniversary of the respective grant dates in connection with an executive's transition to a consulting arrangement. In October 2016, vesting of 288,877 stock options and 190,187 restricted stock awards were accelerated in connection with an executive's separation agreement for which the estimated related stock-based compensation expense of approximately $1.3 million will be recognized in the fourth quarter of 2016.

(4) 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 stockholders 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 for all cash dividends paid since 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 impact the calculation of amounts allocated to common stock.

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

	Nine months ended September 30,			
	2015		2016	
	Class A	Class B	Class A	Class B
Basic net income (loss) per share:				
Numerator:				
Net loss from continuing operations	$(235)	$(1,582)	$(9,850)	$(68,472)
Dividends paid to participating securities	—	(37)	—	—
Net loss from continuing operations applicable to common stockholders	$(235)	$(1,619)	$(9,850)	$(68,472)
Discontinued operations, net of tax	3,464	23,815	—	—
Net income (loss) applicable to common stockholders	$3,229	$22,196	$(9,850)	$(68,472)
Denominator:				
Weighted average number of shares outstanding used to calculate basic net income (loss) per share	5,233	35,980	5,233	36,372
Basic net income (loss) per share:				
Net loss from continuing operations applicable to common stockholders	$(0.04)	$(0.04)	$(1.88)	$(1.88)
Discontinued operations, net of tax	0.66	0.66	—	—
Basic net income (loss) per share applicable to common stockholders	$0.62	$0.62	$(1.88)	$(1.88)

	Three months ended September 30,			
	2015		2016	
	Class A	Class B	Class A	Class B
Numerator:				
Net loss from continuing operations applicable to common stockholders	$(24)	$(167)	$(732)	$(5,122)
Discontinued operations, net of tax	25	175	—	—
Net income (loss) applicable to common stockholders	$1	$8	$(732)	$(5,122)
Denominator:				
Weighted average number of shares outstanding used to calculate basic net income (loss) per share	5,233	36,120	5,233	36,639
Basic net income (loss) per share:				
Net loss from continuing operations applicable to common stockholders	$(0.00)	$(0.00)	$(0.14)	$(0.14)
Discontinued operations, net of tax	0.00	0.00	—	—
Basic net income (loss) per share applicable to common stockholders	$0.00	$0.00	$(0.14)	$(0.14)

The following table calculates net income (loss) from continuing operations to 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):

	Nine months ended September 30,			
	2015		2016	
	Class A	Class B	Class A	Class B
Diluted net income (loss) per share:				
Numerator:				
Net loss from continuing operations	$(235)	$(1,582)	$(9,850)	$(68,472)
Dividends paid to participating securities	—	(37)	—	—
Reallocation of net loss for Class A shares as a result of conversion of Class A to Class B shares	—	(235)	—	(9,850)
Net loss from continuing operations applicable to common stockholders	$(235)	$(1,854)	$(9,850)	$(78,322)
Discontinued operations, net of tax	3,464	23,815	—	—
Reallocation of discontinued operations for Class A shares as a result of conversion of Class A to Class B shares	—	3,464	—	—
Diluted discontinued operations, net of tax	$3,464	$27,279	$—	$—
Net income (loss) applicable to common stockholders	$3,229	$25,425	$(9,850)	$(78,322)
Denominator:				
Weighted average number of shares outstanding used to calculate basic net income (loss) per share	5,233	35,980	5,233	36,372
Conversion of Class A to Class B common shares outstanding	—	5,233	—	5,233
Weighted average number of shares outstanding used to calculate diluted net income (loss) per share	5,233	41,213	5,233	41,605
Diluted net (loss) income per share:				

Net loss from continuing operations applicable to common stockholders	$(0.04)	$(0.04)	$(1.88)	$(1.88)
Discontinued operations, net of tax	0.66	0.66	—	—
Diluted net income (loss) per share applicable to common stockholders	$0.62	$0.62	$(1.88)	$(1.88)

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	Three months ended September 30, 2015 Class A	2015 Class B	2016 Class A	2016 Class B
Numerator:				
Net loss from continuing operations	$(24)	$(167)	$(732)	$(5,122)
Dividends paid to participating securities	—	—	—	—
Reallocation of net loss for Class A shares as a result of conversion of Class A to Class B shares	—	(24)	—	(732)
Net loss from continuing operations applicable to common stockholders	$(24)	$(191)	$(732)	$(5,854)
Discontinued operations, net of tax	25	175	—	—
Reallocation of discontinued operations for Class A shares as a result of conversion of Class A to Class B shares	—	25	—	—
Discontinued operations, net of tax	$25	$200	$—	$—
Net income (loss) applicable to common stockholders	$1	$9	$(732)	$(5,854)
Denominator:				
Weighted average number of shares outstanding used to calculate basic net income per share	5,233	36,120	5,233	36,639
Conversion of Class A to Class B common shares outstanding	—	5,233	—	5,233
Weighted average number of shares outstanding used to calculate diluted net income (loss) per share	5,233	41,353	5,233	41,872
Diluted net income (loss) per share:				
Net loss from continuing operations applicable to common stockholders	$(0.00)	$(0.00)	$(0.14)	$(0.14)
Discontinued operations, net of tax	0.00	0.00	—	—
Diluted net income (loss) per share applicable to common stockholders	$0.00	$0.00	$(0.14)	$(0.14)

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

- For both the three and nine months ended September 30, 2015, outstanding options to acquire 9,158 shares of Class B common stock. For both the three and nine months ended September 30, 2016, outstanding options to acquire 9,191 shares of outstanding Class B common stock.
- For the three and nine months ended September 30, 2015 and 2016, 1,052 and 1,221 shares of unvested Class B restricted common shares, respectively.
- For the three and nine months ended September 30, 2015 and 2016 1,427 and 1,734 restricted stock units, respectively.

(5) 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. At various points during the nine months ended September 30, 2016, the Company held cash equivalents in a commercial paper sweep account with the same financial institution. These Level 2 assets were fully liquidated prior to September 30, 2016.

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 paid more than 10% of consolidated revenue for the three and nine months ended September 30, 2015 and 2016.

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

	Nine months ended September 30,		Three months ended September 30,	
	2015	2016	2015	2016
Advertiser A	30 %	23 %	28 %	22 %
Advertiser B	20 %	24 %	19 %	22 %

Advertiser A is also a distribution partner.

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

	At December 31, 2015	At September 30, 2016
Advertiser A	14 %	21 %
Advertiser B	28 %	20 %
Advertiser C	19 %	13 %

In certain cases, the Company may engage directly with one or more advertising agencies who act on an advertiser’s behalf. In addition, an advertising agency may represent more than one advertiser that utilizes the Company’s products and services. One advertising agency represented 17% and 19% of consolidated revenue for the three and nine months ended September 30, 2015, respectively, and 19% and 21% of consolidated revenue for the three and nine months ended September 30, 2016, respectively. This same advertising agency represented 22% and 11% of consolidated accounts receivable as of December 31, 2015 and September 30, 2016, respectively. One other advertising agency represented less than 10% of consolidated accounts receivable as of December 31, 2015, and 11% of consolidated accounts receivable as of September 30, 2016.

(6) 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. Historically, the Company operated under two segments: Call-driven and Archeo. Subsequent to the sale of the Company’s remaining Archeo operations in December 2015, the Company operates primarily under the Call-driven segment which is comprised of performance-based advertising business focused on driving phone calls.

The Archeo segment historically comprised the Company’s click-based advertising businesses. In April 2015, the Company sold certain assets related to Archeo’s domain operations, including the bulk of its domain name portfolio. This disposition is shown as discontinued operations, net of tax, in the condensed consolidated statements of operations for all periods presented and is excluded from segment reporting. On December 31, 2015, the Company sold the remaining Archeo operations, which did not meet the criteria for discontinued operations presentation and is included in segment reporting in 2015. See Note 12. Discontinued Operations, Dispositions, and Other for further discussion.

Call-driven segment expenses include both direct costs incurred by the segment as well as corporate overhead costs. Archeo segment expenses only include direct costs incurred by the segment. Segment expenses exclude the following: stock-based compensation, acquisition and disposition related costs, and other expense.

For the three and nine months ended September 30, 2016, the Company’s operating results are primarily all Call-driven. There were other operating activities related to transition activities of the Archeo operations in 2016, which were not significant.

Selected segment information (in thousands):

	Nine months ended September 30, 2015		
	Call-driven	Archeo	Total
Revenue	$105,621	$2,492	$108,113
Operating expenses	99,412	2,447	101,859
Segment profit	$6,209	$45	$6,254
Less reconciling items:			
Stock-based compensation			7,809
Acquisition and disposition related costs			199
Other expense			52
Loss from continuing operations before provision for income taxes			$(1,806)

	Three months ended September 30, 2015		
	Call-driven	Archeo	Total
Revenue	$36,135	$ 717	$36,852
Operating expenses	33,958	450	34,408
Segment profit	$2,177	$ 267	$2,444
Less reconciling items:			
Stock-based compensation			2,351
Acquisition and disposition related costs			81
Other expense			12
Loss from continuing operations before provision for income taxes			$0

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):

	Nine months ended September 30,		Three months ended September 30,	
	2015	2016	2015	2016
United States	97 %	97 %	97 %	97 %
Canada	3 %	3 %	3 %	3 %
Other countries	*	*	*	*
	100 %	100 %	100 %	100 %

*Less than 1% of revenue.

(7) Property and Equipment

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

	At December 31, 2015	At September 30, 2016
Computer and other related equipment	$ 21,551	$ 20,688
Purchased and internally developed software	7,893	7,874
Furniture and fixtures	1,778	1,825
Leasehold improvements	2,123	2,328
	$ 33,345	$ 32,715
Less: Accumulated depreciation and amortization	(27,567)	(28,802)
Property and equipment, net	$ 5,778	$ 3,913

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Depreciation and amortization expense related to property and equipment was approximately $885,000 and $762,000 for the three months ended September 30, 2015 and 2016, respectively, and was approximately $2.6 million and $2.4 million for the nine months ended September 30, 2015 and 2016, respectively.

(8) Commitments, Contingencies and Taxes

(a) 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 2019. Other contractual obligations primarily relate to minimum contractual payments due to distribution partners and other outside service providers. Future minimum payments are approximately as follows (in thousands):

	Facilities operating leases	Other contractual obligations	Total
2016	$ 588	$ 1,303	$ 1,891
2017	2,362	3,170	5,532
2018	577	1,147	1,724
2019	—	440	440
2020 and after	—	—	—
Total minimum payments	$ 3,527	$ 6,060	$ 9,587

Rent expense incurred by the Company was approximately $460,000 and $559,000 for the three months ended September 30, 2015 and 2016, respectively, and was $1.4 million and $1.5 million for the nine months ended September 30, 2015 and 2016, respectively.

(b) Contingencies

On November 17, 2015, Steven Porter, a purported shareholder of the Company, filed a securities class action against the Company and certain officers of the Company, alleging violations of the federal securities laws (the “Complaint”). Mr. Porter sought to represent all people who purchased or otherwise acquired the Company’s Class B common stock during the period from March 19, 2014 to September 18, 2014, and sought unspecified damages. The Complaint alleged that the Defendants made false and/or misleading statements and/or failed to disclose material adverse facts about the Company’s business, operations, and prospects. On April 1, 2016, Mr. Porter was appointed “Lead Plaintiff” in the action. On April 22, 2016, the case was dismissed without prejudice after the Lead Plaintiff filed a notice of voluntary dismissal of the case.

In addition, the Company from time to time is a party to disputes and legal and administrative proceedings arising from the ordinary course of business. In some agreements to which the Company is a party to, 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 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.

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, results of operations or liquidity.

(c) Taxes

The Company determined that it is not more likely than not that its deferred tax assets will be realized and accordingly recorded 100% valuation allowance against these deferred tax assets as of December 31, 2015 and September 30, 2016. 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 the industry, existing contracts, the Company's ability to project future results and any appreciation of its other assets. The ultimate realization of deferred tax assets depends on the generation of future taxable income during the periods in which those temporary differences are deductible. The Company considered the future reversal of deferred tax liabilities, carryback potential, projected taxable income, and tax planning strategies as well as its history of taxable income or losses in the relevant jurisdictions in making this assessment. Based on the level of historical taxable losses and the uncertainty of projections for future taxable income over the periods for which the deferred tax assets are deductible, the Company concluded that it is not more likely than not that the gross deferred tax assets will be realized.

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. 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 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 2011 are within the statute of limitations and are under examination or may be subject to examination.

(9) Credit Agreement

In April 2008, the Company entered into a Credit Agreement providing for a senior secured $30 million revolving credit facility ("Credit Agreement"). In June 2016, the Company signed an amendment to the Credit Agreement that modifies the unused commitment fees, replaces certain financial covenants with a covenant limiting outstanding balances not to exceed a defined ratio against the Company's unrestricted cash and cash equivalent balances and a covenant with certain earnings thresholds, and modifies the levels and types of indebtedness and payments the Company may make. The Credit Agreement has a maturity date of April 1, 2017 and 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 nine months ended September 30, 2015 and 2016, the Company had no borrowings under the Credit Agreement.

(10) Goodwill

Changes in the carrying amount of goodwill for the nine months ended September 30, 2016 are as follows (in thousands):

Balance as of December 31, 2015	$63,305
Impairment of goodwill	(63,305)
Balance as of September 30, 2016	$—

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, the Company may first perform a qualitative assessment and determine if the fair value of the reporting unit is more likely than not greater than its carrying amount. For the three months ended June 30, 2016, the Company's stock price was impacted by volatility in the U.S. financial markets, and traded below the then book value for an extended period of time. Accordingly, the Company tested its goodwill for impairment and concluded that the carrying value exceeded the estimated fair value of the Company's single reporting unit and recognized an impairment loss during the second quarter of 2016 of $63.3 million. The fair value of the Company's single reporting unit was based on estimates of future operating results, discounted cash flows and other market-based factors, including the Company's stock price. The goodwill impairment loss resulted primarily from a sustained decline in the Company's common stock share price and market capitalization as well as 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.

The testing of goodwill for impairment requires the Company to make significant estimates about its future performance and cash flows, as well as other assumptions. 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 changes in competition and market dynamics; 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. These estimates and circumstances are inherently uncertain and can be affected by numerous factors, including changes in economic, industry or market conditions, changes in business operations, a loss of a significant customer, changes in competition, volatility in financial markets, or changes in the share price of the Company's common stock and market capitalization.

(11) Common Stock

In November 2014, the Company's board of directors authorized a share repurchase program (the "2014 Repurchase Program"), which supersedes and replaces any prior repurchase programs. Under the 2014 Repurchase Program, the Company is authorized to repurchase up to 3 million shares of the Company's Class B common stock in the aggregate through open market and privately negotiated transactions, at such times and in such amounts as the Company deems appropriate. Repurchases may also be made under a Rule 10b5-1 plan, which would permit shares to be repurchased when the Company might otherwise be precluded from doing so under insider trading laws. 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. The 2014 Repurchase Program does not have an expiration date and may be expanded, limited or terminated at any time without prior notice. During the nine months ended September 30, 2015 and 2016, the Company repurchased 781,000 shares of Class B common stock for $3.2 million and 89,000 shares of Class B common stock for $365,000, respectively.

During the nine months ended September 30, 2015 and 2016, the Company's board of directors approved and the Company retired approximately 1,262,000 and 250,000 shares of treasury stock, respectively.

(12) Discontinued Operations, Dispositions and Other

In April 2015, the Company sold certain assets related to Archeo's domain operations, including the bulk of its domain name portfolio. This disposal met the requirements of Accounting Standards Codification 205-20, Discontinued Operations, for presentation as discontinued operations. As a result, the operating results related to this disposition are shown as discontinued operations, net of tax. The operating results for the discontinued operations were as follows (in thousands):

	Nine months ended September 30, 2015
Revenue	$ 7,081
Expenses:	
Service costs	1,663
Sales and marketing	334
Income from discontinued operations, before provision for income taxes	5,084
Income tax expense	—
Income from discontinued operations, net of tax	$ 5,084

The discontinued operations incurred amortization of $16,000 for the nine months ended September 30, 2015.

The net cash proceeds related to Archeo's domain operations sold in April 2015 were approximately $28.1 million. The sale includes a contingent earn-out consideration payment that depends upon the achievement of certain thresholds and will be recognized as income when received.

On December 31, 2015, the Company sold the remaining Archeo operations for cash proceeds of $750,000. The transaction costs were approximately $244,000 and the net carrying value of the liabilities assumed were approximately $990,000, resulting in a net gain of $1.5 million from the sale. The Company evaluated this disposition and determined that it did not meet the criteria for classification as a discontinued operation. As a result, operating results of these Archeo operations are reflected in the Company's continuing operations in the condensed consolidated statements of operations. For the three and nine months ended September 30, 2015, the income before provision for income taxes for these Archeo operations included in the Company's continuing operations was $267,000 and $45,000, respectively.

During the three months ended September 30, 2016, the Company incurred approximately $1.6 million in employee separation and facility termination related costs. As of September 30, 2016, approximately $767,000 of these costs were accrued and unpaid of which $413,000 is expected to be paid prior to December 31, 2016 with the remaining to be paid in 2017.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, 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, dispositions, 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. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements we make. There are a number of important factors that could cause the actual results of Marchex to differ materially from those indicated by such forward-looking statements. 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 but not limited to the risks, uncertainties and assumptions described in this report, in Part II, Item 1A. under the caption "Risk Factors" and elsewhere in this report and in our Annual Report on Form 10-K for the year ended December 31, 2015 and those described from time to time in our future reports filed with the SEC. 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.

The following discussion and analysis provides information that we believe is relevant to an assessment and understanding of our results of operation and financial condition. You should read this analysis in conjunction with the attached condensed consolidated financial statements and related notes thereto, and with our audited consolidated financial statements and the notes thereto, included in our Annual Report on Form 10-K for the year ended December 31, 2015.

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 advertising analytics company that connects online behavior to real-world, offline actions.

We provide products and services for enterprises that depend on consumer phone calls to drive sales. Our media analytics products can connect call data to media channels – including search and display– down to the campaign, keyword and impression so marketers can maximize advertising returns. Our sales analytics products deliver actionable intelligence on the offline consumer journey to help prospects become customers.

Our primary product offerings are:

- Marchex Call Analytics. Marchex Call Analytics is an analytics platform for enterprises that depend on inbound phone calls to drive sales, appointments and reservations. Marketers use this platform to understand which marketing channels, advertisements, keywords and creatives are driving calls to their business, allowing them to optimize their advertising expenditures across media channels. Marchex Call Analytics also includes technology that can extract data and insights about what is happening during a call and measures the outcome of calls and return on investment.

The platform also includes technology that blocks robocalls, telemarketers and spam calls to save businesses time. Marchex Call Analytics data can integrate directly into third-party marketer workflows such as Salesforce, Eloqua, Adobe, Kenshoo, DoubleClick Search, Marin Software and many other marketing dashboards and tools. Advertisers pay us a fee for each call or call related data element they receive from calls including call-based ads we distribute through our sources of call distribution or for each phone number tracked based on pre-negotiated rates.

Marchex Call Analytics for Search. Marchex Call Analytics for Search is a product for search marketers that drive phone calls from search campaigns. Marchex Call Analytics for Search attributes inbound phone calls made directly from paid search ads and landing pages to a keyword. The platform can deliver this data as well as data about call outcomes directly into search management platforms like DoubleClick Search and Kenshoo.

Marchex Display Analytics. Marchex Display Analytics, currently in beta, is a product for marketers that buy digital display advertising. Marchex Display Analytics can measure the influence that display advertising has on inbound phone calls so that marketers can better attribute their return on advertising spend for inbound phone calls and delivers this data to marketers in a reporting dashboard.

- Marchex Call Marketplace. Marchex Call Marketplace is a mobile advertising network for businesses that depend on inbound phone calls to drive sales. We offer advertisers ad placements across numerous mobile and online media sources to deliver qualified calls to their businesses. It leverages Marchex Call Analytics platform for tracking, reporting and optimization. Advertisers are charged on a pay-per-call or cost per action basis.
- 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 search engines. The lead services we offer to small business advertisers through our Local Leads platform include pay-for-call, search marketing and 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. Through our contract with Yellowpages.com

LLC (“YP”), we generate revenues from our local leads platform. We also have a separate pay-for-call services arrangement with YP. In 2015, we extended these agreements through December 31, 2016. The primary local leads platform arrangement includes certain minimum fee commitments by YP through the first half of 2016 and provides YP additional flexibility to migrate active accounts to itself or a third-party provider prior to the end of an advertiser contract. YP is our largest reseller partner and was responsible for 28% and 30% of our total revenues in the three and nine months ended September 30, 2015, respectively, and 22% and 23% of our total revenues in the three and nine months ended September 30, 2016. We also have a separate distribution partner agreement with YP.

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

We have offices in Seattle, Washington; Las Vegas, Nevada; New York, New York; and San Francisco, California. In May 2016, we opened an office in London, England.

On October 3, 2016, by mutual agreement, Peter Christothoulou resigned as our Chief Executive Officer. In addition, Clark Kokich resigned as Executive Chairman of our Board of Directors (the “Board”) and as a member of the Board on October 1, 2016. Effective on October 3, 2016, the Board established an Interim Office of the CEO subject to oversight by Anne Devereux-Mills as Chairman. The Interim Office of the CEO consists of Michael Arends, Ethan Caldwell, Gary Nafus, and Russell C. Horowitz who is currently a consultant to the Company and previously Chief Executive Officer and Chairman of the Board. The Interim Office of the CEO will perform the duties and responsibilities of the chief executive officer on an interim basis while a search for a permanent chief executive officer is conducted.

Consolidated Statements of Operations

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 condensed consolidated financial statements.

We primarily generate our revenues from our Call-driven products and services. Call-driven revenue consists of payments from advertisers for pay-for-call advertising services and for use of our call analytics technology. Call-driven revenue also consists of payments from our reseller partners for use of our local leads technology platform and marketing services, which they offer to their small business customers, as well as payments from advertisers for cost-per-action services. Historically, we also generated revenue from our Archeo operations, which included revenue generated from our click based advertising and Internet domain operations. In 2015, we sold primarily all of our Archeo operations in two separate transactions. In April 2015, we sold the bulk of our domain name portfolio. The operating results related to this disposition is shown as discontinued operations in the condensed consolidated statements of operations for all periods presented. In December 2015, we sold the remaining Archeo operations. This disposition did not meet the criteria for discontinued operations, and as a result, the operating results are reflected in continuing operations in the condensed consolidated statements of operations. See Note 12. Discontinued Operations, Dispositions, and Other for further discussion regarding the dispositions. For detail on revenue by segment, see Note 6. Segment Reporting and Geographic Information of the notes to our condensed consolidated financial statements.

Presentation of Financial Reporting Periods

The comparative periods presented are for the three and nine months ended September 30, 2015 and 2016.

Revenue

We generate revenue through our call advertising services and our local leads platform, which includes our call analytics and pay-for-call services. Historically, we also generated revenue through pay-per-click advertising services.

Our performance-based advertising services, which include call advertising, cost-per-action services, and pay-per-click services, amounted to greater than 80% of revenues in all periods presented. In addition, we generate revenue through our Local Leads platform, which enables partner resellers to sell call advertising and/or search marketing products, and campaign management services. These secondary sources accounted for less than 20% of our revenues in all periods presented. We have no barter transactions.

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.

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 owed that occurs subsequent to period ends.

Performance-Based Advertising Services

Our call analytics technology platform provides data and insights that can measure the performance of mobile, online and offline advertising for advertisers and small business resellers. We generate revenue from our call analytics technology platform when advertisers pay us a fee for each call or call related data element they receive from calls including call-based ads we distribute through our sources of call distribution or for each phone number tracked based on a pre-negotiated rate.

In providing pay-for call advertising services, we generate revenue upon delivery of qualified and reported phone calls to advertisers or advertising service providers’ listings. These advertisers and advertising service providers pay us a designated transaction fee for each qualified phone call, which occurs when a user makes a phone call, clicks, or completes a specified action on any of their advertisement listings after it has been placed by us or by our distribution partners. Each qualified phone call or specified action 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, and other targeted Web-based content, mobile carriers 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, 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.

Industry and Market Factors

We enter into agreements with various mobile, online and offline distribution partners to provide distribution for pay-for-call 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 on these listings. The level of phone calls 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 or renew our existing distribution partner agreements and on terms as favorable as current arrangements, replace traffic lost from terminated distribution agreements with other sources, or if our distribution partners' 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 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 products and services, the amount these advertisers spend on our products and services, advertiser adoption of new products and services and the amount these advertisers are willing to pay for these new products and services.

We utilize phone numbers as part of our pay-for-call and call analytics services to advertisers, which enables advertisers and other users of our services to help measure the effectiveness of mobile, online, and offline advertising campaigns. If we are not able to secure or retain sufficient phone numbers needed for our services or we are limited in the number of available telecommunication carriers or vendors to provide such phone numbers to us in the event of any industry consolidation or if telecommunication carriers or vendors were to experience system disruptions, our revenue and results of operations may be materially and adversely affected.

We have revenue concentrations with certain large customers. Many of these customers are not subject to long term contracts with us or have contracts with near term expiration dates, and are able to reduce or cease advertising spend at any time and for any reason. In some cases, we engage with advertisers through advertising agencies, who act on behalf of the advertisers. Advertising agencies may place insertion orders with us for particular advertising campaigns for a set period of time and are not obligated to commit beyond the campaign governed by a particular insertion order and may also cancel the campaign prior to completion. Advertising agencies also have relationships with many different providers, each of whom may be running portions of the advertising campaign. A significant reduction in advertising spending or budgets 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 have a material adverse effect on our future operating results.

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 phone call usage, the number of phone calls or other actions performed by users of our product and services which will be delivered to our advertisers, and how much advertisers will spend with us and the amount they are willing to pay for our products and services. It is even more difficult to anticipate the average revenue per phone call or other performance-based actions. It is also difficult to anticipate the impact of worldwide and domestic 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 from our call advertising customers. 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 and in turn the market price of our securities. In the first quarter of the calendar year, this trend generally reverses with increased mobile and Internet usage and often new budgets at the beginning of the year for many of our customers with fiscal years ending December 31. The seasonal purchasing cycles of some customers in certain industries may also be higher in the first half versus the latter half of the calendar year. Additionally, the current business environment and our industry has generally both resulted in, and we may continue to see, 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.

We believe that our future revenue growth will depend on, among other factors, our ability to attract new advertisers, compete effectively, maximize our sales efforts, demonstrate a positive return on investment for advertisers, successfully improve existing products and services, develop successful new products and services, and expand internationally. If we are unable to generate adequate revenue growth and to manage our expenses, we may continue to incur significant losses in the future and may not be able to achieve or maintain profitability.

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

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- domain name registration renewal fees;
- domain name costs;
- network fees;
- fees paid to outside service providers;
- delivering customer service;
- depreciation of network equipment and software;
- colocation service charges of our network website 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 consists 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, indexes or other sources of user traffic. 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 other action. Other payment structures that to a lesser degree exist include:

- variable payments based on a specified metric, such as number of paid phone calls or other actions;
- fixed payments, based on a guaranteed minimum amount of usage delivered; 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 variable or fixed payments. Agreements with variable payments based on a percentage of revenue, number of paid phone calls, 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. Agreements with fixed payments with minimum guaranteed amounts of usage are expensed at 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.

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 products and services.

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 statements of operations.

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. Uncertain tax positions as September 30, 2016 amounted to $1.0 million.

At September 30, 2016, based upon both positive and negative evidence available, we determined that it is not more likely than not that our deferred tax assets of $43.4 million will be realized and accordingly, we have recorded a 100% valuation allowance of $43.4 million against these deferred tax assets. This compares to a valuation allowance of $34.5 million at December 31, 2015. Based on the level of historical taxable losses and the uncertainty of projections for future taxable income over the periods for which the deferred tax assets are deductible, we concluded that it is not more likely than not that the gross deferred tax assets will be realized. In assessing the realizability of deferred tax assets, we considered whether it is more likely than not that some or all of the deferred tax assets will be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income during the periods in which those temporary differences are deductible. We also considered the future reversal of deferred tax liabilities, carryback potential, projected taxable income, and tax planning strategies as well as its history of taxable income or losses in the relevant jurisdictions in making this assessment. We incurred taxable losses in 2013, 2014, and 2015. As of September 30, 2016, our federal NOL carryforwards were approximately $52.5 million for income tax purposes, which will begin to expire in 2026. As of September 30, 2016, our state, city, and other foreign jurisdiction NOL carryforwards were approximately $6.4 million, which begin to expire in 2025.

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.

Results of Operations

The following table presents certain of our operating results as a percentage of revenue for the periods indicated:

	Nine Months Ended September 30, 2015	2016	Three Months Ended September 30, 2015	2016
Revenue	100 %	100 %	100 %	100 %
Expenses:				
Service costs	55 %	60 %	54 %	60 %
Sales and marketing	11 %	17 %	12 %	18 %
Product development	22 %	22 %	21 %	22 %
General and administrative	14 %	16 %	13 %	17 %
Acquisition and disposition related costs	0 %	1 %	0 %	1 %
Total operating expenses	102 %	115 %	100 %	119 %
Impairment of goodwill	—	(63 %)	—	—
Income (loss) from operations	(2 %)	(77 %)	0 %	(0 %)
Other expense	0 %	0 %	0 %	0 %
Income (loss) from continuing operations before provision for income taxes	(2 %)	(77 %)	0 %	(19 %)
Income tax expense	0 %	0 %	1 %	0 %
Net loss from continuing operations	(2 %)	(77 %)	(1 %)	(19 %)
Discontinued operations, net of tax	26 %	— %	1 %	— %
Net income (loss)	24 %	(77 %)	0 %	(19 %)
Dividends paid to participating securities	0 %	— %	0 %	— %
Net income (loss) applicable to common stockholders	24 %	(77 %)	0 %	(19 %)

Segment Operating Results

We have historically 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 included our click-based advertising and Internet domain name operations that were sold in 2015. For the three and nine months ended September 30, 2016, our operating results are primarily all Call-driven and other operating activities related to the transition activities of the Archeo operations were not significant. For the three and nine months ended September 30, 2015, operating results by segment were as follows:

	Nine months ended September 30, 2015	Three months ended September 30, 2015

Call-driven		
Revenue	$ 105,621	$ 36,135
Operating expenses	99,412	33,958
Segment profit	$ 6,209	$ 2,177
Archeo		
Revenue	$ 2,492	$ 717
Operating expenses	2,447	450
Segment profit	$ 45	$ 267
Reconciliation of segment profit from operations to loss from continuing operations before provision for income taxes:		
Total segment profit	$ 6,254	$ 2,444
Less reconciling items:		
Stock based compensation	7,809	2,351
Acquisition and disposition related costs	199	81
Other expense	52	12
Loss from continuing operations before provision for income taxes	$ (1,806)	$ 0

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	Nine months ended September 30, 2015	Three months ended September 30, 2015
Reconciliation of segment revenue to consolidated revenue		
Call-driven	$ 105,621	$ 36,135
Archeo	2,492	717
Total	$ 108,113	$ 36,852

Comparison of the three months ended September 30, 2015 to the three months ended September 30, 2016 and the nine months ended September 30, 2015 to the nine months ended September 30, 2016.

Revenue

Revenue decreased 17% from $36.9 million for the three months ended September 30, 2015 to $30.7 million in the same period in 2016. Revenue decreased 6% from $108.1 million for the nine months ended September 30, 2015 to $101.1 million in the same period in 2016. The decrease for the three and nine months ended September 30, 2016, was primarily due to a decrease in Call-driven revenues and no longer generating any Archeo revenues during 2016 as a result of the sale of the remaining Archeo operations in December 2015. Archeo revenues for the three and nine months ended September 30, 2015 were $717,000 and $2.5 million, respectively.

Our Call-driven revenues were $36.1 million for the three months ended September 30, 2015 and $30.7 million in the same period in 2016.

Our Call-Driven revenues were $105.6 million for the nine months ended September 30, 2015 and $101.1 million in the same period in 2016. The decrease for both periods were due primarily to lower advertiser budgets for our pay-for-call services and fewer YP small business accounts and related revenues.

We expect our revenues to be lower in the near and intermediate terms compared to the most recent quarters with fewer small business accounts on our local leads platform and reduced demand for calls from our call advertising customers, particularly in the latter part of the fourth quarter where we have historically experienced lower call volumes.

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. We also have a separate pay-for-call relationship with YP within our Call Marketplace. We charge an agreed-upon price for qualified calls or leads from our network. In 2015, we extended these agreements through December 31, 2016. The primary local leads platform arrangement includes certain minimum fee commitments by YP through the first half of 2016 and provides YP additional flexibility to migrate active accounts to itself or a third-party provider prior to the end of an advertiser contract. 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 revenue may decrease. Additionally, YP's small business account base from their traditional business has declined, and to the extent declines occur in their business, their small business accounts may spend fewer dollars on our pay-for-call services. In addition, we expect YP may decrease the number of new advertiser accounts with us and may elect to migrate certain active accounts to itself or a third party provider which would result in fewer small business accounts and related revenues. We expect YP will comprise lower total revenues in the near term than in recent periods. We also have a separate distribution partner agreement with YP. There can be no assurance that our business with them in the future will continue at or near current revenue and contribution levels, that we will be able to renew and extend the contracts set to expire in December 2016, and if renewed, the contracts are likely to be on less favorable terms to us, any of which could have a material adverse effect on our future operating results. YP accounted for 28% and 22% of total revenues for the three months ended September 30, 2015 and 2016, respectively, and 30% and 23% for the nine months ended September 30, 2015 and 2016, respectively.

We also have arrangements with advertising agencies, such as Resolution Media and OMD Digital, who act on an advertiser's behalf and may represent more than one advertiser that utilizes our products and services. Our primary arrangement with Resolution Media is for pay-for-call services whereby we charge an agreed-upon price for qualified calls or leads from our network and call analytic services. Resolution Media accounted for 17% and 19% of total revenues for the three months ended September 30, 2015 and 2016, respectively, and 19% and 21% of total revenues for the nine months ended September 30, 2015 and 2016, respectively, of which the majority related to a single advertiser, State Farm. State Farm, who utilizes our services through Resolution Media and

OMD Digital, accounted for 19% and 20% of total revenues for the three and nine months ended September 30, 2015, respectively, and 22% and 24% of total revenues for the three and nine months ended September 30, 2016, respectively.

We have revenue concentrations with other certain large customers. Many of these customers are not subject to long term contracts with us or have contracts with near term expiration dates such as Yellow Pages Ltd, and are able to reduce or cease advertising spend at any time and for any reason. In some cases, we engage with advertisers through advertising agencies, who act on behalf of the advertisers. Advertising agencies, such as Resolution Media and OMD Digital, may place insertion orders with us on behalf of advertisers (including State Farm) for particular advertising campaigns for a set period of time and are not obligated to commit beyond the campaign governed by a particular insertion order and may also cancel the campaign prior to completion. Advertising agencies also have relationships with many different providers, each of whom may be running portions of the advertising campaign. A significant reduction in advertising spending or budgets 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 have a material adverse effect on our future operating results.

Our ability to maintain and grow our revenues will depend in part on maintaining and increasing the number and volume of transactions with advertisers and advertising services providers and maintaining and increasing the number of phone calls and the other actions performed by users of our services through our distribution partners. We believe this is dependent in part on delivering quality traffic that ultimately results in purchases or conversions as well as providing through our call analytics platform quality data and insights that can measure the performance of advertising spend for our advertisers and advertising service providers. Our revenues are primarily generated using third party distribution networks to deliver the pay-for-call 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 and offline sources. We generate revenue upon delivery of qualified and reported phone calls 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, local leads platform for resellers, and campaign management services. Companies distributing advertising through mobile and internet based sources have experienced, and are likely to continue to experience consolidation. If we do not add new distribution partners or renew our existing distribution partner agreements and on terms as favorable as current arrangements, replace traffic lost from terminated distribution agreements with other sources, or if our distribution partners' businesses do not grow or are adversely affected, our revenue and results of operations may be materially and adversely affected. We utilize phone numbers as part of our pay-for-call and call analytic services to advertisers, which enables advertisers and other users of our services to help measure the effectiveness of mobile, online, and offline advertising campaigns. If we are not able to secure or retain sufficient phone numbers needed for our services or we are limited in the number of available telecommunication carriers or vendors to provide such phone numbers to us in the event of any industry consolidation or if telecommunication carriers or vendors were to experience system disruptions, our revenue and results of operations may be materially and adversely affected. In addition, 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 call volumes could materially and adversely affect our revenue and results of operations.

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 phone call usage, the number of phone calls or other actions performed by users of our products and services, which will be delivered to our advertisers, and how much advertisers will spend with us and the amount they are willing to pay for our products and services. It is even more difficult to anticipate the average revenue per phone call or other performance-based actions. 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 from our call advertising customers. 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 and in turn the market price of our securities. In the first quarter of the calendar year, this trend generally reverses with increased mobile and internet usage and often new budgets at the beginning of the year for many of our customers with fiscal years ending December 31. The seasonal purchasing cycles of some customers in certain industries may also be higher in the first half versus the latter half of the calendar year. Additionally, the current business environment and our industry has generally both resulted in, and we may continue to see, 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.

We believe that our future revenue growth will depend on, among other factors, our ability to attract new advertisers, compete effectively, maximize our sales efforts, demonstrate a positive return on investment for advertisers, successfully improve existing products and services, develop successful new products and services, and expand internationally. If we are unable to generate adequate revenue growth and to manage our expenses, we may continue to incur significant losses in the future and may not be able to achieve or maintain profitability.

Expenses

Expenses were as follows (in thousands):

	Nine months ended September 30,						Three months ended September 30,					
		% of			% of			% of			% of	
	2015	revenue		2016	revenue		2015	revenue		2016	revenue	
Service costs	$59,166	55	%	$60,964	60	%	$20,003	54	%	$18,505	60	%
Sales and marketing	11,969	11	%	16,733	17	%	4,266	12	%	5,562	18	%
Product development	23,608	22	%	21,859	22	%	7,769	21	%	6,832	22	%
General and administrative	14,925	14	%	15,815	16	%	4,721	13	%	5,320	17	%
Acquisition and disposition related costs	199	0	%	662	1	%	81	0	%	354	1	%
	$109,867	102	%	$116,033	115	%	$36,840	100	%	$36,573	119	%

We record stock-based compensation expense under the fair value method. Stock-based compensation expense was included in the following operating expense categories as follows (in thousands):

	Nine months ended September 30,		Three months ended September 30,	
	2015	2016	2015	2016
Service costs	$1,046	$565	$273	$160
Sales and marketing	893	1,321	339	353
Product development	1,843	1,367	620	206
General and administrative	4,027	3,993	1,119	1,060
Total stock-based compensation	$7,809	$7,246	$2,351	$1,779

See Note 3. Stock-based Compensation Plans of the Notes to Condensed Consolidated Financial Statements as well as our Critical Accounting Policies for additional information about stock-based compensation.

Service Costs. Service costs decreased 7% from $20.0 million in the three months ended September 30, 2015 to $18.5 million in the same period in 2016. The decrease in dollars was primarily attributable to a decrease in network and communication costs, personnel costs, stock-based compensation, travel costs, and fees paid to outside service providers totaling $1.4 million.

Service costs increased 3% from $59.2 million in the nine months ended September 30, 2015 to $61.0 million in the same period in 2016. The increase was primarily due to an increase in distribution partner payments of $5.9 million, offset partially by decreases in personnel costs, stock-based compensation, network and communication costs, travel costs, fees paid to outside service providers and other operating costs totaling $4.1 million.

As a percentage of revenues, service costs were 54% and 60% for the three months ended September 30, 2015 and 2016, respectively, and 55% and 60% for the nine months ended September 30, 2015 and 2016, respectively. The increase as a percentage of revenue was primarily due to an increase in distribution partner payments, as a percentage of revenue and revenues from our local leads platform comprising a lower proportion of revenue compared to the same period in 2015. Our local leads platform 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, 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 other sources of revenues, such as our local leads platform have no corresponding distribution partner payments and accordingly have a lower service cost as a percentage of revenue relative to our overall service cost percentage. In addition, advertisers from whom we generate a portion of our call advertising revenues through our local leads platform generally have lower service costs as a percentage of revenue relative to our overall service cost percentage. To the extent our local leads platform makes up a smaller percentage of our future operations, we expect that service costs will increase as a percentage of revenue. We expect service costs as a percentage of revenue in the near term to be stable to modestly higher relative to the most recent quarterly period. We also expect that in the longer term service costs will increase in absolute dollars and as a percentage of revenue in connection with any revenue increase as a result of costs associated with the expansion and additional investment in our communications and network infrastructure as we scale and adapt to increases in the volume of transactions, calls, and traffic and as we invest in our platforms.

Sales and Marketing. Sales and marketing expenses increased 30% from $4.3 million for the three months ended September 30, 2015 to $5.6 million in the same period in 2016. As a percentage of revenue, sales and marketing expenses were 12% and 18% for the three months ended September 30, 2015 and 2016, respectively. The increase in dollars and percentage of revenue was primarily attributable to an increase in personnel costs as a result of an increase in our sales force, travel costs, and employee separation related costs, totaling $1.6 million, offset partially by a decrease in outside marketing costs of $359,000.

Sales and marketing expenses increased 40% from $12.0 million for the nine months ended September 30, 2015 to $16.7 million in the same period in 2016. As a percentage of revenue, sales and marketing expenses were 11% and 17% for the nine months ended September 30, 2015 and 2016, respectively. The increase in dollars and percentage of revenue was primarily attributable to an increase in personnel costs as a result of an increase in our sales force, stock-based compensation, travel costs, fees paid to outside service providers, and employee separation related costs, totaling $5.2 million, offset partially by a decrease in outside marketing activities of $472,000. The percentage of revenue increase was also attributable to lower revenues in 2016.

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 and intermediate term to be relatively stable to modestly lower in absolute dollars and to increase in the longer term to the extent we expand our sales force, marketing initiatives, and look to further our international initiatives. 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.

Product Development. Product development expenses decreased 12% from $7.8 million for the three months ended September 30, 2015 to $6.8 million in the same period in 2016. The net decrease in dollars was primarily due to a decrease in personnel costs, stock-based compensation, travel costs, and fees paid to outside service providers totaling $917,000. As a percentage of revenue, product development expenses were relatively flat at 21% and 22% for the three months ended September 30, 2015 and 2016, respectively.

Product development expenses decreased 7% from $23.6 million for the nine months ended September 30, 2015 to $21.9 million in the same period in 2016. The net decrease in dollars was primarily due to a decrease in personnel costs, stock-based compensation, travel costs, fees paid to outside service providers, and depreciation totaling $1.8 million. As a percentage of revenue, product development expenses were relatively flat at 22% for the nine months ended September 30, 2015 and 2016.

In the near and intermediate term, we expect product development expenditures to be modestly lower 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.

General and Administrative. General and administrative expenses increased 13% from $4.7 million in the three months ended September 30, 2015 to $5.3 million in the same period in 2016. As a percentage of revenue, general and administrative expenses were 13% and 17% for the three months ended September 30, 2015 and 2016, respectively.

The increase in dollars and percentage of revenue was primarily due to an increase in personnel costs which included employee separation related costs, and fees paid to outside service providers totaling $1.0 million, which was offset partially by a decrease in bad debt expense and other operating expenses. The percentage of revenue increase was also attributable to lower revenues in 2016.

General and administrative expenses increased 6% from $14.9 million in the nine months ended September 30, 2015 to $15.8 million in the same period in 2016. As a percentage of revenue, general and administrative expenses were relatively flat at 14% and 16% for the nine months ended September 30, 2015 and 2016, respectively. The increase in dollars was primarily due to an increase in personnel costs which included employee separation related costs and fees paid to outside service providers totaling $1.3 million which was offset partially by a decrease in bad debt and other operating costs.

We expect our general and administrative expenses to be modestly higher in the near term and lower in the intermediate 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 compensation is impacted by market conditions relating to our stock price.

Impairment of goodwill. For the three months ended June 30, 2016, our stock price was impacted by volatility in the U.S. financial markets, and traded below the then book value for an extended period of time. Accordingly, we tested goodwill for impairment and concluded that the carrying value exceeded the estimated fair value of our single reporting unit and recognized an impairment loss during the second quarter of 2016 of $63.3 million. The estimated fair value of our single reporting unit was based on estimates of future operating results, discounted cash flows and other market-based factors, including our stock price. The goodwill impairment loss resulted primarily from a sustained decline in our common stock share price and market capitalization as well as lower projected revenue growth rates and profitability levels compared to historical results. The lower projected operating results reflected 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. As of September 30, 2016, we no longer have any goodwill on our balance sheet.

The testing of goodwill for impairment requires us to make significant estimates about our future performance and cash flows, as well as other assumptions. 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 changes in competition and market dynamics; significant and sustained declines in our stock price and market capitalization; a significant decline in its expected future cash flows or a significant adverse change in our business climate. These estimates and circumstances are inherently uncertain and can be affected by numerous factors, including changes in economic, industry or market conditions, changes in business operations, a loss of a significant customer, changes in competition, volatility in financial markets, or changes in the share price of our common stock and market capitalization.

Income Taxes. The income tax expense from continuing operations was $191,000 and $11,000 for the three and nine months ended September 30, 2015, respectively. This compares to income tax expense of $15,000 and $40,000 in the same periods in 2016, respectively, and was related to state income taxes. The effective tax rate differed from the expected effective tax rate of 34% due to full valuation allowance and to a lesser extent due to state income taxes, non-deductible stock-based compensation related to incentive stock options recorded under the fair-value method and other non-deductible amounts.

Discontinued Operations, net of tax. In April 2015, we sold certain assets related to Archeo's domain operations, including the bulk of its domain name portfolio. The operating results related to this disposition are shown as discontinued operations as well as the gain on sale, net of tax, of $22.2 million in the nine months ended September 30, 2015. In December 2015, we sold the remaining Archeo operations which did not meet the criteria for discontinued operations, and as a result the operating results are reflected in continuing operations. See Note 12. Discontinued Operations, Dispositions, and Other of the Notes to Condensed Consolidated Financial Statements for further discussion.

Net Income (Loss). Net income was $9,000 for the three months ended September 30, 2015 and was a net loss of ($5.9) million in the same period in 2016. The decrease was primarily due to lower revenues with total operating costs remaining relatively consistent year over year. We also incurred employee separation and facility termination related costs of $1.6 million in the third quarter of 2016.

Net income was $25.5 million for the nine months ended September 30, 2015 and was a net loss of $(78.3) million in the same period in 2016. The decrease was primarily attributable to a goodwill impairment charge in the second quarter of 2016 in the amount of $63.3 million and the sale of Archeo's domain operations in April 2015 which resulted in a $22.2 million gain in discontinued operations, net of tax, in the nine months ended September 30, 2015 with no corresponding amounts in 2016. The decrease to a lesser extent was a result of lower revenues, higher sales and marketing costs, and employee separation and facility termination related costs of $1.6 million incurred in the third quarter of 2016.

Liquidity and Capital Resources

As of September 30, 2016, we had cash and cash equivalents of $105.3 million and we had current and long term contractual obligations of $9.6 million, of which $3.5 million is for rent under our facility leases.

Cash used in operating activities for the nine months ended September 30, 2016 of approximately $2.9 million consisted primarily of a net loss of $78.3 million, adjusted for non-cash items of $74.4 million, which primarily includes impairment of goodwill, depreciation and amortization, allowance for doubtful accounts and advertiser credits, and stock-based compensation, and approximately $1.0 million used in working capital and other activities. Cash provided by operating activities for the nine months ended September 30, 2015 of approximately $12.0 million consisted primarily of net income of $25.5 million, adjusted for the gain on sale of discontinued operations of $22.2 million, non-cash items of $11.2 million, which primarily includes depreciation and amortization, allowance for doubtful accounts and advertiser credits, and stock-based compensation, and approximately $2.5 million used in working capital and other activities.

With respect to a significant portion of our call-based advertising services, the amount payable to our distribution partners will be calculated at the end of a calendar month, with a payment period following the delivery of the phone calls or other actions. These services constituted the majority of revenues for the three and nine months ended September 30, 2015 and 2016. We generally receive payment from advertisers in close proximity to the timing of the corresponding payments to the distribution partners who provide calls, other delivery actions, or 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 local leads platform.

Nearly all of our reseller partner arrangements are billed on a monthly basis following the month of our phone call or other action delivery. This payment structure results in our advancement of monies to the distribution partners who have provided the corresponding calls, other delivery actions, or placements of the listings. For these services, reseller partner payments are generally received two to four weeks following payment to the distribution partners. We also have payment arrangements with advertising agencies whereby we receive payment after the agency's advertiser pays the agency, which is generally between 60 and 120 days or longer, following the delivery of services. We expect that in the future periods, if the amounts from our reseller partner and agency 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 local leads and call advertising services, such as YP, CDK Global, hibu, Supermedia Inc., and Yellow Pages Ltd, whereby we receive payment generally between 30 and 60 days following the delivery of services. We also have payment arrangements with Resolution Media and OMD Digital, advertising agencies related to our call marketplace and call analytics services, whereby we receive payment when the agency's advertiser pays the agency, which is generally between 60 and 90 days following the delivery of services and in some instances may take longer.

For the nine months ended and as of September 30, 2016, amounts from these partners and agencies totaled 60% of revenue and $12.1 million in 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 and advertising agencies. A single advertiser, State Farm, who represented the majority of the revenue and accounts receivable generated by Resolution Media and OMD Digital, accounted for 24% of total revenues and 20% of accounts receivable for the nine months ended and as of September 30, 2016.

In 2015, we amended our arrangements with YP, extending them through December 31, 2016. The primary local leads platform arrangement included certain minimum fee commitments by YP through the first half of 2016 and provides YP additional flexibility to migrate active accounts to itself or a third-party provider prior to the end of an advertiser contract. We also have a separate distribution partner agreement with YP. There can be no assurance that our business with them in the future will continue at or near current revenue and contribution levels, that we will be able to renew and extend the contracts set to expire in December 2016, and, if renewed, the contracts are likely to be on less favorable terms to us, any of which could have a material adverse effect on our future operating results. Net accounts receivable balances outstanding at September 30, 2016 from YP totaled $4.5 million.

We have revenue concentrations with certain other large advertisers and advertising agencies and most of these customers are not subject to long term contracts with us or have contracts with near term expiration dates such as Yellow Pages Ltd, and are generally able to reduce or cease advertising spending at any time and for any reason. In some cases, we engage with advertisers through advertising agencies, who act on behalf of the advertisers. Advertising agencies, such as Resolution Media and OMD Digital, may place insertion orders with us on behalf of advertisers (including State Farm) for particular advertising campaigns for a set period of time and are not obligated to commit beyond the campaign governed by a particular insertion order and may also cancel the campaign prior to completion. Advertising agencies also have relationships with many different providers, each of whom may be running portions of the advertising campaign. A significant reduction in advertising spending or budgets 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 and profitability. This could have a material adverse effect on our results of operations and financial condition. 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.

Cash used in investing activities for the nine months ended September 30, 2016 of approximately $829,000 was primarily attributable to purchases for property and equipment of approximately $594,000 and cash paid for costs incurred as a result of the sale of the remaining Archeo assets of $224,000. Cash provided by investing activities for the nine months ended September 30, 2015 of approximately $21.6 million was primarily attributable to cash from the sale of the bulk of Archeo's domain operations, net of transaction costs, of $25.3 million. These amounts were partially offset by purchases for property and equipment of $3.6 million and purchases of intangible and other noncurrent assets of $46,000.

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. In the intermediate to long term, we also expect to increase the number of personnel supporting our sales, marketing and related growth initiatives.

Cash used in financing activities for the nine months ended September 30, 2016 of approximately $178,000 was primarily attributable to repurchases of 89,000 shares of Class B common stock for treasury and minimum tax withholding payments related to certain executive restricted stock award vests totaling $519,000, which was partially offset by proceeds primarily from employee stock option exercises and the employee stock purchase plan of $341,000. Cash used in financing activities for the nine months ended September 30, 2015 of approximately $4.7 million was primarily attributable to the payment of common stock dividends and repurchases of Class B common stock.

The following table summarizes our contractual obligations as of September 30, 2016, 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
Contractual Obligations:				
Operating leases	$3,527	$ 2,362	$1,165	$ —
Other contractual obligations	6,060	3,912	2,148	—
Total contractual obligations (1)	$9,587	$ 6,274	$3,313	$ —

(1) Our tax contingencies of $1.0 million 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.

As of September 30, 2016, we have a 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. In June 2016, we signed an amendment to the Credit Agreement that modifies the unused commitment fees, replaces certain financial covenants under the Credit Agreement with a covenant limiting outstanding balances not to exceed a defined ratio against our unrestricted cash and cash equivalent balances and a covenant with certain earnings thresholds, and modifies the levels and types of indebtedness and payments we may make. The Credit Agreement has a maturity date of April 1, 2017 and 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 nine months ended September 30, 2015 and 2016, the Company had no borrowings under the Credit Agreement.

In November 2014, our board of directors authorized a new share repurchase program (the “2014 Repurchase Program”) which supersedes and replaces any prior repurchase programs. Under the 2014 Repurchase Program, we are authorized to repurchase up to 3 million shares of our Class B common stock in the aggregate through open market and privately negotiated transactions, at such times and in such amounts as we deem appropriate. Repurchases may also be made under a Rule 10b5-1 plan, which would permit shares to be repurchased when we might otherwise be precluded from doing so under insider trading laws. 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. The 2014 Repurchase Program does not have an expiration date and may be expanded, limited or terminated at any time without prior notice.

In 2015, quarterly dividends of $0.02 per share were paid on February 17 and May 18, 2015 to the holders of record as of the close of business on February 6 and May 7, 2015, respectively. The aggregate quarterly dividend paid in February and May 2015 was $840,000 and $845,000, respectively. We discontinued paying dividends on our common stock after the second quarter of 2015, and we do not anticipate declaring or paying dividends in the foreseeable future.

Based on our operating plans we believe that our existing 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 through our existing credit facility or other financing arrangements may be needed to support our acquisition strategy, our long-term obligations and our company’s needs. There can be no assurance that, if we needed additional funds, our existing credit facility or additional financing arrangements would be available in amounts or on terms acceptable to us, if at all. 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 condensed consolidated financial statements have been prepared using accounting principles generally accepted in the United States for interim financial information. The preparation of these condensed 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;
- Goodwill;
- Stock-based compensation;
- Allowance for doubtful accounts and advertiser credits; and
- Provision for income taxes.

Revenue

We currently generate revenue by delivering call advertising services 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, and cost-per-action services. For pay-for-call advertising, revenue is recognized upon delivery of qualified and reported phone calls or other action 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 other action 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 websites or a third party website in our distribution network to an advertiser website and completes the specified action.

We have entered into agreements with various distribution partners in order to expand our distribution network, which includes search engines, directories, product shopping engines, third party vertical and branded websites, and mobile and offline sources. We generally pay distribution partners based on a specified percentage of revenue or a fixed amount per phone call or other action 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 we, in certain instances, are 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.

When an arrangement involves multiple deliverables, the entire fee from the arrangement is allocated to each respective deliverable based on its relative selling price and recognized when revenue recognition criteria for each deliverable are met. The selling price for each deliverable is established based on the sales price charged when the same deliverable is sold separately, the price at which a third party sells the same or similar and largely interchangeable deliverable on a standalone basis or the estimated selling price if the deliverable were to be sold separately.

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 owed that occurs subsequent to period ends.

Goodwill

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.

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 allow us to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. The testing of goodwill for impairment requires us to make significant estimates about our future performance and cash flows, as well as other assumptions. 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 changes in competition and market dynamics; significant and sustained declines in our stock price and market capitalization; a significant decline in our expected future cash flows or a significant adverse change in our business climate. These estimates and circumstances are inherently uncertain and can be affected by numerous factors, including changes in economic, industry or market conditions, changes in business operations, a loss of a significant customer, changes in competition, volatility in financial markets, or changes in our share price of our common stock and market capitalization.

We recognized an impairment loss during the second quarter of 2016 of $63.3 million. As of September 30, 2016, we have no goodwill on our balance sheet.

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 be 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.

We may issue equity awards of stock options and restricted stock awards 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 use 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 3 Stock-based Compensation Plans in the Condensed Notes to Consolidated Financial Statements for additional information.

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.

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 are subject to income taxes in the U.S. Significant judgment is required in evaluating our uncertain tax positions and determining our 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. Uncertain tax positions as of September 30, 2016 amounted to $1.0 million.

We determined that it is not more likely than not that its deferred tax assets will be realized and accordingly recorded 100% valuation allowance against these deferred tax assets as of December 31, 2015 and September 30, 2016. 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 the industry, existing contracts, our ability to project future results and any appreciation of its other assets. The ultimate realization of deferred tax assets depends on the generation of future taxable income during the periods in which those temporary differences are deductible. We considered the future reversal of deferred tax liabilities, carryback potential, projected taxable income, and tax planning strategies as well as its history of taxable income or losses in the relevant jurisdictions in making this assessment. Based on the level of historical taxable losses and the uncertainty of projections for future taxable income over the periods for which the deferred tax assets are deductible, we concluded that it is not more likely than not that the gross deferred tax assets will be realized.

Recent Accounting Pronouncement Not Yet Effective

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which amends the existing accounting standards for revenue recognition. ASU 2014-09 requires an entity to recognize the amount of revenue to which it expects to be entitled when products or services are transferred to customers. In July 2015, the FASB voted to approve a one-year delay of the effective date. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within those annual periods. ASU 2014-09 may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. In 2016, the FASB issued additional guidance to clarify the implementation guidance. We are currently in the process of evaluating the impact of adoption of ASU 2014-09 on our consolidated financial statements.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, Income Taxes (Topic 740), Balance Sheet Classification of Deferred Taxes (ASU 2015-17), an ASU amending the accounting for income taxes and requiring all deferred tax assets and liabilities to be classified as non-current on the consolidated balance sheet. The ASU is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. The ASU may be adopted either prospectively or retrospectively. We do not expect adoption of ASU 2015-17 to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 Leases (Topic 842), an ASU requiring the recognition of lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU is effective for reporting periods beginning after December 15, 2018, with early adoption permitted. The ASU must be adopted retrospectively. We are currently in the process of evaluating the impact of adoption of ASU 2016-02 on our consolidated financial statements.

In March 2016, the FASB amended the existing accounting standards for stock-based compensation, with Accounting Standards Update No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). The amendments impact several aspects of accounting for share-based payment transactions, including the income tax consequences, forfeitures, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The ASU is effective for reporting periods beginning after December 15, 2016, with early adoption permitted. If early adoption is elected, all amendments must be adopted in the same period. The manner of application varies by the various provisions of the guidance, with certain provisions applied on a retrospective or modified retrospective approach, while others are applied prospectively. We are currently evaluating the impact of these amendments and the transition alternatives on our consolidated financial statements.

In June 2016, the FASB issued Accounting Standards Update No. 2016-13, Financial Instruments — Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments (ASU 2016-13), an ASU amending the impairment model for most financial assets and certain other instruments. The ASU is effective for reporting periods beginning after December 15, 2019, with early adoption permitted after December 15, 2018. The ASU must be adopted using a modified-retrospective approach. We do not expect adoption of ASU 2016-13 to have a material impact on our consolidated financial statements.

Web site

Our web site, 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://www.marchex.com/blog)

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 Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Our exposure to market risk is limited to foreign currency and 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. Due to the nature of our short-term investments, we believe that we are not subject to any material market risk exposure. We do not have any material foreign currency or other derivative financial instruments. The effect of changes in foreign currency exchange rates on our operating results was not material.

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.

Item 4. 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 principal executive officer and our principal 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 principal executive officer and our principal financial officer have concluded that, as of the date of the evaluation, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

During the quarter ended September 30, 2016, 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.

Part II—Other Information

Item 1. 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 products and services.

Item 1A. Risk Factors

Set forth below and elsewhere in this report and in other documents we file with the SEC are risks and uncertainties that could cause our actual results to materially differ from the results contemplated by the forward-looking statements contained in this report and in other documents we file with the SEC. Some of the risk factors were previously disclosed in our December 31, 2015 Annual Report on Form 10-K. They have been updated to include information as of November 7, 2016.

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 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 $241.8 million as of September 30, 2016. 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 believe that our future revenue growth will depend on, among other factors, our ability to attract new advertisers, compete effectively, maximize our sales efforts, demonstrate a positive return on investment for advertisers, successfully improve existing products and services, develop successful new products and services and expand internationally. If we are unable to generate adequate revenue growth and to manage our expenses, we may continue to incur significant losses in the future and may not be able to achieve or maintain profitability.

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 10% of total revenues for the nine months ended September 30, 2016. 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 or contribution 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. desktop search marketplace for August 2016, Yahoo! and Microsoft accounted for 11.9% and 22.0%, respectively, of the core search market in the United States and Google accounted for 63.6%. 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 Google, Microsoft, and Yahoo! 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, Resolution Media, OMD Digital, hibu, Inc., CDK Global, Yodle, and Yellow Pages Ltd 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 and agencies 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 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 YP, we generate revenues from our local leads platform. We also have a separate pay-for-call arrangement with YP. In 2015, we extended these arrangements through December 31, 2016. The primary local leads platform arrangement included certain minimum fee commitments by YP through the first half of 2016 and provides YP additional flexibility to migrate active accounts to itself or a third-party provider prior to the end of an advertiser contract. YP is our largest reseller partner and was responsible for 23% of our total revenues for the nine months ended September 30, 2016. We expect YP may decrease the number of new advertiser accounts with us and may elect to migrate certain active accounts to itself or a third party provider which would result in fewer small business accounts and related revenues, as well as reduced contribution and profitability. We also have a separate distribution partner agreement with YP. There can be no assurance that our business with them in the future will continue at or near current revenue and contribution levels, that we will be able to renew and extend the contracts set to expire in December 2016, and if renewed, the contracts are likely to be on less favorable terms to us, any of which could have a material adverse effect on our future operating results.

We also have arrangements with advertising agencies, such as Resolution Media and OMD Digital, who act on an advertiser’s behalf and may represent more than one advertiser that utilizes our products and services. Our primary arrangements with Resolution Media and OMD Digital are for pay-for-call services whereby we charge an agreed-upon price for qualified calls or leads from our network and call analytic services. Resolution Media and OMD Digital accounted for 21% and less than 10% of total revenues, respectively, for the nine months ended September 30, 2016.

These reseller partners and agencies may in certain cases be subject to negotiated terms and conditions separate from those applied to advertising clients. 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 61% of our revenue from our five largest customers for both the year ended December 31, 2015 and the nine months ended September 30, 2016, 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 61% of our total revenues for both the year ended December 31, 2015 and the nine months ended September 30, 2016. YP and Resolution Media were our largest customers and were responsible for 23% and 21% of our total revenues, respectively, for the nine months ended September 30, 2016.

Through our primary contract with YP, we generate revenues from our local leads platform. We also have a separate pay-for-call services arrangement with YP. In 2015, we extended these arrangements through December 31, 2016. The primary local leads platform arrangement included certain minimum fee commitments by YP through the first half of 2016 and provides YP additional flexibility to migrate active accounts to itself or a third-party provider prior to the end of an advertiser contract. We expect YP may decrease the number of new advertiser accounts with us and may elect to migrate certain active accounts to itself or a third party provider which would result in fewer small business accounts and related revenues, as well as reduced contribution and profitability. We also have a separate distribution partner agreement with YP. There can be no assurance that our business with them in the future will continue at or near current revenue and contribution levels, that we will be able to renew and extend the contracts set to expire in December 2016, and, if renewed, the contracts are likely to be on less favorable terms to us, any of which could have a material adverse effect on our future operating results.

Our primary arrangement with Resolution Media, who acts as an agent on advertisers' behalf, is for pay-for-call services whereby we charge an agreed upon price for qualified calls or leads from our network and call analytic services. A single advertiser, State Farm, represented the majority of the revenue generated by Resolution Media for the nine months ended September 30, 2016. State Farm, who utilizes our services through multiple relationships, accounted for 24% of total revenues for the nine months ended September 30, 2016.

Many of our other largest customers are not subject to long term contracts with us or have contracts with near term expiration dates such as Yellow Pages Ltd, and are able to reduce or cease advertising spend at any time and for any reason. In some cases, we engage with our customers through advertising agencies, who act on behalf of the customer. Advertising agencies, such as Resolution Media and OMD Digital, may place insertion orders with us on behalf of advertisers (including State Farm) for particular advertising campaigns for a set period of time and are not obligated to commit beyond the campaign governed by a particular insertion order and may also cancel the campaign prior to completion. Advertising agencies also have relationships with many different providers, each of whom may be running portions of the advertising campaign. A significant reduction in advertising spending or budgets 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 have a material adverse effect on our future operating results.

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.

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 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 or third parties they may contract with 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. Any costs incurred as a result of activities of our distribution partners and their third party partners could have a material adverse effect on our business, operating results and financial condition.

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 websites. 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 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. 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 depends in part 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 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 may 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.

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 agencies, 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 or other actions such as non-human processes, including robots or robocallers, spiders or other software, the mechanical automation of calling or clicking, and other types of invalid calls or clicks, call or click fraud, or call 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 phone calls and Internet traffic, 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 automated voice and mobile advertising-based technologies are heavily reliant on vendors.

Certain voice and mobile advertising-based products 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.

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, and claims of copyright infringement with respect to certain of our websites 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, our existing credit facility or 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;

- 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;

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- 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 international operations and any expansion subjects us to additional risks and uncertainties and we may not be successful with our strategy to expand such operations.

One potential area of growth for us is in international markets. We have operations, through our international subsidiaries, in other countries. Currently, we have international subsidiaries in Australia, Canada, Ireland, and the United Kingdom. We are exploring various customer opportunities internationally. Any 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. We may also have to offer our products and services in a modified format which may not be as compelling to certain customers, and we are subject to increased foreign currency exchange rate risks and our international operations and any expansion will require additional management attention and resources. We cannot assure you that we will be successful in any 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, including the possibility of storing data locally if customers require;
- difficulties in managing operations due to language barriers, distance, staffing and cultural differences;
- application of foreign laws and regulations to us, in particular data and privacy regulations in Europe and other international jurisdictions, which continue to change and impose significantly more liability and product limitations on service providers in our industry;
- compliance with anti-bribery laws, such as the Foreign Corrupt Practices Act and the UK Anti-Bribery Act;
- tariffs and other trade barriers;
- fluctuations in currency exchange rates;
- establishing local offices, sales channels, management systems and infrastructures;
- reduced protection for intellectual property rights in some countries;
- changes in foreign political and economic conditions;
- compliance with the laws of numerous taxing jurisdictions, both foreign and domestic;
- foreign exchange controls that might prevent us from repatriating cash earned outside the United States;
- the complexity and potentially adverse tax consequences of U.S. tax laws as they relate to our international operations;
- increased costs to establish and maintain effective controls at foreign locations; and
- overall higher costs of doing business internationally.

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 other key personnel, could harm our current and future operations and prospects.

We are heavily dependent upon the continued services of members of our senior management team and other key personnel. Each member of our senior management team and other key personnel are at-will employees and may voluntarily terminate his or her 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. The loss of the services of any member of our senior management, including other key personnel, for any reason, or any conflict among our senior management or other key personnel, could harm our current and future operations and prospects.

We have experienced recent turnover in certain senior executives at our Company. In particular, our chief executive officer resigned, by mutual agreement, from the Company and our executive chairman resigned as a member of the Board of Directors in October 2016. As a result, our Board of Directors has established an Interim Office of the CEO consisting of Michael Arends, Ethan Caldwell, Gary Nafus and Russell C. Horowitz and subject to oversight by our Chairman, Anne Devereux-Mills. We are currently working with an executive search firm to locate a successor chief executive officer, although we may not be successful in finding or hiring a suitable replacement. Additional turnover at the senior management level may create instability within the Company and our employees may decide to terminate their employment, which could further impede the Company's maintenance of its day to day operations. Such instability could impede our ability to implement fully our business plan and growth strategy, which would harm our business and prospects.

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 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 would result in a decrease in earnings.

Current accounting rules require that goodwill be tested for impairment at least annually and reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. 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; and significant changes in competition and market dynamics. These estimates are inherently uncertain and can be affected by numerous factors, including changes in economic, industry or market conditions, changes in business operations, a loss of a significant customer, changes in competition or changes in the share price of our common stock and market capitalization. Significant and sustained declines in the stock price and market capitalization, a significant decline in expected future cash flows or a significant adverse change in the business climate, among other factors, could result in the need to perform an impairment analysis.

During the three months ended June 30, 2016, the Company tested goodwill for impairment and recorded a non-cash impairment loss of $63.3 million. We determined that the carrying exceeded the estimated fair value of our single reporting unit. The goodwill impairment resulted primarily from a sustained decline in the Company's common stock share price and market capitalization as well as lower projected revenue growth rates and profitability levels compared to historical results. As of September 30, 2016, we have no goodwill on our balance sheet.

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. We increased the valuation allowance by $22.3 million to record a full valuation allowance against our deferred tax assets as of September 30, 2014 resulting in a corresponding income tax expense of $22.3 million for the third quarter of 2014. As of September 30, 2016, our deferred tax assets were $43.4 million and we have provided a full valuation allowance of $43.4 million as we believe it is not more likely than not that these assets will be realized.

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

We display pay-for-call listings on third party domain names and third party websites that are part of our distribution network, which could subject us to a wide variety of civil claims including intellectual property ownership and infringement. 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.

We may face risks related to litigation that could result in significant legal expenses and settlement or damage awards.

From time to time, we are subject to claims and litigation, which could seriously harm our business and require us to incur significant costs.

We are generally obliged, to the extent permitted by law, to indemnify our current and former directors and officers who are named as defendants in these types of lawsuits. Defending against litigation may require significant attention and resources of management. Regardless of the outcome, such litigation could result in significant legal expenses.

If we are a party to material litigation and if the defenses we claim are ultimately unsuccessful, or if we are unable to achieve a favorable settlement, we could be liable for large damage awards that could have a material adverse effect on our business and consolidated financial statements.

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;
- delivery of pay-for-call advertising to end users or customers of advertisers through mobile and online destination websites or other offline distribution outlets;
- sales to advertisers of call tracking and call analytics;
- services and outsourcing of technologies that allow advertisers to manage their advertising campaigns across multiple networks and track the success of these campaigns;
- aggregation or optimization of online advertising for distribution through mobile and online search engines and applications, product shopping engines, directories, websites or other offline outlets;
- provision of local and vertical websites 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 online advertising to end users or customers of advertisers through mobile and online destination websites or other offline distribution outlets; and
- local search sales training.

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 leading search engines and digital advertising networks such as Google, Microsoft, and Yahoo!. We also compete with call analytics technology providers such as Twilio, Telemetrics, Invoca, DialogTech and Convirza. As we continue to advance our data analytics technologies, we anticipate facing increased competition from companies providing more broad advertising solutions, such as data management companies like Datalogix. We also face competition on the call supply side, where competing mobile ad companies like xAd look to outbid, partner with or otherwise secure sources of call supply we utilize. 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. 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 digital/online 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 mobile or 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.

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 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.

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, including those of our vendors or partners, are breached or are perceived as not being secure, we may lose advertisers, reseller partners and distribution partners and as a result we may incur significant legal and financial exposure and suffer an adverse effect on our business.

We store and transmit data and information about our advertisers, reseller partners, distribution partners and their respective users. We also work with vendors and partners who may come into contact with certain data, such as carriers, colocation and data storage facilities and distribution partners referring callers. 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, as well as to assist in the delivery of services to our advertisers, 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. Similarly, security breaches of our vendors and partners, or ineffective data security by our vendors or partners, may result in similar significant liability. In addition, security breaches, actual or perceived, could result in legal liability, government fines, and 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 were also filed: 14/045,536 titled “Method and System for Phone Number Cleaning” was filed November 3, 2013; 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 October 18, 2013, and 14/065,345 titled “Method and System for Tracking Telephone Calls” was filed October 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 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 Number 8,259,915 entitled “System and Method to Analyze Calls to Advertised Telephone Numbers” was issued September 4, 2012 and its continuation Patent Number 8,788,344 was issued July 22, 2014.
- U.S. Patent Number 8,630,393 entitled “System and Method for Blocking Telephone Calls” was issued January 14, 2014.
- 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.
- U.S. Patent Number 9,367,846 entitled “Telephone Search Supported By Advertising Based On Past History Of Requests” was issued June 14, 2016.
- 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 Number 8,929,522 entitled "System and Method to Customize a Connection Interface for Multimodal Connection to a Telephone Number" was issued January 16, 2015.
- U.S. Patent Number 8,634,520 entitled "Call Tracking System Utilizing an Automated Filtering Function" was issued January 21, 2014.
- U.S. Patent Number 8,671,020 entitled "Call Tracking System Utilizing a Pooling Algorithm" was issued March 11, 2014.
- U.S. Patent Number 8,687,782 entitled "Call Tracking System Utilizing a Sampling Algorithm" was issued April 1, 2014.
- 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. Provisional Patent Application Number 61/801,893 entitled "Cross-Channel Targeting Using Historical Online and Call Data" filed March 15, 2013, and its continuation Patent Application Number 15/019,826 entitled "Cross-Channel Correlation of Consumer Telephone Numbers and User Identifiers" was filed February 9, 2016.
- U.S. Patent Number 9,118,751 entitled "System and Method for Analyzing and Classifying Calls without Transcription" was issued August 25, 2015 and its continuation U.S. Patent Application Number 14/834,196 entitled "System and Method for Analyzing and Classifying Calls Without Transcription" was filed August 24, 2015, and will issue as U.S. Patent Number 9,484,026 on November 1, 2016.
- U.S. Patent Number 9,263,038 entitled "System and Method for Analyzing and Classifying Calls Without Transcription via Keyword Spotting" was issued February 16, 2016, and its continuation Patent Application Number 14/990,221 was filed January 7, 2016.
- U.S. Patent Number 9,232,052 entitled "Analyzing Voice Characteristics to Detect Fraudulent Call Activity and Take Corrective Action Without Using Recording, Transcription or Caller ID" was issued January 5, 2016 and its continuation Patent Application Number 14/987,565 was filed January 4, 2016.
- U.S. Patent Application Number 14/550,089 entitled "Identifying Call Characteristics to Detect Fraudulent Call Activity and Take Corrective Action Without Using Recording, Transcription or Caller ID" was filed November 21, 2014.
- U.S. Patent Application Number 14/714,141 entitled "Call Analytics for Mobile Advertising" was filed May 15, 2015.
- U.S. Patent Application Number 14/721,912 entitled "Identifying Call Features and Associations to Detect Call Traffic Pumping and Take Corrective Action" was filed May 26, 2015, claiming priority to 62/159,086 filed May 8, 2015, and will issue as U.S. Patent Number 9,485,354 on November 1, 2016.

In the future, additional patent applications 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 patent applications, 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 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 from our call advertising customers. 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, and in turn, the market price of our securities. In the first quarter of the calendar year, this trend generally reverses with increased mobile and Internet usage and often new budgets at the beginning of the year for many of our customers with fiscal years ending December 31. The seasonal purchasing cycles of some customers in certain industries may also be higher in the first half versus the latter half of the calendar year. Additionally, the current business environment and our industry has both resulted in, and we may continue to see, many advertisers and reseller partners reducing advertising and marketing services budgets or changing such budgets throughout the year, which we expect may impact our quarterly results of operations in addition to typical seasonality seen in our industry.

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 data 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.

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 websites. 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 website operators and online service providers that do not comply with the law. We do not currently offer any websites 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. At least one state already has enacted a law, which went 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 countries may enact 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, Data Protection Directives (and similar legislation in other countries where we may have operations), and the recently enacted EU General Data Protection Regulation, which is directly applicable to all member states. 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, state, and foreign 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 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.
- Our international operations may expose us to telecommunications regulations in the countries where we are operating and these regulations could negatively affect the viability of our business in those regions.

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.

The federal government has placed a ban for now on state and local governments’ imposition of new taxes on Internet access or electronic commerce transactions through the Internet Tax Freedom Act. The proposed Marketplace Fairness Act, 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 Class B 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 and has more recently declined significantly. 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:

- actual or anticipated fluctuations in our operating results;
- 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;
- loss of senior management or other key personnel;
- registration of additional shares of Class B common stock in connection with acquisitions;
- lawsuits initiated against us or lawsuits initiated by us;
- announcements of acquisitions or technical innovations;

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- potential loss or reduced contributions from distribution partners, reseller partners and agencies, or advertisers;
- significant volatility in the market price and trading volume of technology companies in general and of companies in the digital advertising industry in particular;
- 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;
- 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 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, as amended (the “Exchange Act”);
- short sales, hedging and other derivative transactions on shares of our Class B common stock; and
- an adverse impact on us from any of the other risks cited n this Risk Factors section.

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 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.

If securities analysts do not continue to publish research or publish negative research about our business, our stock price and trading volume could decline.

The trading market for our Class B common stock depends in part on the research and reports that securities analysts publish about us or our business. If one or more of the analysts who covers us downgrades our stock or publishes negative research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, we could lose visibility in the market for our stock and demand for our stock could decrease, which could cause our stock price or trading volume to decline.

Our 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 September 30, 2016, Russell C. Horowitz, Ethan A. Caldwell and Peter Christothoulou, three of our founders, beneficially owned 100% of the outstanding shares of our Class A common stock, which shares represented 78% of the combined voting power of all outstanding shares of our capital stock. These founders together controlled 78% of the combined voting power of all outstanding shares of our capital stock as of September 30, 2016. 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 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 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 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 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 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 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 pay dividends on our Class B 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 initiated and paid a quarterly dividend on our Class B common stock from November 2006 through May 2015. Our ability to pay dividends in the future will depend on our financial results, liquidity and financial condition. We currently do not anticipate declaring or paying dividends in the foreseeable future.

Item 2. Issuer Purchases of Equity Securities

During the third quarter of 2016, 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 (1)
Class B Common Shares:				
August 1, 2016 – August 31, 2016 (3)	2,565	$ 2.81	—	1,319,128
September 1, 2016 – September 30, 2016 (2), (3)	174,097	$ 0.32	—	1,319,128
Total Class B Common Shares	176,662	$ 0.35	—	1,319,128

(1) In November 2014, we established a 2014 share repurchase program, which supersedes and replaces any prior repurchase programs, and authorized the Company to repurchase up to 3 million shares in the aggregate 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.
(2) Includes 155,000 shares of restricted equity subject to vesting, which were issued to a certain employee and not already vested, repurchased for $0.01 per share upon termination of employment.
(3) Includes 2,565 and 19,097 shares of Class B common stock repurchased to satisfy certain employees' minimum tax withholding obligations in connection with the vesting of restricted stock awards for the months ended August 31, 2016 and September 30, 2016, and were based on the fair market value on the vesting date.

Item 4. Mine Safety Disclosures

Not applicable.

Item 6. Exhibits

Exhibits:

†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.

† Filed herewith.
†† Furnished herewith.

SIGNATURE

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

	MARCHEX, INC.	
Date: November 7, 2016	By:	/s/ MICHAEL A. ARENDS
	Name:	Michael A. Arends
	Title:	Chief Financial Officer
		(Principal Financial and
		Accounting Officer)

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