

LIVEPERSON INC  
Form 10-K  
March 13, 2012

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

**FORM 10-K**

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

**For the Fiscal Year Ended December 31, 2011**

**OR**

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**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 000-30141**

**LIVEPERSON, INC.**

(Exact Name of Registrant As Specified in Its Charter)

Delaware  
(State of Incorporation)

13-3861628  
(I.R.S. Employer  
Identification Number)

**475 Tenth Avenue, 5th Floor,  
New York, New York 10018**

(Address of Principal Executive Offices) (Zip Code)

**(212) 609-4200**

(Registrant's Telephone Number, Including Area Code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value \$0.001 per share	The Nasdaq Stock Market LLC

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

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

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting

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company in Rule 12b-2 of the Exchange Act. (Check one).

Large accelerated filer  Accelerated filer  Non-accelerated filer  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

The aggregate market value of the voting common stock held by non-affiliates of the registrant as of June 30, 2011 (the last business day of the registrant's most recently completed second fiscal quarter) was approximately \$679,426,321 (computed by reference to the last reported sale price on The Nasdaq Capital Market on that date). The registrant does not have any non-voting common stock outstanding.

On February 28, 2012, 54,543,837 shares of the registrant's common stock were outstanding.

## DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for the 2012 Annual Meeting of Stockholders, to be filed not later than April 30, 2012, are incorporated by reference into Items 10, 11, 12, 13 and 14 of Part III of this Form 10-K.

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TABLE OF CONTENTS

**LIVEPERSON, INC.**

**2011 ANNUAL REPORT ON FORM 10-K**

**TABLE OF CONTENTS**

	Page
PART I	
<u>Item 1.</u>	1
<u>Business</u>	
<u>Item 1A.</u>	11
<u>Risk Factors</u>	
<u>Item 1B.</u>	27
<u>Unresolved Staff Comments</u>	
<u>Item 2.</u>	27
<u>Properties</u>	
<u>Item 3.</u>	28
<u>Legal Proceedings</u>	
<u>Item 4.</u>	29
<u>Mine Safety Disclosures</u>	
PART II	
<u>Item 5.</u>	30
<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	
<u>Item 6.</u>	32
<u>Selected Consolidated Financial Data</u>	
<u>Item 7.</u>	34
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	
<u>Item 7A.</u>	45
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	
<u>Item 8.</u>	47
<u>Consolidated Financial Statements and Supplementary Data</u>	

<u>Item 9.</u>	<u>74</u>
<u>Changes in and Disagreements With Accountants on Accounting and Financial Disclosure</u>	
<u>Item 9A.</u>	<u>74</u>
<u>Controls and Procedures</u>	
<u>Item 9B.</u>	<u>76</u>
<u>Other Information</u>	
PART III	
<u>Item 10.</u>	<u>76</u>
<u>Directors, Executive Officers and Corporate Governance</u>	
<u>Item 11.</u>	<u>76</u>
<u>Executive Compensation</u>	
<u>Item 12.</u>	<u>76</u>
<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	
<u>Item 13.</u>	<u>77</u>
<u>Certain Relationships and Related Transactions, and Director Independence</u>	
<u>Item 14.</u>	<u>77</u>
<u>Principal Accountant Fees and Services</u>	
PART IV	
<u>Item 15.</u>	<u>78</u>
<u>Exhibits and Financial Statement Schedules</u>	

TABLE OF CONTENTS

## **CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS**

STATEMENTS IN THIS REPORT ABOUT LIVEPERSON, INC. THAT ARE NOT HISTORICAL FACTS ARE FORWARD-LOOKING STATEMENTS BASED ON OUR CURRENT EXPECTATIONS, ASSUMPTIONS, ESTIMATES AND PROJECTIONS ABOUT LIVEPERSON AND OUR INDUSTRY. THESE FORWARD-LOOKING STATEMENTS ARE SUBJECT TO RISKS AND UNCERTAINTIES THAT COULD CAUSE ACTUAL FUTURE EVENTS OR RESULTS TO DIFFER MATERIALLY FROM SUCH STATEMENTS. THESE FORWARD-LOOKING STATEMENTS ARE BASED ON OUR CURRENT EXPECTATIONS, WHICH MAY NOT PROVE TO BE ACCURATE. MANY OF THESE STATEMENTS ARE FOUND IN THE BUSINESS AND MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS SECTIONS OF THIS FORM 10-K. WHEN USED IN THIS FORM 10-K, THE WORDS ESTIMATES, EXPECTS, ANTICIPATES, PROJECTS, PLANS, INTENDS, BELIEVES AND VARIOUS SUCH WORDS OR SIMILAR EXPRESSIONS ARE INTENDED TO IDENTIFY FORWARD-LOOKING STATEMENTS. ALL FORWARD-LOOKING STATEMENTS, INCLUDING, WITHOUT LIMITATION, OUR EXAMINATION OF HISTORICAL OPERATING TRENDS, ARE BASED UPON OUR CURRENT EXPECTATIONS AND VARIOUS ASSUMPTIONS. OUR EXPECTATIONS, BELIEFS AND PROJECTIONS ARE EXPRESSED IN GOOD FAITH, AND WE BELIEVE THERE IS A REASONABLE BASIS FOR THEM, BUT WE CANNOT ASSURE YOU THAT OUR EXPECTATIONS, BELIEFS AND PROJECTIONS WILL BE REALIZED. ANY SUCH FORWARD-LOOKING STATEMENTS ARE MADE PURSUANT TO THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. IT IS ROUTINE FOR OUR INTERNAL PROJECTIONS AND EXPECTATIONS TO CHANGE AS THE YEAR OR EACH QUARTER IN THE YEAR PROGRESS, AND THEREFORE IT SHOULD BE CLEARLY UNDERSTOOD THAT THE INTERNAL PROJECTIONS AND BELIEFS UPON WHICH WE BASE OUR EXPECTATIONS MAY CHANGE PRIOR TO THE END OF EACH QUARTER OR THE YEAR. ALTHOUGH THESE EXPECTATIONS MAY CHANGE, WE ARE UNDER NO OBLIGATION TO INFORM YOU IF THEY DO. ACTUAL EVENTS OR RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTAINED IN THE PROJECTIONS OR FORWARD-LOOKING STATEMENTS. IMPORTANT FACTORS THAT COULD CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM THE FORWARD-LOOKING STATEMENTS WE MAKE IN THIS FORM 10-K ARE SET FORTH IN THIS FORM 10-K, INCLUDING THE FACTORS DESCRIBED IN THE SECTION ENTITLED ITEM 1A RISK FACTORS. IF ANY OF THESE RISKS OR UNCERTAINTIES MATERIALIZE, OR IF ANY OF OUR UNDERLYING ASSUMPTIONS ARE INCORRECT, OUR ACTUAL RESULTS MAY DIFFER SIGNIFICANTLY FROM THE RESULTS THAT WE EXPRESS IN OR IMPLY BY ANY OF OUR FORWARD-LOOKING STATEMENTS. WE DO NOT UNDERTAKE ANY OBLIGATION TO REVISE THESE FORWARD-LOOKING STATEMENTS TO REFLECT FUTURE EVENTS OR CIRCUMSTANCES.

TABLE OF CONTENTS

## **PART I**

### **Item 1. Business**

#### **Overview**

LivePerson, Inc. ( LivePerson , the Company , we or our ) is a leading provider of online engagement solutions offering a cloud-based platform which enables businesses to pro-actively connect with consumers through chat, voice, and content delivery, across multiple channels and screens, including websites, social media, and mobile devices. Our engagements are driven by intelligence derived from a broad set of consumer and business data, including historical, behavioral, operational, and third party data. Each engagement is based on proprietary analytics and a real-time understanding of consumer needs and business objectives. LivePerson's products, coupled with our domain knowledge and industry expertise, have been proven to maximize the effectiveness of the online channel by increasing sales, as well as consumer satisfaction and loyalty ratings for our customers, while also enabling them to reduce consumer service costs.

LivePerson monitors and analyzes a valuable set of online consumer behavioral data on behalf of our customers. Spanning the breadth of an online visitor session starting from an initial keyword search, through actions on our customer's website, and even into a shopping cart and an executed sale, this data enables us to develop unique insights into consumer behavior during specific transactions and within a customer's user base. Based on our internal measures, on average during 2011, we monitored approximately 1.4 billion visitor sessions per month across our customers' websites. Today this session data is primarily used to proactively engage consumers in order to increase online conversion rates and average order values, and we continue to invest in products that can leverage the value of this data to provide new and innovative solutions for our customers.

More than 8,500 companies, including Cisco, Hewlett-Packard, IBM, Microsoft, Verizon, Sky, Walt Disney, PNC, QVC and Orbitz employ our technology to keep pace with rising consumer expectations for service and relevance through the online channel. LivePerson has unique insight into consumer behavior, which we offer our customers through our intelligent engagement products and our consulting services.

Bridging the gap between visitor traffic and successful business outcomes, our business solutions deliver measurable return on investment by enabling our customers to:

- increase conversion rates and reduce abandonment by selectively engaging website visitors;
- accelerate the sales cycle, drive repeat business and increase average order values;
- increase consumer satisfaction, retention and loyalty while reducing consumer service costs;
- refine and improve performance by understanding which initiatives deliver the highest rate of return; and

lower operating costs in the call center by deflecting costly phone and email interactions and improving agent efficiency.

As a cloud computing or software-as-a-service (SaaS) provider, LivePerson provides solutions on a hosted basis. This model offers significant benefits over premise-based software, including lower up-front costs, faster implementation, lower total cost of ownership (TCO), scalability, cost predictability and simplified upgrades. Organizations that adopt multi-tenant architecture that is fully hosted and maintained by LivePerson eliminate the majority of the time, server infrastructure costs and IT resources required to implement, maintain and support traditional on-premise software. According to a recent study by Forrester Research 31% of companies are moderate to heavy users of SaaS software and 68% of larger companies have begun adopting SaaS software solutions.

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Our consumer services offering is an online marketplace that connects independent service providers (Experts) who provide information and knowledge for a fee via real-time chat with individual consumers (Users). Users seek assistance and advice in various categories including personal counseling and coaching, computers and programming, education and tutoring, spirituality and religion, and other topics.

1

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## TABLE OF CONTENTS

LivePerson was incorporated in the State of Delaware in November 1995 and the LivePerson service was introduced in November 1998. In April 2000, the company completed an initial public offering and is currently traded on the Nasdaq and the Tel Aviv Stock Exchange. LivePerson is headquartered in New York City with offices in Atlanta, London, San Francisco, Melbourne, and Tel Aviv.

## **Market Opportunity**

While many sectors of the global economy are challenged to maintain historical growth rates, worldwide e-commerce continues to grow steadily. According to a recent J.P. Morgan report, global e-commerce sales should reach \$963 billion by 2013, growing at a compounded annual growth rate (CAGR) of 19.4% from 2010 to 2013. According to this report, e-commerce growth will benefit from several trends including the emergent adoption of broadband, predicting the strongest growth to come from Asia with a projected 28% CAGR from 2010 to 2013. In comparison, on the same basis, U.S. and European e-commerce sales are expected to grow by 12% and 13%, respectively.

The rise of online video and social media has stimulated Internet advertising spending, which is projected to exceed \$105 billion in 2014, according to J.P. Morgan. Furthermore, according to a Forrester Research survey published during 2011, it was predicted by year-end that 37% of all online U.S. consumers would use chat for customer service, which is nearly double the 19% that used chat for customer service in 2009. Chat adoption has increased to roughly one in four seniors and has risen to nearly one-half of online consumers ages 18 to 32. At 62%, chat has the highest satisfaction rate among all online customer service channels in the Forrester survey.

We believe that the positive trends in e-commerce described above, along with the diversifying channels of consumer engagement worldwide, offer LivePerson opportunities to expand. LivePerson continues to deliver increased value to customers through its core product while also seeking to expand its product set as well as the availability and integration of its core product through different channels, such as mobile and social. By seeking to offer our solutions through different channels of engagement, we are improving the convenience and accessibility of our solutions, responding to the reality of today's online market.

We also believe that demographics shifts favor LivePerson's current and planned offerings. According to a Forrester Research survey, members of Generation Y are dedicated consumers of online content and wide adopters of social support; most use multiple technologies for online communications such as email, social networking and text messaging, and create and share user-generated content. Survey results indicated that in 2011 39% of Generation Y consumers had used a forum or community for social support. Forrester also indicated that this demographic is demanding, with high expectations for the services they purchase via the Web which may in turn accelerate the demand for LivePerson's online, real-time customer engagement solutions.

## **Strategy**

The key elements of LivePerson's business solutions strategy include:

### ***Strengthening Our Position in Both Existing and New Markets and Growing Our Recurring Revenue***

**Base.** LivePerson plans to continue to develop its market position by increasing its customer base, and expanding within its existing installed base. We will continue to focus primarily on key target markets: financial services, retail, telecommunications, technology and travel/hospitality within both our enterprise and midmarket sectors, as well as the small business (SMB) sector. Healthcare, insurance and energy utilities are new target industries and natural extensions of our primary target markets. As the online community is increasingly exposed to the benefits and functionality of our solutions, we intend to capitalize on our growing base of existing customers by collaborating with

them to optimize our added value and effectiveness. Continuing to grow our customer base will enable us to strengthen our recurring revenue stream.

***Leveraging Our Platform Across Multiple Applications and Partners.*** In developing our chat product over the last 15 years, we have created highly reliable and secure data gathering and analytic capabilities that are coupled with a sophisticated rules-based segmentation engine. In 2011, we packaged these technologies together into LiveEngage, a real-time data and intelligence platform powering our full suite of applications, adding voice and content engagement solutions to our market-leading chat product. By leveraging these existing assets we provide our customers with the same capabilities across all engagement channels. In

TABLE OF CONTENTS

addition, we have opened up access to our platform and our products with application programming interfaces (APIs) that allow third parties to develop on top of our platform. Customers, eco-system partners, and value added resellers can utilize these APIs to build our capabilities into their own applications and to enhance our applications with their services.

***Expanding the Engagement Tools and Capabilities We Provide to Our Customers.*** We have created, and will continue to create, new proprietary applications and also provide third-party tools and capabilities through our partner eco-system. Today, our customers intelligently engage with approximately two percent of their website visitors via chat. As part of our strategy, we are striving to provide our customers with the ability to intelligently engage a greater proportion of their website visitors in new ways, such as with the delivery of personalized content and the use of voice and video. In addition to developing our own applications, we continue to cultivate a partner eco-system capable of offering additional applications and services to our customers. These include partners that augment the data used in our rules engine, provide complementary services, such as translation and virtual agents, and partners that expand our reach to social and mobile channels. In 2011, we expanded our eco-system to approximately 25 partners and we continue to see growing adoption of these third-party applications by our customer base.

***Maintaining Market Leadership in Technology and Security Expertise.*** As described above, we are devoting significant resources to creating new products and enabling technologies designed to accelerate innovation and delivery of new products and technologies to our customer base. We evaluate emerging technologies and industry standards and continually update our technology in order to retain our leadership position in each market we serve. We monitor legal and technological developments in the area of information security and confidentiality to ensure our policies and procedures meet or exceed the demands of the world's largest and most demanding corporations. We believe that these efforts will allow us to effectively anticipate changing customer and consumer requirements in our rapidly evolving industry.

***Expanding our International Presence.*** During 2011, we continued our investment in direct sales and services personnel to expand our customer base in the United Kingdom and Western Europe, including expansion within several of the largest financial services and telecommunications companies in this region. We currently plan to continue to invest in our operations in this region in 2012. We have also invested in direct sales and service personnel in Australia and continue to evaluate partnership opportunities and sales and marketing strategies to support further expansion into the Asia-Pacific region. We currently have a partner supporting our sales, marketing and support efforts in the Asia-Pacific region, based in Melbourne, with initial focus on Australia, New Zealand, the Philippines and Singapore.

***Continuing to Build Brand Recognition.*** As a pioneer of real-time, intelligent engagement, LivePerson enjoys strong brand recognition and credibility. We strategically target decision makers and influencers within key vertical markets, leveraging customer successes to generate increased awareness and demand for online engagement tools. In addition, we continue to develop relationships with the media, industry analysts and relevant business associations to reinforce our position and leadership within the industry. Our brand name is also visible to both business users and consumers.

When a consumer engages in a text-based chat on a customer's website, our brand name is displayed on the LivePerson dialogue window. We believe that this high-visibility placement will continue to create brand awareness for our solutions.

***Increasing the Value of Our Service to Our Customers.*** We regularly add both new products and services, and new features and functionality to our existing services to further enhance value to our customers. Because we directly manage the server infrastructure, we can make new features available to our customers immediately upon release, without customer or end-user installation of software or hardware. We continue to enhance our reporting, analysis and administrative tools as part of our overall portfolio of services, as well as our ability to capture, analyze and report on

the substantial amount of online activity data we collect on behalf of our customers to further our customers online strategies. Our customers may use these capabilities to increase productivity, manage call center staffing, develop one-to-one marketing tactics and pinpoint consumer engagement opportunities. Through these and other innovations, we intend to reinforce our value proposition to customers, which we believe will result in additional revenue from new and existing customers over time.

3

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## TABLE OF CONTENTS

***Evaluating Strategic Alliances and Acquisitions When Appropriate.*** We have successfully integrated several acquisitions over the past decade. While we have in the past, and may from time to time in the future, engage in discussions regarding acquisitions or strategic alliances or to acquire other companies that can accelerate our growth or broaden our product offerings, we currently have no binding commitments with respect to any future acquisitions or strategic alliances.

## **Products and Services**

LivePerson's hosted platforms support and manage intelligent, real-time online interactions for businesses. Our business-to-business services: chat, voice/click-to-call, and personalized content delivery, are all managed from a single agent desktop. By supplying a complete, unified consumer history, our solutions enable businesses to deliver a relevant, timely, personalized, and seamless consumer experience. In addition to product offerings, LivePerson provides professional services and value-added business consulting to support complete deployment and optimization of our enterprise solutions.

***LP Chat.*** LP Chat, creates meaningful, real-time connections with consumers that result in higher conversion rates and superior experiences across the consumer lifecycle. LP Chat offers a reliable, secure and efficient way for businesses to connect with consumers wherever they are, including websites, social media, and mobile devices. Delivered through an open, integrated and scalable platform/architecture, LP Chat combines sophisticated technology with robust business intelligence to produce compelling, measurable results for e-commerce, marketing, consumer experience and contact center executives.

Leveraging online site traffic monitoring and a sophisticated rules engine, LP Chat enables customers to proactively engage online visitors. This engagement solution enables customers to maximize online revenue opportunities, improve conversion rates and reduce shopping cart abandonment by proactively engaging the right visitor, using the right channel, at the right time. Our solution identifies website visitors who demonstrate the highest propensity to convert, and engages them in real-time with relevant content and offers, helping to generate incremental sales. LP Chat also reduces costs in the contact center by identifying consumers who may be struggling with their self-help experience, and proactively connecting them to a live consumer care specialist. This comprehensive solution blends a proven value-based methodology with an active rules-based engagement engine and deep domain expertise to increase first contact resolution, improve consumer satisfaction, and reduce attrition rates (typically at a lower cost per engagement).

***Professional Services.*** The mission of our Professional Services team is to help customers optimize the performance of our products in order to drive incremental value through their online sales and/or service channel(s). This talented group utilizes their deep domain expertise and years of hands-on experience to provide customers with detailed analyses and measurements of their LivePerson deployment that drive strategies and decisions on how to optimize the chat channel and broaden intelligent engagement of their consumers. Deliverables of the team include scorecards that measure and chart performance trends, analyses and recommendations for web design and process improvement, transcript reviews to discover both voice of the consumer insight and agent improvement opportunities, custom training of call center agents and management, and ongoing management of chat programs to ensure alignment with current business practices and objectives. The team's value-added methodology and approach to guiding customers towards chat channel optimization is an important component of the LivePerson offering, and gives our customers a competitive advantage in the online world.

***LP Voice.*** LP Voice provides customers with a seamless connection between a website and the voice channel to effectively engage prospects and consumers at their most critical moments online.

***LivePerson Expert Platform.*** LivePerson continues to maintain a marketplace platform where Users can chat live with independent Experts in a variety of categories.

4

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## TABLE OF CONTENTS

***LP Marketer.*** Introduced in 2011, LP Marketer provides businesses of all sizes with a real-time data-driven targeting solution that intelligently delivers personalized digital user experiences. LP Marketer features a powerful combination of advanced visitor intelligence, robust traffic segmentation capabilities and user-friendly campaign-building tools that greatly reduce or eliminate reliance upon a company's internal IT resources. The result is a highly-relevant and compelling experience for each visitor, which can lead to increased consumer satisfaction and loyalty as well as measurable improvements in conversion rates and transaction values.

***LP Insights.*** Introduced in 2011, LP Insights provides customers with a text analytics tool that enables them to data mine for Voice of the Customer and Voice of the Agent content. LP Insights analyzes chat transcripts and other internal and external sources of text (such as Facebook, twitter, and email), making sense of consumers' words, behavior, reasons for contact, buying patterns, and sentiments. These insights deliver turn-key business intelligence driving improvement opportunities across the entire business system.

## **Customers**

Our business operations customer base includes Fortune 500 companies, dedicated Internet businesses, a broad range of online merchants, as well as numerous universities, libraries, government agencies and not-for-profit organizations.

Our solutions benefit organizations of all sizes conducting business or communicating with consumers online. We plan to continue to focus on key target markets: financial services, retail, telecommunications, technology, and travel/hospitality industries, as well as the SMB sector, within the United States and Canada, Latin America, Europe and the Asia-Pacific region.

No single customer accounted for or exceeded 10% of our total revenue in 2011.

## **Sales and Marketing**

### **Sales**

We sell our business products and services by leveraging a common methodology through both direct and indirect sales channels:

***Direct Sales.*** Our sales process focuses on how our solutions and industry expertise deliver financial and operational value that support our customers' strategic initiatives. Our sales and marketing-focused solutions are targeted at business executives whose primary responsibility is maximizing online consumer acquisition. These executives have a vested interest in improving conversion rates, increasing application completion rates and increasing average order value, as well as enhancing consumer satisfaction. The value proposition for our customer service focused solutions appeals to professionals who hold both top and bottom line responsibility for consumer service and technical support functions within their organization, as well as enhancing consumer satisfaction. Our proactive service solution enables these organizations to provide effective consumer service by deflecting costly phone calls and emails to the more cost efficient chat channel. Our personalization solution is targeted at marketing and e-commerce professionals who are tasked with providing a personalized consumer experience to drive a multitude of business outcomes onsite. LivePerson supports any organization with a company-wide strategic initiative to improve the overall online consumer experience. Our sales methodology often begins with research and discovery meetings that enable us to develop a deep understanding of the value drivers and key performance metrics of a prospective customer. We then present an analytical review detailing how our solutions and industry expertise can affect these value drivers and metrics. Once we validate solution capabilities and prove financial return on investment (ROI), we transition to a program

management model wherein we work hand-in-hand with the customer, providing detailed analyses, measurements and recommendations that help optimize their performance and ensure ongoing program success.

*Indirect Sales.* Resources within our organization are focused on developing partnerships to generate revenues via referral partnerships and indirect sales particularly as an adjunct to our SMB sales. By maximizing market coverage via partners who provide lead referrals and complementary products and services, we believe this channel supports revenue opportunities without incurring the costs associated with traditional direct sales.



TABLE OF CONTENTS

## **Customer Support**

Our Professional Services group provides deployment support and ongoing business consulting to enterprise and midmarket customers and maintains involvement throughout the engagement lifecycle. All LivePerson customers have access to 24/7 help desk services through chat, email and phone.

## **Marketing**

Our marketing efforts in support of our business operations are organized around the needs, trends and characteristics of our existing and prospective customer base. Our deep relationship with existing customers fosters continuous feedback, thereby allowing us to develop and refine marketing programs for specific industry segments. We market our products and services to executives responsible for the online channel and consumer service operations of their organization. Our focus is on the financial services, retail, telecommunications, technology, and travel/hospitality industries, as well as SMBs. Our integrated marketing strategy includes personalized lead generation campaigns to reach potential and existing customers using mediums such as paid and organic search, direct email and mail, industry- and category-specific tradeshows and events, and telemarketing.

Our marketing efforts in support of our consumer operations are focused on generating increased traffic to the LivePerson website primarily through paid and organic search, affiliate programs, display advertising and direct email. We are continually developing relationships with online publishers whose audiences have an affinity towards the services offered by Experts. By providing the Experts with tools to self-promote their live advice services on LivePerson through blogs and social media, we also receive qualified traffic through these channels. We also work to maximize the rate of conversion of this traffic into either paying Users or active Experts.

Our marketing strategy also encompasses public relations. As a result of relationships developed with the media and industry analyst community, we gain positive media and editorial coverage. Other initiatives include securing public speaking opportunities, case studies and bylined articles featuring key executives and customers, which helps raise LivePerson's profile and reinforces our position as an industry leader. We also proactively facilitate formal and informal interaction among our most accomplished customers, enabling us to expand our role as one of their key strategic partners.

## **Competition**

The markets for online engagement technology and online consumer services are intensely competitive and characterized by aggressive marketing, evolving industry standards, rapid technology developments, and frequent new product introductions. LivePerson's business solutions compete directly with companies that facilitate real-time sales, email management, searchable knowledgebase applications and consumer service interaction. These markets remain fairly saturated with small companies that compete on price and features. LivePerson faces competition from online interaction solution providers, including SaaS providers such as RightNow Technologies (recently acquired by Oracle Corporation), Talisma, eGain and TouchCommerce. We believe that our long-standing relationships with customers, particularly at the enterprise level, and our online selling expertise, including knowledge of online consumer purchasing habits, sophisticated methodologies to efficiently engage online consumers and reporting capabilities that measure return on investment differentiate us from existing competitors. We believe that as the scope, size and sophistication of our customers' requirements increases, our competitors' relative strengths as compared to our offerings declines. We also face potential competition from Web analytics and online engagement service providers, and other enterprise software and SaaS solutions companies such as Adobe, Oracle, Google and SAP. In addition, established technology and/or consumer-oriented companies such as Google, Microsoft, Salesforce.com and Yahoo!

may leverage their existing relationships and capabilities to offer online engagement solutions that facilitate real-time assistance. The most significant challenges facing any new market entrant include the ability to design and build scalable software that can support the world's most highly-trafficked websites, and, with respect to outsourced solution providers, the ability to design, build and manage a highly secure and scalable network infrastructure.

LivePerson's consumer operations compete with companies that provide cross category advice such as About.com and Yahoo Answers. The consumer operations also compete with niche players offering advice in specific vertical categories.

6

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## TABLE OF CONTENTS

Finally, LivePerson competes with in-house online engagement solutions, as well as, to a lesser extent, traditional offline consumer service solutions, such as telephone call centers.

LivePerson believes that competition will increase as our current competitors increase the sophistication of their offerings and as new participants enter the market. Compared to LivePerson, some of our larger current and potential competitors may have:

stronger brand recognition;  
a wider range of products and services; and  
greater financial, marketing and research and development resources.

Additionally, some competitors may enter into strategic or commercial relationships with larger, more established and better-financed companies, enabling them to:

undertake more extensive marketing campaigns;  
adopt more aggressive pricing policies; and

make more attractive offers to potential business customers to induce them to use their products or services.

Any change in the general market acceptance of the real-time customer engagement, sales, marketing or customer service solutions business model or in online, real-time consumer advice services may harm our competitive position. Our competitors may at any time improve their services or product offerings, or develop real-time sales, marketing, customer service and Web analytics applications or competitive consumer service offerings and solicit prospective customers within our target markets. Increased competition could result in pricing pressure, reduced operating margins and loss of market share.

## Technology

Three key technological features distinguish the LivePerson services:

We support our customers through a secure, scalable server infrastructure. In North America, our primary servers are hosted in a fully-secured, top-tier, third-party server center located in the Mid-Atlantic United States, and are supported by a top-tier backup server facility located in the Western United States. In Europe, our primary servers are hosted in a fully-secured, top-tier, third-party server center located in the United Kingdom and are supported by a top-tier backup server facility located in The Netherlands. Nearly all of our larger customers outside of the United States are hosted within our UK-based hosting facility. By managing our servers directly, we maintain greater flexibility and control over the production environment allowing us to be responsive to customer needs and to continue to provide a superior level of service. Utilizing advanced network infrastructure and protocols, our network, hardware and software are designed to accommodate our customers' demand for secure, high-quality 24/7 service, including during peak times such as the holiday shopping season.

As a hosted service, we are able to add additional capacity and new features quickly and efficiently. This has enabled us to provide these benefits simultaneously to our entire customer base. In addition, it allows us to maintain a relatively short development and implementation cycle.

As a SaaS provider, we focus on the development of tightly integrated software design and network architecture. We dedicate significant resources to designing our software and network architecture based on the fundamental principles of security, reliability and scalability.

**Software Design.** Our software design is based on client-server architecture. As a SaaS provider, our customers install only the LivePerson Agent Console (Windows or Java-based) on their operators' workstations. Visitors to our customers' websites require only a standard Web browser and do not need to download software from LivePerson in order to interact with our customers' operators or to use the LivePerson services.



## TABLE OF CONTENTS

Our software design is also based on open standards. These standard protocols facilitate integration with our customers' legacy and third-party systems. Representative examples include:

Java

XML (Extensible Mark-up Language)

HTML (Hypertext Mark-up Language)

SQL (Structured Query Language)

HTTP (Hypertext Transfer Protocol)

**Network Architecture.** The software underlying our services is integrated with scalable and reliable network architecture. Our network is scalable; we do not need to add new hardware or network capacity for each new LivePerson customer. This network architecture is hosted in collocation facilities with redundant network connections, servers and other infrastructure, enabling superior availability. Our backup server infrastructure housed at separate locations provides our primary hosting facilities with effective disaster recovery capability. We maintain the highest level of compliance with standards such as SOC2 and PCI. For increased security, through a multi-layered approach, we use advanced firewall architecture and industry-leading encryption standards and employ third-party experts to further validate our systems' security. We also enable our customers to further encrypt their sensitive data using more advanced encryption algorithms.

## **Government Regulation**

We are subject to a number of foreign and domestic laws and regulations that apply to the conduct of business on the Internet and the management of customer and consumer data such as, but not limited to, laws and regulations relating to user privacy, freedom of expression, data privacy, content and quality of products and services, taxation, advertising, information security and intellectual property rights. We post on our website our privacy policies and practices concerning the use and disclosure of user data, and we observe data security protocols and other business practices to comply with applicable laws. Interpretation of user privacy and data protection laws, and their application to the Internet in the U.S. and foreign jurisdictions is ongoing. There is a risk that these laws may be interpreted and applied differently in any given jurisdiction in a manner that is not consistent with our current practices, which could cause us to incur substantial costs and otherwise negatively impact our business.

Various U.S. and foreign jurisdictions impose laws regarding the collection of data. Some U.S. states have enacted legislation designed to protect consumers' privacy by prohibiting the distribution of spyware over the Internet. Such legislation typically focuses on restricting the proliferation of software that, when installed on an end user's computer is used to intentionally and deceptively take control of the end user's machine. We do not believe that the data monitoring methods employed by our technology constitute spyware or that our data monitoring methods are prohibited by applicable laws. If the scope of this type of legislation were changed to include Web analytics, such legislation could be deemed to apply to the technology we use and could potentially restrict our ability to conduct our business.

Domestic and foreign governments are also considering restricting the collection and use of Internet visitor data generally. Some jurisdictions are considering whether the collection of even anonymous data may invade the privacy of Web site visitors. If laws that limit data collection practices are enacted, we and/or our customers may be required to obtain the express consent of web visitors in order for our technology to perform certain of its basic functions that are based on collection of data. Requirements that a website must first obtain consent from its Web visitors before using our technology could reduce the amount and value of the services we provide to customers, which might impede sales and/or cause some existing customers to discontinue using our services. We could also need to expend considerable effort and resources to develop new product features and/or procedures to comply with any such legal

requirements.

8

---

TABLE OF CONTENTS

Businesses using our products may collect personal information from their web users when those web users contact them with inquiries. Federal, state and foreign government bodies and agencies, however, have adopted and are considering adopting laws and regulations regarding the collection, use and disclosure of personal information obtained from consumers. When required, we use a variety of data security procedures and practices such as encryption and masking algorithms to comply with applicable regulations, and encourage our customers to do the same. Changes to applicable laws and or interpretation thereof could significantly increase the economic burden to us of such compliance, and could negatively impact our business. The European Union and many countries within the European Union have adopted privacy directives or have imposed restrictions on the collection and use of data that are far more stringent, and impose more substantial burdens on subject businesses than current privacy standards in the United States. The U.S. federal Trade Commission has also taken action against website operators who do not comply with their stated privacy policies. All of these domestic and international legislative and regulatory initiatives have the potential to adversely affect our customers' ability to use our products.

A range of other proposed or existing laws and new interpretations of existing laws could have an impact on our business. For example:

proposed regulations regarding cybersecurity and monitoring of online behavioral data such as the proposed Do Not Track regulations could potentially apply to some of our current or planned products and services. The FTC has also increased its enforcement actions against companies that fail to meet their privacy or data security commitments to consumers. While there are currently many proposals by lawmakers and industry in this area that address the collection, maintenance and use of personal information, Web browsing and geolocation data, and establish data security and breach notification procedures, and several of those proposals, if adopted, would not be expected to materially impact our business, this is an evolving and unsettled area of regulation and any new significant restrictions or technological requirements imposed could have a negative impact on our business;

the Digital Millennium Copyright Act has provisions that limit, but do not necessarily eliminate, our liability for third-party content delivered through our website and products. In the U.S., laws relating to the liability of providers of online services for activities of their users and other third parties are currently being tested and could change. Certain foreign jurisdictions are also testing the liability of providers of online services for activities of their users and other third parties. While providers of online services currently are generally not held liable for activities of their third party users, changes in applicable laws imposing liability on providers of online services for activities of their users and other third parties could harm our business;

the Child Online Protection Act and the Children's Online Privacy Protection Act restrict the distribution of materials considered harmful to children and impose additional restrictions on the ability of online services to collect information from children under 13. Today, our policies limit use of our consumer-facing site to adults over 18 years of age; and

the federal Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, or CAN-SPAM Act, regulates the transmission and content of commercial emails and, among other things, obligates the sender of such emails to provide recipients with the ability to opt-out of receiving future emails from the sender, and establishes penalties for the transmission of email messages which are intended to deceive the recipient as to source or content. Many state legislatures also have adopted laws that impact the delivery of commercial email, and laws that regulate commercial email practices have been enacted in some of the international jurisdictions in which we do business. In addition, Internet service providers and licensors of software products have introduced a variety of systems and products to filter out certain types of commercial email, without any common protocol to determine whether the recipient desired to receive the email being blocked. As a result, it is difficult for us to determine in advance whether or not emails generated by our customers using our solutions will be permitted by spam filters to reach the intended recipients.





## TABLE OF CONTENTS

In addition, because our services are accessible worldwide, certain foreign jurisdictions may claim, that we are required to comply with their laws, even if we don't have a local entity, employees or infrastructure. The Company monitors pending legislation and regulatory initiatives to ascertain relevance, analyze impact and develop strategic direction surrounding regulatory trends and developments.

## **Intellectual Property and Proprietary Rights**

We rely on a combination of patent, copyright, trade secret, trademark and other common law in the United States and other jurisdictions, as well as confidentiality procedures and contractual provisions, to protect our proprietary technology, processes and other intellectual property. However, we believe that factors such as the technological and creative skills of our personnel, new service developments, frequent enhancements and reliable maintenance are more essential to establishing and maintaining a competitive advantage. Others may develop technologies that are similar or superior to our technology. We enter into confidentiality and other written agreements with our employees, consultants, customers, potential customers and strategic partners, and through these and other written agreements, we attempt to control access to and distribution of our software, documentation and other proprietary information. Despite our efforts to protect our proprietary rights, third parties may, in an unauthorized manner, attempt to use, copy or otherwise obtain and market or distribute our intellectual property rights or technology or otherwise develop a service with the same functionality as our services. Policing unauthorized use of our services and intellectual property rights is difficult, and we cannot be certain that the steps we have taken will prevent misappropriation of our technology or intellectual property rights, particularly in foreign countries where we do business, where our services are sold or used, where the laws may not protect proprietary rights as fully as do the laws of the United States or where enforcement of laws protecting proprietary rights is not common or effective.

Substantial litigation regarding intellectual property rights exists in the software industry. In the ordinary course of our business, our services have been and may be increasingly subject to third-party infringement claims as claims by non-practicing entities become more prevalent and as the number of competitors in our industry segment grows and the functionality of services in different industry segments overlaps. Some of our competitors in the market for real-time sales, marketing and customer service solutions or other third parties may have filed or may intend to file patent applications covering aspects of their technology. Any claims alleging infringement of third-party intellectual property rights could require us to spend significant amounts in litigation (even if the claim is invalid), distract management from other tasks of operating our business, pay substantial damage awards, prevent us from selling our products, delay delivery of the LivePerson services, develop non-infringing software, technology, business processes, systems or other intellectual property (none of which might be successful), or limit our ability to use the intellectual property that is the subject of any of these claims, unless we enter into license agreements with the third parties (which may be costly, unavailable on commercially reasonable terms, or not available at all). Therefore, such claims could have a material adverse effect on our business, results of operations and financial condition.

## **Employees**

As of March 1, 2012, we had 524 full-time employees. Our employees are not covered by collective bargaining agreements. We believe our relations with our employees are satisfactory.

## **Website Access to Reports**

We make available, free of charge, on our website ([www.liveperson.com](http://www.liveperson.com)), our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our current reports on Form 8-K and amendments to those reports filed or

furnished pursuant to Sections 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we have electronically filed such material with, or furnished it to, the Securities and Exchange Commission. *The Company's web site address provided above is not intended to function as a hyperlink, and the information on the Company's web site is not and should not be considered part of this Annual Report on Form 10-K and is not incorporated by reference herein.*

TABLE OF CONTENTS

## Item 1A. Risk Factors

The following are certain of the important risk factors that could cause, or contribute to causing, our actual operating results to differ materially from those indicated, expected or suggested by forward-looking statements made in this Annual Report on Form 10-K or presented elsewhere by management from time to time. The risks described below are not the only ones we face. Additional risks not presently known to us, or that we currently deem immaterial, may become important factors that impair our business operations. Prospective and existing investors are strongly urged to carefully consider the various cautionary statements and risks set forth in this report and other public filings before deciding to purchase, hold or sell our common stock.

### Risks Related to Our Business

#### **Our quarterly revenue and operating results may be subject to significant fluctuations, which may adversely affect the trading price of our common stock.**

Although we achieved profitability in 2011, we may in the future incur losses and experience negative cash flow, either or both of which may be significant and may cause our quarterly revenue and operating results to fluctuate significantly. These fluctuations may be as a result of a variety of factors, including the following factors which are in part within our control, and in part outside of our control:

continued adoption by companies doing business online of real-time sales, marketing and customer service solutions;  
continued adoption by individual Experts and consumers of online real-time advice services;  
changes in our pricing models, policies or the pricing policies of our current and future competitors;  
our customers' business success;  
our customers' demand for our services;  
consumer demand for our services;  
our ability to attract and retain customers;  
the amount and timing of capital expenditures and other costs relating to the expansion of our operations, including those related to acquisitions; and  
the introduction of new services by us or our competitors.

Our revenue and results may also fluctuate significantly in the future due to the following factors that are entirely outside of our control:

economic conditions specific to the Internet, electronic commerce and online media; and  
general economic and political conditions.

Period-to-period comparisons of our operating results may not be meaningful because of these factors. You should not rely upon these comparisons as indicators of our future performance.

Due to the foregoing factors, it is possible that our results of operations in one or more future quarters may fall below the expectations of securities analysts and investors. If this occurs, the trading price of our common stock could decline.

**The ongoing global economic downturn may adversely affect our business and results of operations.**

The U.S. and other global economies have continued to experience an economic downturn that has affected all sectors of the economy, particularly in the financial services and retail industries, resulting in declines in economic growth and consumer confidence, increases in unemployment rates and uncertainty about economic stability. Global credit and financial markets have also experienced extreme disruptions, including diminished liquidity and credit availability and rapid fluctuations in market valuations. Our business has been affected by these conditions, and there is no certainty that economic conditions will not deteriorate further.

11

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TABLE OF CONTENTS

These uncertainties affect businesses such as ours in a number of ways, making it difficult to accurately forecast and plan our future business activities.

Weak economic conditions may also cause our customers to experience difficulty in supporting their current operations and implementing their business plans. Our customers may reduce their spending on our services, may not be able to discharge their payment and other obligations to us, may experience difficulty raising capital, or may elect to scale back the resources they devote to customer service and/or sales and marketing technology, including services such as ours. The economic condition may also lead consumers and businesses to continue to postpone spending, which may cause our customers to decrease or delay their purchases of our products and services. If the current economic conditions continue or further deteriorate for us or our customers, we could be required to record charges relating to restructuring costs or the impairment of assets, may not be able to collect receivables on a timely basis, and our business, financial condition and results of operations could be materially adversely affected.

**If we are not competitive in the markets for online sales, marketing and customer service solutions, or online consumer services, our business could be harmed.**

The markets for online engagement technology and online consumer services are intensely competitive and characterized by aggressive marketing, evolving industry standards, rapid technology developments and frequent new product introductions. Established or new entities may enter the market in the near future, including those that provide solutions for real-time interaction online, or online consumer services related to real-time advice.

We compete directly with companies focused on technology that facilitates real-time sales, email management, searchable knowledgebase applications and customer service interaction. These markets remain fairly saturated with small companies that compete on price and features. We face significant competition from online interaction solution providers, including SaaS providers such as RightNow Technologies (recently acquired by Oracle Corporation), Talisma, eGain and TouchCommerce. We also face potential competition from Web analytics and online engagement service providers, and other enterprise software and SaaS solutions companies such as Adobe, Oracle, Google and SAP. In addition, established technology and/or consumer-oriented companies such as Google, Microsoft, Salesforce.com and Yahoo! may leverage their existing relationships and capabilities to offer online engagement solutions that facilitate real-time assistance. Furthermore, many of our competitors offer a broader range of customer relationship management products and services than we currently offer. We may be disadvantaged and our business may be harmed if companies doing business online choose real-time sales, marketing and customer service solutions from such providers.

Finally, we compete with customers and potential customers that choose to provide a real-time sales, marketing and customer service solution in-house as well as, to a lesser extent, traditional offline customer service solutions, such as telephone call centers.

We believe that competition will increase as our current competitors increase the sophistication of their offerings and as new participants enter the market. As compared to our company, some of our larger current and potential competitors have:

greater brand recognition;  
more diversified lines of products and services; and  
significantly greater financial, marketing and research and development resources.

Additionally, some competitors may enter into strategic or commercial relationships with larger, more established and better-financed companies. These competitors may be able to:

undertake more extensive marketing campaigns;  
adopt more aggressive pricing policies; and  
make more attractive offers to businesses or individuals to induce them to use their products or services.

12

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TABLE OF CONTENTS

Any change in the general market acceptance of the real-time sales, marketing and customer service solution business model or in online, real-time consumer advice services may harm our competitive position. Such changes may allow our competitors additional time to improve their service or product offerings, and would also provide time for new competitors to develop real-time sales, marketing, customer service and Web analytics applications or competitive consumer service offerings and solicit prospective customers within our target markets. Increased competition could result in pricing pressures, reduced operating margins and loss of market share.

**The success of our business is dependent on the retention of existing customers and their purchase of additional services, as well as attracting new customers and consumer users to our consumer services.**

Our business services agreements typically have twelve month terms. In some cases, our agreements are terminable or may terminate upon 30 to 90 days notice without penalty. If a significant number of our customers, or any one client to whom we provide a significant amount of services, were to terminate services, or reduce the amount of services purchased or fail to purchase additional services, our results of operations may be negatively and materially affected. Dissatisfaction with the nature or quality of our services could also lead customers to terminate our service. We depend on monthly fees and interaction-based fees from our services for substantially all of our revenue. If our retention rate declines, our revenue could decline unless we are able to obtain additional customers or alternate revenue sources. Because of the historically small amount of services sold in initial orders, we depend on the growth of our customer base and sales to new customers and sales of additional services to our existing customers.

**New and developing regulatory or other legal requirements could materially impact our business.**

We, and our customers, are subject to a number of foreign and domestic laws and regulations that apply to the conduct of business on the Internet such as, but not limited to, laws and regulations relating to user privacy, data privacy, content, advertising, information security and intellectual property rights. We post on our web site our privacy policies and practices concerning the use and disclosure of user data, and we observe data security protocols and other business practices to comply with applicable laws. Interpretation of user privacy and data protection laws, and their application to the Internet in the U.S. and foreign jurisdictions is ongoing. There is a risk that these laws may be interpreted and applied differently in any given jurisdiction in a manner that is not consistent with our current practices, which could cause us to incur substantial costs and otherwise negatively impact our business.

Various U.S. and foreign jurisdictions impose laws regarding the collection of data. Some U.S. states have enacted legislation designed to protect consumers' privacy by prohibiting the distribution of spyware over the Internet. Such legislation typically focuses on restricting the proliferation of software that, when installed on an end user's computer is used to intentionally and deceptively take control of the end user's machine. We do not believe that the data monitoring methods employed by our technology constitute spyware or that our data monitoring methods are prohibited by applicable laws. If the scope of this type of legislation were changed to include Web analytics, such legislation could be deemed to apply to the technology we use and could potentially restrict our ability to conduct our business.

Domestic and foreign governments are also considering restricting the collection and use of Internet visitor data generally. Some jurisdictions are considering whether the collection of even anonymous data may invade the privacy of Web site visitors. If laws that limit data collection practices are enacted, we and/or our customers may be required to obtain the express consent of web visitors in order for our technology to perform certain of its basic functions that

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TABLE OF CONTENTS

Businesses using our products may collect personal information from their web users when those web users contact them with inquiries. Federal, state and foreign government bodies and agencies, however, have adopted and are considering adopting laws and regulations regarding the collection, use and disclosure of personal information obtained from consumers. When required, we use a variety of data security procedures and practices such as encryption and masking algorithms to comply with applicable regulations, and encourage our customers to do the same. Changes to applicable laws and or interpretation thereof could significantly increase the economic burden to us of such compliance, and could negatively impact our business. European Union members have imposed restrictions on the collection and use of data that are far more stringent, and impose more substantial burdens on subject businesses than current privacy standards in the United States. All of these domestic and international legislative and regulatory initiatives have the potential to adversely affect our customers' ability to use our products.

Proposed regulations regarding cybersecurity and monitoring of online behavioral data such as the proposed Do Not Track regulations could potentially apply to some of our current or planned products and services. The FTC has also ratcheted up its enforcement actions against companies that fail to live up to their privacy or data security commitments to consumers. While there are currently many proposals by lawmakers and industry in this area that address the collection, maintenance and use of personal information, Web browsing and geolocation data, and establish data security and breach notification procedures, and several of those proposals, if adopted, would not be expected to materially impact our business, this is an evolving and unsettled area of regulation and any new significant restrictions or technological requirements imposed could have a negative impact on our business.

The Digital Millennium Copyright Act has provisions that limit, but do not necessarily eliminate, our liability for third-party content delivered through our website and products. In the U.S., laws relating to the liability of providers of online services for activities of their users and other third parties are currently being tested and could change. Certain foreign jurisdictions are also testing the liability of providers of online services for activities of their users and other third parties. While providers of online services currently are generally not held liable for activities of their third party users, changes in applicable laws imposing liability on providers of online services for activities of their users and other third parties could harm our business.

The Child Online Protection Act and the Children's Online Privacy Protection Act restrict the distribution of materials considered harmful to children and impose additional restrictions on the ability of online services to collect information from children under 13. Today, our policies limit use of our consumer-facing site to adults over 18 years of age.

In January 2004, the federal Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, or CAN-SPAM Act, became effective. The CAN-SPAM Act regulates the transmission and content of commercial emails and, among other things, obligates the sender of such emails to provide recipients with the ability to opt-out of receiving future emails from the sender, and establishes penalties for the transmission of email messages which are intended to deceive the recipient as to source or content. Many state legislatures also have adopted laws that impact the delivery of commercial email, and laws that regulate commercial email practices have been enacted in some of the international jurisdictions in which we do business. In addition, Internet service providers and licensors of software products have introduced a variety of systems and products to filter out certain types of commercial email, without any common protocol to determine whether the recipient desired to receive the email being blocked. As a result, it is difficult for us to determine in advance whether or not emails generated by our customers using our solutions will be permitted by spam filters to reach the intended recipients.

**If our goodwill becomes impaired, we may be required to record a charge to earnings.**

Under accounting principles generally accepted in the U.S., we review our goodwill for impairment at least annually and when events or changes in circumstances indicate the carrying value may not be recoverable. Factors that may be considered a change in circumstances indicating that the carrying value of our goodwill may not be recoverable include a decline in stock price and market capitalization, reduced future cash flow estimates, and slower growth rates in our industry. In December 2008, we recorded a \$23.5 million impairment charge in connection with the Kasamba Inc. acquisition. From time to time, we may be required to record additional charges to earnings in our financial statements during the period in which any impairment of our goodwill is determined, which may negatively impacting our results of operations.

TABLE OF CONTENTS

**We are exposed to currency rate fluctuations and our results of operations may be affected as a result.**

Although the functional currency of our Israeli subsidiaries is the U.S. dollar, as a result of the expanding scope of our Israeli operations, our currency rate fluctuation risk associated with the exchange rate movement of the U.S. dollar against the New Israeli Shekel has increased. In addition, the functional currency of our operations in the U.K. is the U.K. pound. Conducting business in currencies other than the U.S. dollar subjects us to fluctuations in currency exchange rates that could adversely affect our results of operations. Fluctuations in the value of the U.S. dollar relative to other foreign currencies affect our revenue, cost of revenue and operating expenses, and result in foreign currency transaction gains and losses. Currently, we are not a party to any hedging transactions intended to reduce our exposure to exchange rate fluctuations for our international operations. We may seek to enter into hedging transaction in the future, but we may be unable to enter into those transactions successfully, on acceptable terms or at all. We cannot predict whether or not we will incur foreign exchange losses in the future. To the extent the international component of our revenues grows, our results of operations will become more sensitive to foreign exchange rate fluctuations.

**We could face additional regulatory requirements, tax liabilities, currency exchange rate fluctuations and other risks as we expand internationally and/or as we expand into direct-to-consumer services.**

In October 2007, we acquired Kasamba Inc., an Israeli-based provider of a platform for online, real-time expert advice. In October 2000, we acquired HumanClick, an Israeli-based provider of real-time online customer service applications. In addition, we have established a sales, marketing and client support presence in the United Kingdom in support of expansion efforts into Western Europe, and have integrated the United Kingdom operations of Proficient Systems into that office. There are risks related to doing business in international markets as well as in the online consumer market, such as changes in regulatory requirements, tariffs and other trade barriers, fluctuations in currency exchange rates, more stringent rules relating to the privacy of Internet users and adverse tax consequences. In addition, there are likely to be different consumer preferences and requirements in specific international markets. Furthermore, we may face difficulties in staffing and managing any foreign operations. One or more of these factors could harm any future international operations.

**We may be unable to respond to the rapid technological change and changing client preferences in the online sales, marketing, customer service, and/or online consumer services industries and this may harm our business.**

If we are unable, for technological, legal, financial or other reasons, to adapt in a timely manner to changing market conditions in the online sales, marketing, customer service and/or e-commerce industry or our customers' or Internet users' requirements or preferences, our business, results of operations and financial condition would be materially and adversely affected. Business on the Internet is characterized by rapid technological change. In addition, the market for online sales, marketing, customer service and expert advice solutions is relatively new. Sudden changes in client and Internet user requirements and preferences, frequent new product and service introductions embodying new technologies, such as broadband communications, and the emergence of new industry standards and practices such as but not limited to security standards could render the LivePerson services and our proprietary technology and systems obsolete. The rapid evolution of these products and services will require that we continually improve the performance, features and reliability of our services. Our success will depend, in part, on our ability to:

enhance the features and performance of our services;

We are exposed to currency rate fluctuations and our results of operations may be affected as a result. 35

develop and offer new services that are valuable to companies doing business online as well as Internet users; and respond to technological advances and emerging industry standards and practices in a cost-effective and timely manner.

If any of our new services, including upgrades to our current services, do not meet our customers' or Internet users' expectations, our business may be harmed. Updating our technology may require significant additional capital expenditures and could materially and adversely affect our business, results of operations and financial condition.

TABLE OF CONTENTS

If new services require us to grow rapidly, this could place a significant strain on our managerial, operational, technical and financial resources. In order to manage our growth, we could be required to implement new or upgraded operating and financial systems, procedures and controls. Our failure to expand our operations in an efficient manner could cause our expenses to grow, our revenue to decline or grow more slowly than expected and could otherwise have a material adverse effect on our business, results of operations and financial condition.

**Our business is significantly dependent on our ability to retain our current key personnel, to attract new personnel, and to manage staff attrition.**

Our future success depends to a significant extent on the continued services of our senior management team. The loss of the services of any member of our senior management team could have a material and adverse effect on our business, results of operations and financial condition. We cannot assure you that we would be able to successfully recruit and integrate newly-hired senior managers who would work together successfully with our existing management team.

We may be unable to attract, integrate or retain other highly qualified employees in the future. If our retention efforts are ineffective, employee turnover could increase and our ability to provide services to our customers would be materially and adversely affected. Furthermore, the requirement to expense stock options may discourage us from granting the size or type of stock option awards that job candidates may require to join our company.

Any staff attrition we experience, whether initiated by the departing employees or by us, could place a significant strain on our managerial, operational, financial and other resources. To the extent that we do not initiate or seek any staff attrition that occurs, there can be no assurance that we will be able to identify and hire adequate replacement staff promptly, if at all, and even that if such staff is replaced, we will be successful in integrating these employees. In addition, we may not be able to outsource certain functions. We expect to evaluate our needs and the performance of our staff on a periodic basis, and may choose to make adjustments in the future. If the size of our staff is significantly reduced, either by our choice or otherwise, it may become more difficult for us to manage existing, or establish new, relationships with customers and other counter-parties, or to expand and improve our service offerings. It may also become more difficult for us to implement changes to our business plan or to respond promptly to opportunities in the marketplace. Further, it may become more difficult for us to devote personnel resources necessary to maintain or improve existing systems, including our financial and managerial controls, billing systems, reporting systems and procedures. Thus, any significant amount of staff attrition could cause our business and financial results to suffer.

**We may be unsuccessful in expanding our operations internationally, which could adversely affect our results of operations.**

During the past decade, we have completed acquisitions outside the United States. We have also continued to invest in expansion of operations in the United Kingdom, Europe, Israel and the Asia-Pacific region. Our ability to continue our international expansion involves various risks, including the possibility that returns on such investments will not be achieved in the near future, or ever, and the difficulty of competing in markets with which we are unfamiliar.

Our international operations may also fail due to other risks inherent in foreign operations, including:

varied, unfamiliar and unclear legal and regulatory restrictions, including different legal and regulatory standards applicable to Internet services, communications, privacy, and data protection;  
difficulties in staffing and managing foreign operations;  
differing intellectual property laws that may not provide sufficient protection for our intellectual property;

Our business is significantly dependent on our ability to retain our current key personnel, to attract new personnel, and to manage staff attrition.

adverse tax consequences;  
difficulty in addressing country-specific business requirements and regulations;  
fluctuations in currency exchange rates;

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TABLE OF CONTENTS

strains on financial and other systems to properly administer VAT and other taxes; and legal, political or systemic restrictions on the ability of U.S. companies to do business in foreign countries. Our current and any future international expansion plans will require management attention and resources and may be unsuccessful. We may find it impossible or prohibitively expensive to continue expand internationally or we may be unsuccessful in our attempt to do so, and our results of operations could be adversely impacted.

**If we do not successfully integrate past or potential future acquisitions, our business could adversely impacted.**

We have made several acquisitions during the past decade. In April 2010, we acquired NuConomy Ltd., an Israeli-based development-stage company. In October 2007, we acquired Kasamba Inc., an Israeli-based provider of a platform for online, real-time expert advice. In July 2006, we acquired Proficient Systems, Inc., a U.S. provider of hosted proactive chat solutions that help companies generate revenue on their websites. In the future, we may acquire or invest in complementary companies, products or technologies. Acquisitions and investments involve numerous risks to us, including:

- difficulties in integrating operations, technologies, products and personnel with LivePerson;
- diversion of financial and management resources from efforts related to the LivePerson services or other pre-existing operations;
- risks of entering new markets beyond providing real-time sales, marketing and customer service solutions for companies doing business online;
- potential loss of either our existing key employees or key employees of any companies we acquire; and
- our inability to generate sufficient revenue following an acquisition to offset acquisition or investment costs.

These difficulties could disrupt our ongoing business, expose us to unexpected costs, distract our management and employees, increase our expenses and adversely affect our results of operations. Furthermore, we may incur debt or issue equity securities to pay for any future acquisitions. The issuance of equity securities could be dilutive to our existing stockholders.

**We are dependent on technology systems and third-party content that are beyond our control.**

The success of our services depends in part on our customers' online services as well as the Internet connections of visitors to websites, both of which are outside of our control. As a result, it may be difficult to identify the source of problems if they occur. In the past, we have experienced problems related to connectivity which has resulted in slower than normal response times to Internet user chat requests and messages and interruptions in service. Our services rely both on the Internet and on our connectivity vendors for data transmission. Therefore, even when connectivity problems are not caused by our services, our customers or Internet users may attribute the problem to us. This could diminish our brand and harm our business, divert the attention of our technical personnel from our product development efforts or cause significant client relations problems.

In addition, we rely in part on third-party service providers and other third parties for Internet connectivity and network infrastructure hosting, security and maintenance. These providers may experience problems that result in slower than normal response times and/or interruptions in service. If we are unable to continue utilizing the third-party services that support our Web hosting and infrastructure or if our services experience interruptions or delays due to third party providers, our reputation and business could be harmed.





TABLE OF CONTENTS

We also rely on the security of our third party providers to protect our proprietary information and information of our customers. Information technology system failures, including a breach of our or our third party providers' data security, could disrupt our ability to function in the normal course of business by potentially causing, among other things, an unintentional disclosure of customer information. Additionally, despite our security procedures or those of our third party providers, information systems may be vulnerable to threats such as computer hacking, cyber-terrorism or other unauthorized attempts by third parties to access, modify or delete our or our customers' personal information. Any such breach could have a material adverse effect on our operating results and our reputation as a provider of business collaboration and communications solutions.

We also depend on third parties for hardware and software and our consumer services depend on third parties for content. Such products and content could contain defects or inaccurate information. Problems arising from our use of such hardware or software or third party content could require us to incur significant costs or divert the attention of our technical or other personnel from our product development efforts or to manage issues related to content. To the extent any such problems require us to replace such hardware or software we may not be able to do so on acceptable terms, if at all.

**Failures or breaches in our services, those of our third party providers, or in the websites of our customers, including those resulting from security vulnerabilities, defects or errors, could harm our business.**

While we continue to expand our focus on this issue and are taking measures to safeguard our services from cybersecurity threats, device capabilities continue to evolve, enabling more data and processes, such as mobile computing, potentially increasing the risk that security failures will occur are increasing. Our products are inherently complex and may contain defects or errors that are detected only when the products are in use. Because our services are responsible for critical communication between our customers and consumers, security failures, defects or errors in our components, materials or software or those used by our customers could have an adverse impact on us, on our customers and on the end users of their websites. Such adverse impact could include a decrease in demand for our services, damage to our reputation and to our customer relationships, and other financial liability or harm to our business.

**Privacy concerns relating to the Internet could result in new legislation, negative public perception and/or user behavior that negatively affect our business.**

We collect data from live online Internet user dialogues and enable our customers to capture and save information about their Internet user interactions. To the extent that additional legislation regarding Internet user privacy is enacted, such as legislation governing the collection and use of information regarding Internet users through the use of cookies, the effectiveness of the LivePerson services could be impaired by restricting us from collecting information which may be valuable to our customers. The foregoing could have a material adverse effect on our business, results of operations and financial condition.

In addition, privacy concerns may cause Internet users to avoid online sites that collect such behavioral information and even the perception of security and privacy concerns, whether or not valid, may indirectly inhibit market acceptance of our services. In addition, we or our customers may be harmed by any laws or regulations that restrict the ability to collect, transmit or use this data. The European Union and many countries within the E.U. have adopted privacy directives or laws that strictly regulate the collection and use of personally identifiable information of Internet

Failures or breaches in our services, those of our third party providers, or in the websites of our customers, including

users. The United States has also adopted legislation which governs the collection and use of certain personal information, such as the Children's Online Privacy Protection Act which directs the U.S. Federal Trade Commission to regulate the collection of data from children on commercial websites. The U.S. Federal Trade Commission has also taken action against website operators who do not comply with their stated privacy policies. Furthermore, other foreign jurisdictions have adopted legislation governing the collection and use of personal information. These and other governmental efforts may limit our customers' ability to collect and use information about their interactions with their Internet users through our services. As a result, such laws and efforts could create uncertainty in the marketplace that could reduce demand for our services or increase the cost of doing business as a result of litigation costs or increased service delivery costs, or could in some other manner have a material adverse effect on our business, results of operations and financial condition.

TABLE OF CONTENTS

**We may be liable if third parties misappropriate personal information belonging to our customers Internet users.**

The dialogue transcripts of the text-based chats and email interactions between our customers and Internet users may include personal information, such as contact and demographic information. Although we employ and continually test and update our security measures to protect this information from unauthorized access, it is still possible that our security measures could be breached and such a breach could result in unauthorized access to our customers data or our data, including our intellectual property and other confidential business information. Because the techniques employed by hackers to obtain unauthorized access or to sabotage systems change frequently and are becoming more sophisticated, we may be unable to anticipate all techniques or to implement adequate preventative measures. Any security breach could result in disclosure of our trade secrets or disclosure of confidential customer, supplier or employee data. If third parties were able to penetrate our network security or otherwise misappropriate personal information relating to our customers Internet users or the text of customer service inquiries, our competitive position may be harmed and we could be subject to liability. We could be subject to negligence claims or claims for misuse of personal information. These claims could result in litigation, which could have a material adverse effect on our business, results of operations and financial condition. We may incur significant costs to protect against the threat of security breaches or to alleviate problems caused by such breaches. The need to physically secure and securely transmit confidential information online has been a significant barrier to e-commerce and online communications. Any well-publicized compromise of security could deter people from using online services such as the ones we offer or from using them to conduct transactions, which involve transmitting confidential information. Because our success depends on the general acceptance of our services and electronic commerce, we may incur significant costs to protect against the threat of security breaches or to alleviate problems caused by these breaches.

**We may be subject to legal liability and/or negative publicity for the services provided to consumers via our technology platforms.**

Our technology platforms enable representatives of our customers as well as individual service providers to communicate with consumers and other persons seeking information or advice on the Internet. The law relating to the liability of online platform providers such as us for the activities of users of their online platforms is often challenged in the U.S. and internationally. We may be unable to prevent users of our technology platforms from providing negligent, unlawful or inappropriate advice, information or content via our technology platforms, or from behaving in an unlawful manner, and we may be subject to allegations of civil or criminal liability for negligent, fraudulent, unlawful or inappropriate activities carried out by users of our technology platforms.

Claims could be made against online services companies under both U.S. and foreign law such as fraud, defamation, libel, invasion of privacy, negligence, copyright or trademark infringement, or other theories based on the nature and content of the materials disseminated by users of our technology platforms. In addition, domestic and foreign legislation has been proposed that could prohibit or impose liability for the transmission over the Internet of certain types of information. Our defense of any of these actions could be costly and involve significant time and attention of our management and other resources.

The Digital Millennium Copyright Act, or DMCA, is intended, among other things, to reduce the liability of online service providers for listing or linking to third party Web properties that include materials that infringe copyrights or rights of others. Additionally, portions of The Communications Decency Act, or CDA, are intended to provide statutory protections to online service providers who distribute third party content. A safe harbor for copyright infringement is also available under the DMCA to certain online service providers that provide specific services, if the providers take certain affirmative steps as set forth in the DMCA. Important questions regarding the safe harbor under

the DMCA and the CDA have yet to be litigated, and we cannot guarantee that we will meet the safe harbor requirements of the DMCA or of the CDA. If we are not covered by a safe harbor, for any reason, we could be exposed to claims, which could be costly and time-consuming to defend.

TABLE OF CONTENTS

Our consumer service allows consumers to provide feedback regarding service providers. Although all such feedback is generated by users and not by us, claims of defamation or other injury could be made against us for content posted on our websites. Our liability for such claims may be higher in jurisdictions outside the U.S. where laws governing Internet transactions are unsettled.

If we become liable for information provided by our users and carried via our service in any jurisdiction in which we operate, we could be directly harmed and we may be forced to implement new measures to reduce our exposure to this liability. In addition, the increased attention focused upon liability issues as a result of these lawsuits and legislative proposals could harm our reputation or otherwise impact the growth of our business. Any costs incurred as a result of this potential liability could harm our business.

In addition, negative publicity and user sentiment generated as a result of fraudulent or deceptive conduct by users of our technology platforms could damage our reputation, reduce our ability to attract new users or retain our current users, and diminish the value of our brand.

In the future, we may be required to spend substantial resources to take additional protective measures or discontinue certain service offerings, either of which could harm our business. Any costs incurred as a result of potential liability relating to the sale of unlawful services or the unlawful sale of services could harm our business.

In addition to privacy legislation, any new legislation or regulation regarding the Internet, software sales or export and/or the Software-as-a-Service industry, and/or the application of existing laws and regulations to the Internet, software sales or export, and/or the Software-as-a-Service industry could create new legal or regulatory burdens on our business that could have a material adverse effect on our business, results of operations and financial condition. Additionally, as we operate outside the U.S., the international regulatory environment relating to the Internet, software sales or export, and/or the Software-as-a-Service industry could have a material adverse effect on our business, results of operations and financial condition.

**Our products and services may infringe upon intellectual property rights of third parties and any infringement could require us to incur substantial costs and may distract our management.**

We are subject to the risk of claims alleging infringement of third-party proprietary rights against us or against our customers for use of our products. Certain of our customer contracts contain indemnification obligations requiring us to indemnify our customers from certain claims arising from the use of our services. Substantial litigation regarding intellectual property rights exists in the software industry. In the ordinary course of our business, our services and/or our customers' use of our services may be increasingly subject to third-party infringement claims as claims by non-practicing entities become more prevalent and the number of competitors in our industry segment grows and the functionality of services in different industry segments overlaps. Some of our competitors in the market for real-time sales, marketing and customer service solutions or other third parties may have filed or may intend to file patent applications covering aspects of their technology. Any claims alleging infringement of third-party intellectual property rights could require us to spend significant amounts in litigation (even if the claim is invalid), distract management from other tasks of operating our business, pay substantial damage awards, prevent us from selling our products, delay delivery of the LivePerson services, develop non-infringing software, technology, business processes, systems or other intellectual property (none of which might be successful), or limit our ability to use the intellectual property that is the subject of any of these claims, unless we enter into license agreements with the third parties (which may be costly, unavailable on commercially reasonable terms, or not available at all). Therefore, such claims could have a material adverse effect on our business, results of operations and financial condition.

Our products and services may infringe upon intellectual property rights of third parties and any infringement could

**Our business and prospects would suffer if we are unable to protect and enforce our intellectual property rights.**

Our success and ability to compete depend, in part, upon the protection of our intellectual property rights relating to the technology underlying the LivePerson services. It is possible that:

any issued patent or patents issued in the future may not be broad enough to protect our intellectual property rights;

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TABLE OF CONTENTS

any issued patent or any patents issued in the future could be successfully challenged by one or more third parties, which could result in our loss of the right to prevent others from exploiting the inventions claimed in the patents; current and future competitors may independently develop similar technologies, duplicate our services or design around any patents we may have; and

effective patent protection may not be available in every country in which we do business, where our services are sold or used, where the laws may not protect proprietary rights as fully as do the laws of the U.S. or where enforcement of laws protecting proprietary rights is not common or effective.

Further, to the extent that the invention described in any U.S. patent was made public prior to the filing of the patent application, we may not be able to obtain patent protection in certain foreign countries. We also rely upon copyright, trade secret, trademark and other common law in the U.S. and other jurisdictions, as well as confidentiality procedures and contractual provisions, to protect our proprietary technology, processes and other intellectual property. Any steps we might take may not be adequate to protect against infringement and misappropriation of our intellectual property

by third parties. Similarly, third parties may be able to independently develop similar or superior technology, processes or other intellectual property. Policing unauthorized use of our services and intellectual property rights is difficult, and we cannot be certain that the steps we have taken will prevent misappropriation of our technology or intellectual property rights, particularly in foreign countries where we do business, where our services are sold or used, where the laws may not protect proprietary rights as fully as do the laws of the United States or where enforcement of laws protecting proprietary rights is not common or effective. The unauthorized reproduction or other misappropriation of our intellectual property rights could enable third parties to benefit from our technology without paying us for it. If this occurs, our business, results of operations and financial condition could be materially and adversely affected. In addition, disputes concerning the ownership or rights to use intellectual property could be costly and time-consuming to litigate, may distract management from operating our business and may result in our loss of significant rights.

**Technological or other defects could disrupt or negatively impact our services, which could harm our business and reputation.**

We face risks related to the technological capabilities of our services. We expect the number of interactions between our customers operators and Internet users over our system to increase significantly as we expand our client base. Our network hardware and software may not be able to accommodate this additional volume. Additionally, we must continually upgrade our software to improve the features and functionality of our services in order to be competitive in our markets. If future versions of our software contain undetected errors, our business could be harmed. If third-party content is flawed, our business could be harmed. As a result of major software upgrades at LivePerson, our client sites have, from time to time, experienced slower than normal response times and interruptions in service. If we experience system failures or degraded response times, our reputation and brand could be harmed. We may also experience technical problems in the process of installing and initiating the LivePerson services on new Web hosting services. These problems, if not remedied, could harm our business.

Our services also depend on complex software which may contain defects, particularly when we introduce new versions onto our servers. We may not discover software defects that affect our new or current services or enhancements until after they are deployed. It is possible that, despite testing by us, defects may occur in the software.

These defects could result in:

- damage to our reputation;
- lost sales;
- delays in or loss of market acceptance of our products; and
- unexpected expenses and diversion of resources to remedy errors.





TABLE OF CONTENTS

**The non-payment or late payment of amounts due to us from a significant number of customers may negatively impact our financial condition or make it difficult to forecast our revenues accurately.**

During 2011, we increased our allowance for doubtful accounts by \$290,000 to approximately \$851,000, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of receivables due from customers with greater credit risk. We wrote off approximately \$163,000 of previously reserved accounts, leaving a net allowance for doubtful accounts of approximately \$688,000. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles. During 2010, we increased our allowance for doubtful accounts by \$166,000 to approximately \$561,000, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of receivables due from customers with greater credit risk. As a result of increasingly long payment cycles, we have faced increased difficulty in predicting our operating results for any given period, and have experienced significant unanticipated fluctuations in our revenues from period to period. Any failure to achieve anticipated revenues in a period could cause our stock price to decline.

**Our services are subject to payment-related risks.**

For certain payment methods, including credit and debit cards, we pay interchange and other fees, which may increase over time and raise our operating costs and lower our profit margins. We rely on third parties to provide payment processing services, including the processing of credit cards, debit cards and it could disrupt our business if these companies become unwilling or unable to provide these services to us. We are also subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, we may be subject to fines and higher transaction fees and lose our ability to accept credit and debit card payments from our customers or facilitate other types of online payments, and our business and operating results could be adversely affected.

Through our consumer-facing platform, we facilitate online transactions between individual service providers who provide online advice and information to consumers. In connection with these services, we accept payments using a variety of methods, such as credit card, debit card and PayPal. These payments are subject to chargebacks when consumers dispute payments they have made to us. Chargebacks can occur whether or not services were properly provided. Susceptibility to chargebacks puts a portion of our revenue at risk. We take measures to manage our risk relative to chargebacks and to recoup properly charged fees, however, if we are unable to successfully manage this risk our business and operating results could be adversely affected. As we offer new payment options to our users, we may be subject to additional regulations, compliance requirements, and fraud.

We are also subject to a number of other laws and regulations relating to money laundering, international money transfers, privacy and information security and electronic fund transfers. If we were found to be in violation of applicable laws or regulations, we could be subject to civil and criminal penalties or forced to cease our payments services business.

**We have a history of losses, we had an accumulated deficit of \$88.1 million as of December 31, 2011 and we may incur losses in the future.**

The non-payment or late payment of amounts due to us from a significant number of customers may negatively impact

Although we achieved profitability in 2011, we may, in the future, incur losses and experience negative cash flow, either or both of which may be significant. We recorded net losses from inception through the year ended December 31, 2003. We recorded net income for the years ended December 31, 2004 through 2007 and 2009 through 2011.

We recorded a net loss of \$23.8 million for the year ended December 31, 2008. As of December 31, 2011, our accumulated deficit was approximately \$88.1 million. We cannot assure you that we can sustain or increase profitability on a quarterly or annual basis in the future. Failure to maintain profitability may materially and adversely affect the market price of our common stock.

TABLE OF CONTENTS

**With the recent volatility in the capital markets, there is a risk that we could suffer a loss of principal in our cash and cash equivalents and short term investments and suffer a reduction in our interest income or in our return on investments.**

As of December 31, 2011, we had \$93.3 million in cash and cash equivalents. We regularly invest excess funds from our cash and cash equivalents in short-term money market funds. We currently hold no mortgaged-backed or auction rate securities. However, some of our investments are subject to general credit, liquidity, market and interest rate risks, which may be exacerbated by the ongoing uncertainty in the U.S. and global credit markets that have affected various sectors of the financial markets and caused global credit and liquidity issues. In the future, these market risks associated with our investment portfolio may harm the results of our operations, liquidity and financial condition. Although we believe we have chosen a more cautious portfolio designed to preserve our existing cash position, it may not adequately protect the value of our investments. Furthermore, this more cautious portfolio is unlikely to provide us with any significant interest income in the near term.

**We cannot assure our stockholders that our current or future stock repurchase programs will enhance/has enhanced long-term stockholder value and stock repurchases could increase the volatility of the price of our common stock and will diminish our cash reserves.**

On May 14, 2010, our Board of Directors approved a stock repurchase program through June 30, 2012. Under the program, we are authorized to repurchase shares of our common stock, in the open market or privately negotiated transactions, at times and prices considered appropriate by them depending upon prevailing market conditions and other corporate considerations, up to an aggregate purchase price of \$10.0 million. The timing and actual number of shares repurchased depend on a variety of factors including the timing of open trading windows, price, corporate and regulatory requirements, and other market conditions. The program may be suspended or discontinued at any time without prior notice. Repurchases pursuant to our stock repurchase program could affect our stock price and increase its volatility. The existence of a stock repurchase program could also cause our stock price to be higher than it would be in the absence of such a program and could potentially reduce the market liquidity for our stock. Additionally, our stock repurchase program will diminish our cash reserves, which could impact our ability to pursue possible future strategic opportunities and acquisitions and could result in lower overall returns on our cash balances. There can be no assurance that any stock repurchases will enhance stockholder value because the market price of our common stock may decline below the levels at which we repurchased shares of stock. Although our stock repurchase program is intended to enhance long-term stockholder value, short-term stock price fluctuations could reduce the program's effectiveness. As of March 1, 2012, approximately \$6.4 million remained available for purchases under the program.

**Failure to license necessary third party software for use in our products and services, or failure to successfully integrate third party software, could cause delays or reductions in our sales, or errors or failures of our service.**

We license third party software that we plan to incorporate into our products and services. In the future, we might need to license other software to enhance our products and meet evolving customer requirements. These licenses may not continue to be available on commercially reasonable terms or at all. Some of this technology could be difficult to replace once integrated. The loss of, or inability to obtain, these licenses could result in delays or reductions of our applications until we identify, license and integrate or develop equivalent software, and new licenses could require us

With the recent volatility in the capital markets, there is a risk that we could suffer a loss of principal in our cash and

to pay higher royalties. If we are unable to successfully license and integrate third party technology, we could experience a reduction in functionality and/or errors or failures of our products, which may reduce demand for our products and services.

Third-party licenses may expose us to increased risks, including risks associated with the integration of new technology, the impact of new technology integration on our existing technology, the diversion of resources from the development of our own proprietary technology, and our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs.

TABLE OF CONTENTS

**We believe our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.**

Accounting principles generally accepted in the U.S. are subject to interpretation by the FASB, the American Institute of Certified Public Accountants, the SEC, and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of a change.

**Our reputation depends, in part, on factors which are partially or entirely outside of our control.**

Our services typically appear under the LivePerson brand or as a LivePerson-branded icon on our customers' websites. The customer service operators who respond to the inquiries of our customers' Internet users are employees or agents of our customers; they are not our employees. The experts who respond to the inquiries of Internet users are independent consultants or agents of our customers; they are not our employees. As a result, we are not able to control the actions of these operators or experts. In addition, an Internet user may not know that the operator or expert is not a LivePerson employee. If an Internet user were to have a negative experience in a LivePerson-powered real-time dialogue, it is possible that this experience could be attributed to us, which could diminish our brand and harm our business. Finally, we believe the success of our business services is aided by the prominent placement of the chat icon on a customer's website, over which we also have no control.

**Our products are complex, and errors, failures or bugs may be difficult to correct.**

Our products are complex, integrating hardware, software and elements of a customer's existing infrastructure. Despite quality assurance testing conducted prior to the release of our products our software may contain bugs that are difficult to detect and fix. Any such issues could interfere with the expected operation of a solution, which might negatively impact customer satisfaction, reduce sales opportunities or affect gross margins. Depending upon the size and scope of any such issue, remediation may have a negative impact on our business. Our inability to cure an application or product defect, should one occur, could result in the failure of an application or product line, damage to our reputation, litigation and/or product reengineering expenses. Our insurance may not cover or may be insufficient to cover expenses associated with such events.

**Political, economic and military conditions in Israel could negatively impact our Israeli operations**

Our product development staff, help desk and online sales support operations are located in Israel. As of December 31, 2011, we had 290 full-time employees in Israel. Although substantially all of our sales to date have been made to customers outside Israel, we are directly influenced by the political, economic and military conditions affecting Israel. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors. A state of hostility, varying in degree and intensity, has caused security and economic problems in Israel. Since September 2000, there has been a marked increase in violence, civil unrest and hostility, including armed clashes, between the State of Israel and the Palestinians, primarily but not exclusively in the West Bank and Gaza Strip, and negotiations between the State of Israel and Palestinian representatives have effectively ceased. The election of representatives of the Hamas movement to a majority of seats in the Palestinian Legislative Council in January 2006 created additional unrest and uncertainty in the region. In July and August of 2006, Israel was involved in a

full-scale armed conflict with Hezbollah, a Lebanese Islamist Shiite militia group and political party, in southern Lebanon, which involved missile strikes against civilian targets in northern Israel that resulted in economic losses. Since June 2007, there has been an escalation in violence in the Gaza Strip. In December 2008 and January 2009,

Israel engaged in an armed conflict with Hamas, which involved civilian targets in various parts of Israel and negatively affected business conditions in Israel. Recent popular uprisings in various countries in the Middle East and northern Africa are affecting the political stability of those countries. This instability may lead to deterioration of the political and trade relationships that exist between the State of Israel and these countries, as well as potentially affecting the global economy and marketplace through changes in oil and gas prices. In addition, Iran has publicly threatened to attack Israel and is widely believed to be developing nuclear weapons. Iran is also believed to have a strong influence among extremist groups in the region, such

## TABLE OF CONTENTS

as Hamas in Gaza and Hezbollah in Lebanon. This situation may potentially escalate in the future to violent events which may negatively affect Israel. Continued hostilities between Israel and its neighbors and any future armed conflict, terrorist activity or political instability in the region could adversely affect our operations in Israel and adversely affect the market price of our ordinary shares. Further escalation of tensions or violence might require more widespread military reserve service by some of our Israeli employees and might result in a significant downturn in the economic or financial condition of Israel, either of which could have a material adverse effect on our operations in Israel and our business. In addition, several Arab countries still restrict business with Israeli companies. Our operations in Israel could be adversely affected by restrictive laws or policies directed towards Israel and Israeli businesses.

### **Capital needs necessary to execute our business strategy could increase substantially and we may not be able to secure additional financing to execute this strategy.**

We believe that our current cash and cash equivalents and cash generated from operations, if any, will be sufficient to fund our working capital and capital expenditure requirements for at least the next twelve months. To the extent that we require additional funds to support our operations or the expansion of our business, or to pay for acquisitions, we may need to sell additional equity, issue debt or convertible securities or obtain credit facilities through financial institutions. In the past, we have obtained financing principally through the sale of preferred stock, common stock and warrants. If additional funds are raised through the issuance of debt or preferred equity securities, these securities could have rights, preferences and privileges senior to holders of common stock, and could have terms that impose restrictions on our operations. If additional funds are raised through the issuance of additional equity or convertible securities, our stockholders could suffer dilution. We cannot assure you that additional funding, if required, will be available to us in amounts or on terms acceptable to us. If sufficient funds are not available or are not available on acceptable terms, our ability to fund any potential expansion, take advantage of acquisition opportunities, develop or enhance our services or products, or otherwise respond to competitive pressures would be significantly limited. Those limitations would materially and adversely affect our business, results of operations and financial condition.

## **Risks Related to Our Industry**

### **Future regulation of the Internet may slow our growth, resulting in decreased demand for our services and increased costs of doing business.**

State, federal and foreign regulators could adopt laws and regulations that impose additional burdens on companies that conduct business online. These laws and regulations could discourage communication by e-mail or other web-based communications, particularly targeted e-mail of the type facilitated by our services, which could reduce demand for our services.

The growth and development of the market for online services may prompt calls for more stringent consumer protection laws or laws that may inhibit the use of Internet-based communications or the information contained in these communications. The adoption of any additional laws or regulations may decrease the expansion of the Internet. A decline in the growth of the Internet, particularly as it relates to online communication, could decrease demand for our services and increase our costs of doing business, or otherwise harm our business. Any new legislation or regulations, application of laws and regulations from jurisdictions whose laws do not currently apply to our business, or application of existing laws and regulations to the Internet and other online services could increase our costs and harm our growth.

## **We depend on the continued viability of the infrastructure of the Internet.**

To the extent that the Internet continues to experience growth in the number of users and frequency of use by consumers resulting in increased bandwidth demands, we cannot assure you that the infrastructure for the Internet will be able to support the demands placed upon it. The Internet has experienced outages and delays as a result of damage to portions of its infrastructure. Outages or delays could adversely affect online sites, email and the level of traffic on the Internet. We also depend on Internet service providers that provide our customers and Internet users with access to the LivePerson services. In the past, users have experienced difficulties due to system failures unrelated to our service. In addition, the Internet could lose its viability due to delays in the adoption of new standards and protocols required to handle increased levels of Internet



TABLE OF CONTENTS

activity. Insufficient availability of telecommunications services to support the Internet also could result in slower response times and negatively impact use of the Internet generally, and our customers' sites (including the LivePerson dialogue windows) in particular. If the infrastructure of the Internet does not effectively support the growth of the Internet, we may not maintain profitability and our business, results of operations and financial condition will suffer.

**We are dependent on the continued growth and acceptance of the Internet as a medium for commerce, and the related expansion of the Internet infrastructure.**

We cannot be sure that a sufficiently broad base of consumers will continue to use the Internet as a medium for commerce. Convincing our customers to offer real-time sales, marketing and customer service technology may be difficult. The continuation of the Internet as a viable commercial marketplace is subject to a number of factors, including:

- continued growth in the number of users;
- concerns about transaction security or security problems such as viruses and worms or hackers;
- concerns about cybersecurity attacks or the security of confidential information online;
- continued development of the necessary technological infrastructure;
- development of enabling technologies;
- uncertain and increasing government regulation; and
- the development of complementary services and products.

**Other Risks**

**Our stock price has been highly volatile and may experience extreme price and volume fluctuations in the future, which could reduce the value of your investment and subject us to litigation.**

Fluctuations in market price and volume are particularly common among securities of Internet and other technology companies. The market price of our common stock has fluctuated significantly in the past and may continue to be highly volatile, with extreme price and volume fluctuations, in response to the following factors, some of which are beyond our control:

- variations in our quarterly operating results;
- changes in market valuations of publicly-traded companies in general and Internet and other technology companies in particular;
- our announcements of significant client contracts, acquisitions and our ability to integrate these acquisitions, strategic partnerships, joint ventures or capital commitments;
- our failure to complete significant sales;
- additions or departures of key personnel;
- future sales of our common stock;
- changes in financial estimates by securities analysts; and
- terrorist attacks against the United States, in Israel, or in the United Kingdom, the engagement in hostilities or an escalation of hostilities by or against the United States, Israel, or the United Kingdom, or the declaration of war or national emergency by the United States, Israel, or the United Kingdom.

In the past, companies that have experienced volatility in the market price of their stock have been the subject of securities class action litigation. We may in the future be the target of similar litigation, which could result in substantial costs and distract management from other important aspects of operating our business.

TABLE OF CONTENTS

**Our common stock is traded on more than one market and this may result in price variations.**

Shares of our common stock are currently traded on the Nasdaq Capital Market and the Tel Aviv Stock Exchange ( TASE ). Trading in our common stock on these markets takes place in different currencies (U.S. dollars on the Nasdaq and NIS on the TASE), and at different times (resulting from different time zones, different trading days and different public holidays in the United States and Israel). The trading prices of our common stock on these two markets may differ due to these and other factors. Any decrease in the trading price of our common stock on one of these markets could cause a decrease in the trading price of our common stock on the other market. Differences in trading prices on the two markets could negatively impact our trading price.

**Our stockholders who each own greater than five percent of the outstanding common stock and our named executive officers and directors will be able to influence matters requiring a stockholder vote.**

Our stockholders who each own greater than five percent of the outstanding common stock and their affiliates, and our named executive officers and directors, in the aggregate, and as of December 31, 2011, beneficially own approximately 41% of our outstanding common stock. As a result, these stockholders, if acting together, will be able to significantly influence all matters requiring approval by our stockholders, including the election of directors and approval of significant corporate transactions. This concentration of ownership could also have the effect of delaying or preventing a change in control.

**The future sale of shares of our common stock may negatively affect our stock price.**

If our stockholders sell substantial amounts of our common stock, including shares issuable upon the exercise of outstanding options and warrants in the public market, or if our stockholders are perceived by the market as intending to sell substantial amounts of our common stock, the market price of our common stock could fall. These sales also might make it more difficult for us to sell equity securities in the future at a time and price that we deem appropriate. No prediction can be made as to the effect, if any, that market sales of our common stock will have on the market price of our common stock.

**Anti-takeover provisions in our charter documents and Delaware law may make it difficult for a third party to acquire us.**

Provisions of our amended and restated certificate of incorporation, such as our staggered Board of Directors, the manner in which director vacancies may be filled and provisions regarding the calling of stockholder meetings, could make it more difficult for a third party to acquire us, even if doing so might be beneficial to our stockholders. In addition, provisions of our amended and restated bylaws, such as advance notice requirements for stockholder proposals, and applicable provisions of Delaware law, such as the application of business combination limitations, could impose similar difficulties. Further, provisions of our amended and restated certificate of incorporation relating to directors, stockholder meetings, limitation of director liability, indemnification and amendment of the certificate of incorporation and bylaws may not be amended without the affirmative vote of not less than 66.67% of the outstanding shares of our capital stock entitled to vote generally in the election of directors (considered for this purpose as a single class) cast at a meeting of our stockholders called for that purpose. Our amended and restated bylaws may not be

amended without the affirmative vote of at least 66.67% of our Board of Directors or without the affirmative vote of not less than 66.67% of the outstanding shares of our capital stock entitled to vote generally in the election of directors (considered for this purpose as a single class) cast at a meeting of our stockholders called for that purpose.

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

None.

## **Item 2. Properties**

We currently lease approximately 18,500 square feet at our headquarters location in New York City, under a lease expiring in April 2020. In March 2012, we modified our existing lease for additional office space of approximately 18,500 also expiring in April 2020. We also lease approximately 4,500 square feet of office space in San Francisco under a lease expiring in October 2013.

## TABLE OF CONTENTS

Two of our wholly-owned subsidiaries, LivePerson Ltd. (formerly HumanClick Ltd.) and Kasamba, Ltd., maintain offices in Raanana, Israel of approximately 54,000 square feet, under leases expiring in December 2015.

Our wholly-owned subsidiary, Proficient Systems, Inc. maintains offices in Atlanta, Georgia of approximately 9,000 square feet, under a lease expiring in November 2015.

Our wholly-owned subsidiary, LivePerson (UK) Ltd. maintains offices in Reading, United Kingdom of approximately 1,000 square feet, under a lease expiring in May 2012.

We also lease space for our primary and back-up hosting facilities at separate locations in the continental U.S and Europe.

We believe that our properties are in good condition, are well maintained and are suitable and adequate to carry on our operations for the foreseeable future.

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

On July 31, 2007, we were served with a complaint filed in the United States District Court for the Southern District of New York by the Shareholders Representative of Proficient Systems, Inc. In connection with the July 2006 acquisition of Proficient, we were contingently required to issue up to 2,050,000 shares of common stock based on the terms of an earn-out provision in the merger agreement. In accordance with the terms of the earn-out provision, we issued 1,127,985 shares of LivePerson common stock in the second quarter of 2007 to the former shareholders of Proficient. The amended complaint filed by the Shareholders Representative, or Plaintiff, on May 12, 2009 alleges that we breached the merger agreement by failing to properly account for net annualized revenue, and demands payment of damages on the grounds that substantially all of the remaining contingently issuable earn-out shares should have been paid. We believe the claims are without merit. The case proceeded to trial, which ended on November 4, 2010. Post-trial filings were made on November 19, 2010. The Court has still not issued its ruling in this case. In the event that the Court finds in whole or in part for Plaintiff, we would be required to pay monetary damages in the amount held by the Court to have been underpaid in the earn-out. We are presently unable to reasonably estimate the amount of actual damages, if any, that will be awarded by the Court. If the Court were to find in favor of Plaintiff on every claim at issue in the litigation, the maximum potential damages award would be approximately \$6.0 million. Should we be required to pay any damages award, the associated payment would be allocated to goodwill in connection with Proficient acquisition.

On November 3, 2010, Gemini IP LLC filed an amended complaint in a suit pending in the United States District Court for the Eastern District of Texas, adding patent infringement allegations against us and various other defendants, including LANDesk Software, Inc., Saba Software, Inc., Genesys S.A. d/b/a Genesys Conferencing, Genesys Conferencing, Inc., Avaya Inc., Best Buy Co., Inc., Bomgar Corporation, ConnectWise, Inc., Elsinore Technologies Inc., GFI Software Ltd., GFI USA, Inc., GFI Software Development, Ltd., LogMeIn, Inc., N-able Technologies Incorporated, NTR Global, Venti Solutions, LLC, Zoho Corporation, Zenith Infotech Ltd., International Business Machines Corp., Samsung Electronics America, Inc., Samsung Electronics Co., Ltd., Samsung Telecommunications America, LLC, AT&T, Inc., Sony Corporation, and Sony Corporation of America. On August 26, 2011, Gemini and LivePerson jointly filed a motion asking the Court to dismiss all claims with prejudice. The Court has not yet ruled on that motion.

On June 15, 2011, we filed suit against Lodsystech, LLC, in the United States District Court for the Northern District of Illinois, seeking a declaratory judgment that our products do not infringe four patents which Lodsystech had previously

asserted were infringed by our customers, as well as a declaratory judgment that those four patents are invalid. On July 5, 2011, Lodsys moved to dismiss the Illinois case based on lacking personal jurisdiction, and also countersued us and other plaintiffs in similarly-situated declaratory judgment actions, including DriveTime Automotive Group, Inc., ESET, LLC, ForeSee Results, LLC, OpinionLab, Inc., and The New York Times Company, in the United States District Court for the Eastern District of Texas. In the Texas case, Lodsys alleges that we infringe one of the patents involved in the co-pending Illinois case, and seeks damages for past infringement, and an injunction against future infringement. We believe Lodsys's claims are without merit. On October 25, 2011 the Court granted the parties' joint motion to transfer the cases from Illinois to the Eastern District of Wisconsin, and all pending motions were withdrawn, including Lodsys's

TABLE OF CONTENTS

pending motion to dismiss. On January 6, 2012 Lodsys filed a motion to dismiss the Wisconsin case, or, in the alternative, for a more definite statement. On January 27, 2012 we filed an amended complaint in the Wisconsin case. On February 10, 2012 Lodsys filed a motion to dismiss the Wisconsin case, or, in the alternative, to transfer or stay. On January 23, 2012, we moved to dismiss the Texas case in favor of the first-filed Wisconsin case. On February 9, 2012 Lodsys filed its opposition to the Cour motion, and we filed our reply on February 21, 2012. This motion is fully briefed.

On February 7, 2012, we filed suit against Pragmatum Telecom LLC in the District of Delaware, seeking a declaratory judgment that our products do not infringe three patents owned by Pragmatum which Pragmatum had previously asserted were infringed by certain of our customers, as well as a declaratory judgment that those four patents are invalid.

Although we do not currently expect that the outcome in any of these matters, individually or collectively, will have a material adverse effect on our financial condition or results of operations, litigation is inherently unpredictable. Therefore, judgments could be rendered or settlements entered, that could adversely affect our operating results or cash flows in a particular period. We routinely assess all of our litigation and threatened litigation as to the probability of ultimately incurring a liability, and record our best estimate of the ultimate loss in situations where we assess the likelihood of loss as probable.

From time to time, we are involved in other legal proceedings arising in the ordinary course of its business, which may arise from direct legal claims brought by or against us, or from claims brought against our customers for which we have a contractual indemnification obligation.

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

Not Applicable.

TABLE OF CONTENTS

**PART II**

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

**Price Range of Common Stock**

The principal United States market on which our common stock is traded is The Nasdaq Capital Market of The Nasdaq Stock Market under the symbol LPSN. Our shares of common stock are also traded on the Tel Aviv Stock Exchange.

The following table sets forth, for each full quarterly period within the two most recent fiscal years, the high and low sales prices (in U.S. dollars per share) of our common stock as reported or quoted on The Nasdaq Capital Market:

	High	Low
Year ended December 31, 2011:		
First Quarter	\$ 12.67	\$ 9.72
Second Quarter	\$ 14.14	\$ 10.46
Third Quarter	\$ 14.71	\$ 9.95
Fourth Quarter	\$ 13.52	\$ 9.22
Year ended December 31, 2010:		
First Quarter	\$ 8.13	\$ 5.85
Second Quarter	\$ 8.94	\$ 5.99
Third Quarter	\$ 8.77	\$ 6.10
Fourth Quarter	\$ 11.75	\$ 8.47

**Holders**

As of February 28, 2012, there were approximately 186 holders of record of our common stock.

**Dividends**

We have not declared or paid any cash dividends on our capital stock since our inception. We intend to retain earnings, if any, to finance the operation and expansion of our business and do not anticipate paying any cash dividends in the foreseeable future.

**Issuer Purchases of Equity Securities**

On May 14, 2010, our Board of Directors approved a stock repurchase program through June 30, 2012.

The following table summarizes repurchases of our common stock under our stock repurchase program during the quarter ended December 31, 2011:



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Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(1)</sup>
10/1/2011 - 10/31/2011		\$		\$ 6,365,000
11/1/2011 - 11/30/2011				6,365,000
12/1/2011 - 12/31/2011				6,365,000
Total		\$		\$ 6,365,000

Under the stock repurchase program, we are authorized to repurchase shares of our common stock, in the open market or privately negotiated transactions, at times and prices considered appropriate by our Board of Directors (1) depending upon prevailing market conditions and other corporate considerations, up to an aggregate purchase price of \$10.0 million. As of March 1, 2012, approximately \$6.4 million remained available for purchases under the program.

30

TABLE OF CONTENTS

## Stock Performance Graph

The graph depicted below compares the annual percentage changes in the LivePerson's cumulative total stockholder return with the cumulative total return of the Standard & Poor's SmallCap 600 Index and the Standard & Poor's Information Technology Index.

### **COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\*** **Among Live Person, Inc., the S&P Smallcap 600 Index, and the S&P Information Technology Index**

\* \$100 invested on 12/31/06 in stock or index, including reinvestment of dividends.  
Fiscal year ending December 31.  
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Notes:

- (1) The graph covers the period from December 31, 2006 to December 31, 2011.
- (2) The graph assumes that \$100 was invested at the market close on December 31, 2006 in LivePerson's Common Stock, in the Standard & Poor's SmallCap 600 Index and in the Standard & Poor's Information Technology Index, and that all dividends were reinvested. No cash dividends have been declared on LivePerson's Common Stock.
- (3) Stockholder returns over the indicated period should not be considered indicative of future stockholder returns. *Notwithstanding anything to the contrary set forth in any of our previous or future filings under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, that might incorporate by reference this Annual Report on Form 10-K or future filings made by the Company under those statutes, the Stock Performance Graph above is not deemed filed with the Securities and Exchange Commission, is not deemed soliciting material and shall not be deemed incorporated by reference into any of those prior filings or into any future filings made by us under those statutes, except to the extent that we specifically incorporate such information by reference into a previous or future filing, or specifically requests that such information be treated as soliciting material, in each case under those statutes.*

TABLE OF CONTENTS**Item 6. Selected Consolidated Financial Data**

The selected consolidated financial data with respect to our consolidated balance sheets as of December 31, 2011 and 2010 and the related consolidated statements of operations for the years ended December 31, 2011, 2010 and 2009 have been derived from our audited consolidated financial statements which are included herein. The selected financial data with respect to our balance sheets as of December 31, 2009, 2008 and 2007 and the related statements of operations for the years ended December 31, 2008 and 2007 have been derived from our audited financial statements which are not included herein. Due to our acquisitions of NuConomy in April 2010 and Kasamba in October 2007, we believe that comparisons of our operating results with each other, or with those of prior periods, may not be meaningful. The following selected consolidated financial data should be read in conjunction with the consolidated financial statements and the notes thereto and the information contained in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

	Year Ended December 31,				
	2011	2010	2009	2008	2007
	(In Thousands, Except Share and per Share Data)				
Consolidated Statement of Operations Data:					
Revenue	\$133,089	\$109,862	\$87,490	\$74,655	\$52,228
Operating expenses:					
Cost of revenue	33,195	29,640	21,076	20,307	13,534
Product development	20,222	15,711	12,111	12,899	9,032
Sales and marketing	38,884	32,835	27,355	26,124	16,124
General and administrative	21,044	17,077	13,417	13,042	9,208
Amortization of intangibles	109	259	745	1,407	1,116
Goodwill impairment				23,501	
Total operating expenses	113,454	95,522	74,704	97,280	49,014
Income (loss) from operations	19,635	14,340	12,786	(22,625)	3,214
Other (expense) income:					
Financial (expense)	(548)	(106)	(80)	(376)	(18)
Interest income	63	99	94	329	914
Total other (expense) income, net	(485)	(7)	14	(47)	896
Income (loss) before (provision for) benefit from income taxes	19,150	14,333	12,800	(22,672)	4,110
(Provision for) benefit from income taxes <sup>(1)</sup>	(7,112)	(5,074)	(5,037)	(1,165)	1,711
Net income (loss) attributable to common stockholders	\$12,038	\$9,259	\$7,763	\$(23,837)	\$5,821
Basic net income (loss) per common share	\$0.23	\$0.18	\$0.16	\$(0.50)	\$0.13
Diluted net income (loss) per common share	\$0.22	\$0.18	\$0.16	\$(0.50)	\$0.12
Weighted average shares outstanding used in basic net income (loss) per common share	52,876,999	50,721,880	47,962,688	47,428,251	43,696,378

calculation

Weighted average shares

outstanding used in diluted net income (loss) per common share calculation	55,008,742	52,907,541	49,008,440	47,428,251	46,814,080
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(1) For the year ended December 31, 2007, the benefit from income taxes is related to the release of the Company's valuation allowance against deferred tax assets.

32

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TABLE OF CONTENTS

	December 31,				
	2011	2010	2009	2008	2007
	(In Thousands)				
Consolidated Balance Sheet Data:					
Cash and cash equivalents	\$ 93,278	\$ 61,336	\$ 45,572	\$ 25,500	\$ 26,222
Working capital	96,354	61,600	39,996	19,924	17,641
Total assets	166,051	131,143	104,281	81,948	102,488
Total stockholders equity	137,698	104,643	81,137	63,583	84,712

TABLE OF CONTENTS

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

### **General**

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which are prepared in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments and assumptions that management believes are reasonable based upon the information available. We base these estimates on our historical experience, future expectations and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for our judgments that may not be readily apparent from other sources. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods. These estimates and assumptions relate to estimates of the carrying amount of goodwill, intangibles, stock based-compensation, valuation allowances for deferred income taxes, accounts receivable, the expected term of a client relationship, accruals and other factors. We evaluate these estimates on an ongoing basis. Actual results could differ from those estimates under different assumptions or conditions, and any differences could be material.

### **Overview**

LivePerson provides online engagement solutions that facilitate real-time assistance and expert advice. We are organized into two operating segments: Business and Consumer. The Business segment facilitates real-time online interactions – chat, voice/click-to-call, email and self-service/knowledgebase for global corporations of all sizes. The Consumer segment facilitates online transactions between independent service providers ( Experts ) and individual consumers ( Users ) seeking help on the Web. We were incorporated in the State of Delaware in November 1995 and the LivePerson service was introduced initially in November 1998.

In order to sustain growth in these segments, our strategy is to expand our position as the leading provider of online engagement solutions that facilitate real-time assistance and expert advice. To accomplish this, we are focused on the following current initiatives:

*Expanding Business with Existing Customers and Adding New Customers.* We are expanding our sales capacity by adding enterprise sales agents, and we have recently established a midmarket sales group focused on adding new customers that are larger than our typical SMB customers, but smaller than our typical enterprise customers. We have also expanded our efforts to retain existing SMB customers through increased interaction with them during the early stages of their usage of our services.

*Introducing New Products and Capabilities.* We are investing in product marketing, research and development and executive personnel to support our expanding efforts to build and launch new products and capabilities to support existing customer deployments, and to further penetrate our total addressable market. These investments are initially focused in the areas of online marketing engagement and chat transcript text analysis. Over time, we expect to develop and launch additional capabilities that leverage our existing market position as a leader in proactive, intelligence-driven online engagement.

*Creating and Supporting an Open Development Platform.* We have recently introduced an open development platform capability, supported by a community of developers and developer tools that enable third-party developers to create and deliver new applications that leverage our existing customer base and proactive engagement technology.

By creating and supporting this platform, we expect to enable both independent developers and research and development personnel within our customer base to accelerate their product development and innovation, and to expand the value and usage of our current and future products and capabilities.

34

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## TABLE OF CONTENTS

*Expanding our international presence.* We continue to increase our investment in sales and support personnel in the United Kingdom, Latin America and Western Europe, particularly France and Germany. We are also working with sales and support partners as we expand our investment in the Asia-Pacific region. We continue to improve the multi-language and translation capabilities within our hosted solutions to further support international expansion.

## **Financial Overview for the Three and Twelve Months Ended December 31, 2011**

Financial overview of the three and twelve months ended December 31, 2011 compared to the comparable periods in 2010 are as follows:

Revenue increased 22% and 21% to \$36.5 million and \$133.1 million in the three and twelve months ended December 31, 2011, respectively from \$29.9 million and \$109.9 million in the comparable periods in 2010.

Gross profit margin increased to 78% and 75% in the three and twelve months ended December 31, 2011 from 72% and 73% in the in the comparable periods in 2010.

Operating expenses increased 18% and 19% to \$30.4 million and \$113.5 million in the three and twelve months ended December 31, 2011, respectively from \$25.8 million and \$95.5 million in the comparable periods in 2010.

We incurred financial expense of \$132,000 and \$548,000 in the three and twelve months ended December 31, 2011, respectively from \$59,000 and \$106,000 in the comparable periods in 2010.

Net income increased 41% to \$3.9 million in the three months ended December 31, 2011 from net income of \$2.7 million for the three months ended December 31, 2010. Net income increased 30% to \$12.0 million in the twelve months ended December 31, 2011 from net income of \$9.3 million for the twelve months ended December 31, 2010.

## **Critical Accounting Policies and Estimates**

The significant accounting policies which we believe are the most critical to aid in fully understanding and evaluating the reported consolidated financial results include the following:

### **Revenue Recognition**

The majority of our revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. Because we provide our application as a service, we follow the provisions of ASC 605-10-S99, Revenue Recognition and ASC 605-25, Revenue Recognition with Multiple-Element Arrangements. We charge a monthly fee, which varies by type of service, the level of customer usage and website traffic, and in some cases, the number of orders placed via our online engagement solutions.

For certain of our larger customers, we may provide call center labor through an arrangement with one or more of several qualified vendors. For most of these customers, we pass the fee we incur with the labor provider and our fee for the hosted services through to our customers in the form of a fixed fee for each order placed via our online engagement solutions. For these Pay for Performance ( PFP ) arrangements, we recognize revenue net of the labor provider s fee in accordance with ASC 605-45, Principal Agent Considerations, due primarily to the fact that the call center labor vendor is the primary obligor with respect to the labor services provided. Additionally, we perform as an agent without risk of loss for collection and do not bear inventory risk with respect to the outsourced labor services. Finally, we do not provide any part of the labor services, have no latitude in establishing prices for the labor services and generally do not have discretion in selecting the vendor.

The majority of our larger customers also pay a professional services fee related to implementation. We defer these implementation fees and associated direct costs and recognize them ratably over the expected term of the client



relationship upon commencement of the hosting services. We may also charge professional service fees related to additional training, business consulting and analysis in support of the LivePerson services.

## TABLE OF CONTENTS

We also sell certain of the LivePerson services directly via Internet download. These services are marketed as LivePerson Pro and LivePerson Contact Center for small and mid-sized businesses (SMBs), and are paid for almost exclusively by credit card. Credit card payments accelerate cash flow and reduce our collection risk, subject to the merchant bank's right to hold back cash pending settlement of the transactions. Sales of LivePerson Pro and LivePerson Contact Center may occur with or without the assistance of an online sales representative, rather than through face-to-face or telephone contact that is typically required for traditional direct sales.

We recognize monthly service revenue based upon the fee charged for the LivePerson services, provided that there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable. Our service agreements typically have twelve month terms and are terminable or may terminate upon 30 to 90 days' notice without penalty. When professional service fees add value to the customer on a standalone basis, we recognize professional service fees upon completion and customer acceptance in accordance with FASB Accounting Standards Update 2009-13. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) estimates. If a professional services arrangement does not qualify for separate accounting, we recognize the fees, and the related labor costs, ratably over a period of 48 months, representing our current estimate of the term of the client relationship.

For revenue generated from online transactions between Experts and Users, we recognize revenue net of Expert fees in accordance with ASC 605-45, Principal Agent Considerations, due primarily to the fact that the Expert is the primary obligor. Additionally, we perform as an agent without any risk of loss for collection, and are not involved in selecting the Expert or establishing the Expert's fee. We collect a fee from the consumer and retain a portion of the fee, and then remit the balance to the Expert. Revenue from these transactions is recognized when there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable.

## **Stock-Based Compensation**

We follow ASC 718-10, Stock Compensation, which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. ASC 718-10 requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). Incremental compensation costs arising from subsequent modifications of awards after the grant date must be recognized.

As of December 31, 2011, there was approximately \$26.5 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements. That cost is expected to be recognized over a weighted average period of approximately 2.2 years.

## **Accounts Receivable**

Our customers are located primarily in the United States. We perform ongoing credit evaluations of our customers' financial condition (except for customers who purchase the LivePerson services by credit card via Internet download) and have established an allowance for doubtful accounts based upon factors surrounding the credit risk of customers, historical trends and other information that we believe to be reasonable, although they may change in the future. If there is a deterioration of a customer's credit worthiness or actual write-offs are higher than our historical experience, our estimates of recoverability for these receivables could be adversely affected. Our concentration of credit risk is

limited due to our large number of customers; we do have several large customers. If we experience a significant write-off from one of these large customers, it could have a material adverse impact on our consolidated financial statements. No single customer accounted for or exceeded 10% of our total revenue in 2011, 2010 and 2009. One customer accounted for approximately 18% and 22% of accounts receivable at December 31, 2011 and 2010, respectively. We increased our allowance for doubtful accounts by \$290,000 to approximately \$851,000, principally due to an increase in accounts receivable as a result of increased sales and to a lesser extent, to an increase in the proportion of our receivables due from customers with greater credit risk. We wrote off approximately \$163,000 of previously

## TABLE OF CONTENTS

reserved accounts, leaving a net allowance for doubtful accounts of approximately \$688,000. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles.

### **Goodwill**

In accordance with ASC 350, Goodwill and Other Intangible Assets, goodwill and indefinite-lived intangible assets are not amortized, but reviewed for impairment upon the occurrence of events or changes in circumstances that would reduce the fair value below its carrying amount. Goodwill is required to be tested for impairment at least annually. In

September 2011, the FASB issued ASU No. 2011-08, Intangibles – Goodwill and Other (Topic 350). ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. If it is determined that the fair value of a reporting unit is more likely than not to be less than its carrying value (including unrecognized intangible assets) than it is necessary to perform the second step of the goodwill impairment test. The second step of the goodwill impairment test is judgmental in nature and often involves the use of significant estimates and assumptions. Similarly, estimates and assumptions are used in determining the fair value of other intangible assets. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. We perform internal valuation analyses and consider other market information that is publicly available. Estimates of fair value are primarily determined using discounted cash flows and market comparisons. These approaches use significant estimates and assumptions including projected future cash flows (including timing), discount rates reflecting the risk inherent in future cash flows, perpetual growth rates, determination of appropriate market comparables and the determination of whether a premium or discount should be applied to comparables.

In the third quarter of 2011, we adopted ASU 2011-08 and determined that it is not more-likely that the fair value of the reporting units are less than their carrying amount. Accordingly, we did not perform the two-step goodwill impairment test.

### **Impairment of Long-Lived Assets**

In accordance with ASC 360-10, Accounting for the Impairment or Disposal of Long-lived Assets, long-lived assets, such as property, plant and equipment and purchased intangibles subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying value of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying value of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying value of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying value or the fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

### **Use of Estimates**

The preparation of our consolidated financial statements in accordance with accounting principles generally accepted in the U.S. requires our management to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period. Significant items subject to such

estimates and assumptions include the carrying amount of goodwill, intangibles, stock-based compensation, valuation allowances for deferred income tax assets, accounts receivable, the expected term of a customer relationship, accruals and other factors. Actual results could differ from those estimates.

TABLE OF CONTENTS

**Recently Issued Accounting Standards**

In December 2011, the FASB issued ASU No. 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities. This ASU is intended to provide enhanced disclosures that will enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities within the scope of this update. The amendments require enhanced disclosures by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45. An entity is required to apply this amendment for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. ASU No. 2011-11 relates specifically to disclosures, it will not have an impact on our consolidated financial statements.

In September 2011, the FASB issued ASU No. 2011-08, Intangibles – Goodwill and Other (Topic 350): Testing Goodwill for Impairment. This ASU is intended to simplify how entities, test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, Intangibles – Goodwill and Other. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. This update is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued. We elected early adoption of this update and it had no impact on our consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. This ASU represents the converged guidance of the FASB and the IASB (the Boards) on fair value measurement. The collective efforts of the Boards and their staffs, reflected in ASU 2011-04, have resulted in common requirements for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning of the term fair value. The Boards have concluded the common requirements will result in greater comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and IFRSs. The amendments to the FASB Accounting Standards Codification (Codification) in this ASU are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011. Early application by public entities is not permitted. We are currently assessing the impact of this update on our consolidated financial statements.

**Revenue**

The majority of our revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. We charge a monthly fee, which varies by service and customer usage. The majority of our larger customers also pay a professional services fee related to implementation. A large proportion of our revenue from new customers comes from large corporations. These companies typically have more significant implementation requirements and more stringent data security standards. Such customers also have more sophisticated data analysis and performance reporting requirements, and are likely to engage our professional services organization to provide such analysis and reporting on a recurring basis.

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Revenue from our Business segment accounted for 89% of total revenue for the year ended December 31, 2011. Revenue from our Business segment accounted for 87% and 86% of total revenue for the years ended December 31, 2010 and 2009, respectively. Revenue attributable to our monthly hosted Business services accounted for 94% of total Business revenue for the year ended December 31, 2011. Revenue attributable to our monthly hosted Business services accounted for 95% of total Business revenue for the year ended December 31, 2010. Revenue attributable to our monthly hosted Business services accounted for 96%

38

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## TABLE OF CONTENTS

of total Business revenue for the year ended December 31, 2009. Our service agreements typically have twelve month terms and, in some cases, are terminable or may terminate upon 30 to 90 days notice without penalty. Given the time required to schedule training for our customers operators and our customers resource constraints, we have historically experienced a lag between signing a customer contract and recognizing revenue from that customer. This lag has recently ranged from 30 to 90 days.

Revenue from our Consumer segment is generated from online transactions between Experts and Users is recognized net of Expert fees and accounted for approximately 11% of total revenue for the year ended December 31, 2011. Revenue generated from online transactions between Experts and Users accounted for approximately 13% and 14% of total revenue for the years ended December 31, 2010 and 2009, respectively.

We also have entered into contractual arrangements that complement our direct sales force and online sales efforts. These are primarily with call center service companies, pursuant to which LivePerson is paid a commission based on revenue generated by these service companies from our referrals. To date, revenue from such commissions has not been material.

## **Operating Expenses**

Our cost of revenue consists of:

compensation costs relating to employees who provide customer support and implementation services to our customers;

compensation costs relating to our network support staff;  
depreciation of certain hardware and software;  
allocated occupancy costs and related overhead;

the cost of supporting our infrastructure, including expenses related to server leases, infrastructure support costs and Internet connectivity;

the credit card fees and related payment processing costs associated with the consumer and SMB services; and  
amortization of certain intangibles.

Our product development expenses consist primarily of compensation and related expenses for product development personnel, allocated occupancy costs and related overhead, outsourced labor and expenses for testing new versions of our software. Product development expenses are charged to operations as incurred.

Our sales and marketing expenses consist of compensation and related expenses for sales personnel and marketing personnel, online marketing, allocated occupancy costs and related overhead, advertising, sales commissions, public relations, promotional materials, travel expenses and trade show exhibit expenses.

Our general and administrative expenses consist primarily of compensation and related expenses for executive, accounting, legal and human resources personnel, allocated occupancy costs and related overhead, professional fees, provision for doubtful accounts and other general corporate expenses.

During 2011, we increased our allowance for doubtful accounts by \$290,000 to approximately \$851,000, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of receivables due from customers with greater credit risk. We wrote off approximately \$163,000 of previously reserved accounts, leaving a net allowance for doubtful accounts of approximately \$688,000. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles. During 2010, we increased our allowance for doubtful accounts by \$166,000 to approximately \$561,000, principally due to an



increase in accounts receivable as a result of increased sales. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles. We base our allowance for doubtful accounts on specifically identified credit risks of customers, historical trends and other information that we believe to be reasonable. We adjust our allowance for doubtful accounts when accounts previously reserved have been collected.

TABLE OF CONTENTS**Non-Cash Compensation Expense**

The net non-cash compensation amounts for the years ended December 31, 2011, 2010 and 2009 consist of:

	2011	2010	2009
	(In Thousands)		
Stock-based compensation expense related to ASC 718-10	\$ 6,771	\$ 5,142	\$ 4,726
Total	\$ 6,771	\$ 5,142	\$ 4,726

**Results of Operations**

The Company is organized into two operating segments. The Business segment facilitates real-time online interactions chat, voice/click-to-call, email and self-service/knowledgebase for global corporations of all sizes. The Consumer segment facilitates online transactions between Experts and Users.

**Comparison of Fiscal Years Ended December 31, 2011 and 2010**

*Revenue Business.* Revenue increased by 24% to \$118.6 million for the year ended December 31, 2011, from \$95.7 million for the year ended December 31, 2010. This increase is primarily attributable to revenue from new customers in the amount of approximately \$11.3 million and, to a lesser extent, to revenue from existing customers who increased their use of our services in the amount of approximately \$9.4 million, net of cancellations, as well as an increase in professional services revenue of approximately \$2.2 million. Our revenue growth has traditionally been driven by a mix of revenue from new customers as well as expanding business and revenue from existing customers.

*Revenue Consumer.* Revenue increased by 2% to \$14.5 million for the year ended December 31, 2011, from \$14.2 million for the year ended December 31, 2010. This increase is primarily attributable to an increase in gross revenue as a result of higher rates charged by experts, partially offset by a decrease in minutes. In addition, net revenue also increased due to an increase in the fees we charge experts.

*Cost of Revenue Business.* Cost of revenue consists of compensation costs relating to employees who provide customer service to our customers, compensation costs relating to our network support staff, the cost of supporting our server and network infrastructure, and allocated occupancy costs and related overhead. Cost of revenue increased by 15% to \$29.8 million in 2011, from \$25.9 million in 2010. This increase in expense is primarily attributable to an increase in total compensation and related costs for additional and existing customer service and network operations personnel in the amount of approximately \$2.6 million and an increase for primary and backup server facilities and allocated overhead related to costs of supporting our server and network infrastructure of approximately \$1.2 million as a result of increased revenue.

*Cost of Revenue Consumer.* Cost of revenue consists of compensation costs relating to employees who provide customer service to Experts and Users, compensation costs relating to our network support staff, the cost of supporting our server and network infrastructure, credit card and transaction processing fees and related costs, and allocated occupancy costs and related overhead. Cost of revenue decreased by 10% to \$3.4 million in 2011, from \$3.8 million in 2010. This decrease is primarily attributable to the intangible assets related to the Kasamba acquisition that was fully amortized as of September 30, 2011.

*Product Development.* Our product development expenses consist primarily of compensation and related expenses for product development personnel as well as allocated occupancy costs and related overhead. Product development costs

increased by 29% to \$20.2 million in 2011, from \$15.7 million in 2010. This increase is primarily attributable to an increase in compensation and related costs for additional and existing product development personnel of approximately \$4.5 million as a result of our increased efforts to expand our product offerings. We are increasing our investment in new product development efforts to expand future product offerings. We are also investing in partner programs that enable third-parties to develop value-added software applications for our existing and future customers.

40

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TABLE OF CONTENTS

*Sales and Marketing Business.* Our sales and marketing expenses consist of compensation and related expenses for sales and marketing personnel, as well as advertising, public relations, trade show exhibit expenses and allocated occupancy costs and related overhead. Sales and marketing expenses increased by 25% to \$32.7 million in 2011, from \$26.2 million in 2010. This increase is primarily attributable to an increase in compensation and related costs for additional and existing sales and marketing personnel of approximately \$4.6 million, an increase in advertising, public relations and trade show exhibit expenses of approximately \$1.2 million, and an increase in allocated occupancy costs and related overhead in the amount of approximately \$593,000. This increase relates to our continued efforts to enhance our brand recognition and increase sales lead activity.

*Sales and Marketing Consumer.* Our sales and marketing expenses consist of compensation and related expenses for marketing personnel, as well as online promotion and trade show exhibit expenses and allocated occupancy costs and related overhead. Sales and marketing expenses decreased by 7% to \$6.2 million in 2011, from \$6.7 million in 2010. This decrease is primarily attributable to a decrease in compensation and related costs and allocated overhead for additional and existing marketing personnel in the amount of approximately \$554,000.

*General and Administrative.* Our general and administrative expenses consist primarily of compensation and related expenses for executive, accounting, legal, human resources and administrative personnel, allocated occupancy costs and related overhead, professional fees, provision for doubtful accounts and other general corporate expenses. General and administrative expenses increased by 23% to \$21.0 million in 2011, from \$17.1 million in 2010. This increase is primarily attributable to an increase in compensation and related expenses for additional and existing accounting, legal and human resource personnel in the amount of approximately \$2.3 million and increases in legal and other professional, depreciation, rent and telephone expenses in the amounts of \$1.0 million, \$125,000, \$84,000 and \$82,000, respectively.

*Amortization of Intangibles.* Amortization expense was \$109,000 for the year ended December 31, 2011 and relates primarily to acquisition costs recorded as a result of our acquisition of NuConomy in April 2010 and to the purchases of patents in August 2009. Amortization expense was \$259,000 for the year ended December 31, 2010 and relates primarily to acquisition costs recorded as a result of our acquisition of Kasamba in October 2007. This decrease is attributable to the fact that the intangible assets related to the Kasamba acquisition were fully amortized in 2010. Additional amortization expense in the amount of \$920,000 and \$1.2 million is included in cost of revenue for the years ended December 31, 2011 and 2010, respectively. Amortization expense is expected to be approximately \$306,000 in the year ended December 31, 2012.

*Other (Expense) Income.* Financial expense was \$548,000 and \$106,000 in the twelve months ended December 31, 2011 and 2010, respectively. Financial expense is the result of currency rate fluctuations associated with the exchange rate movement of the U.S. dollar against the New Israeli Shekel. Interest income was \$63,000 and \$99,000 in the twelve months ended December 31, 2011 and 2010 respectively, and consists of interest earned on cash and cash equivalents. This decrease is primarily attributable to decrease in short term interest rates partially offset by increases in cash and cash equivalents.

*Provision for Income Taxes.* For the year ended December 31, 2011, our effective tax rate was 37.1% resulting in a provision for income taxes of \$7.1 million. For the year ended December 31, 2010, our effective tax rate was 35.4% resulting in a provision for income taxes of \$5.1 million in 2010. The increase in effective tax rate is primarily due to a decrease in deductible expenses resulting from disqualifying dispositions from the exercise of incentive stock options in the year ended December 31, 2011.

*Net Income.* We had net income of \$12.0 million in 2011 compared to net income of \$9.3 million in 2010. Revenue increased \$23.2 million while operating expenses increased by \$17.9 million, contributing to a net increase in income

from operations of \$5.3 million.

TABLE OF CONTENTS

**Comparison of Fiscal Years Ended December 31, 2010 and 2009**

*Revenue Business.* Revenue increased by 27% to \$95.7 million for the year ended December 31, 2010, from \$75.6 million for the year ended December 31, 2009. This increase is primarily attributable to revenue from new customers in the amount of approximately \$12.0 million and, to a lesser extent, to revenue from existing customers who increased their use of our services in the amount of approximately \$6.9 million, net of cancellations, partially offset by a decrease in professional services revenue of approximately \$1.2 million. Our revenue growth has traditionally been driven by a mix of revenue from new customers as well as expansion from existing customers.

*Revenue Consumer.* Revenue increased by 19% to \$14.2 million for the year ended December 31, 2010, from \$11.9 million for the year ended December 31, 2009. This increase is primarily attributable to an increase in gross revenue of approximately \$1.8 million as a result of higher rates charged by Experts. In addition, net revenue also increased due to an increase in the fees we charge Experts of approximately \$500,000.

*Cost of Revenue Business.* Cost of revenue consists of compensation costs relating to employees who provide customer service to our customers, compensation costs relating to our network support staff, the cost of supporting our server and network infrastructure, and allocated occupancy costs and related overhead. Cost of revenue increased by 48% to \$25.9 million in 2010, from \$17.5 million in 2009. This increase in expense is primarily attributable to an increase for primary and backup server facilities and allocated overhead related to costs of supporting our server and network infrastructure of approximately \$4.1 million as a result of increased revenue and an increase in total compensation and related costs for additional and existing customer service and network operations personnel in the amount of approximately \$4.1 million. The increase in cost of revenue in excess of revenue growth was driven primarily by increased investment in more robust business continuity capabilities within our hosting facilities. In addition, costs related to data collection and storage has increased, as we have improved the scope and quality of the analytical reporting we provide to our larger customers.

*Cost of Revenue Consumer.* Cost of revenue consists of compensation costs relating to employees who provide customer service to Experts and Users, compensation costs relating to our network support staff, the cost of supporting our server and network infrastructure, credit card and transaction processing fees and related costs, and allocated occupancy costs and related overhead. Cost of revenue increased by 6% to \$3.8 million in 2010, from \$3.6 million in 2009. This increase is primarily attributable to an increase in credit card and transaction processing fees and related costs in the amount of approximately \$97,000 and to an increase in primary and backup server facilities and allocated overhead related to costs of supporting our server and network infrastructure of approximately \$80,000 as a result of increased revenue and an increase in total compensation and related costs for additional and existing customer service and network support personnel in the amount of approximately \$50,000.

*Product Development.* Our product development expenses consist primarily of compensation and related expenses for product development personnel as well as allocated occupancy costs and related overhead. Product development costs increased by 30% to \$15.7 million in 2010, from \$12.1 million in 2009. This increase is primarily attributable to an increase in compensation and related costs for additional and existing product development personnel as a result of our increased efforts to expand our product offerings of approximately \$3.1 million and allocated occupancy costs and related overhead in the amount of approximately \$477,000. We are increasing our investment in new product development efforts to expand future product offerings. We are also investing in partner programs that enable third-parties to develop value-added software applications for our existing and future customers.

*Sales and Marketing Business.* Our sales and marketing expenses consist of compensation and related expenses for sales and marketing personnel, as well as advertising, public relations, trade show exhibit expenses and allocated

occupancy costs and related overhead. Sales and marketing expenses increased by 29% to \$26.2 million in 2010, from \$20.4 million in 2009. This increase is primarily attributable to an increase in compensation and related costs for additional and existing sales and marketing personnel of approximately \$4.9 million, an increase in allocated occupancy costs and related overhead in the amount of

## TABLE OF CONTENTS

approximately \$478,000 and an increase in advertising, public relations and trade show exhibit expenses of approximately \$457,000. This increase relates to our continued efforts to enhance our brand recognition and increase sales lead activity.

*Sales and Marketing – Consumer.* Our sales and marketing expenses consist of compensation and related expenses for marketing personnel, as well as online promotion, public relations, trade show exhibit expenses and allocated occupancy costs and related overhead. Sales and marketing expenses decreased by 5% to \$6.7 million in 2010, from \$7.0 million in 2009. This decrease is primarily attributable to a decrease in advertising and promotional expenses of approximately \$423,000 driven by improved efficiency in search engine optimization partially offset by an increase in compensation and related costs and allocated overhead for additional and existing marketing personnel in the amount of approximately \$69,000.

*General and Administrative.* Our general and administrative expenses consist primarily of compensation and related expenses for executive, accounting, legal, human resources and administrative personnel. General and administrative expenses increased by 27% to \$17.1 million in 2010, from \$13.4 million in 2009. This increase is primarily attributable to an increase in compensation and related expenses for additional and existing accounting, legal and human resource personnel in the amount of approximately \$1.4 million and increases in rent, legal and other professional, corporate learning and development and telephone in the amounts of \$849,000, \$844,000, \$306,000 and \$257,000, respectively.

*Amortization of Intangibles.* Amortization expense was \$259,000 and \$745,000 in the years ended December 31, 2010 and 2009, respectively, and relates primarily to acquisition costs recorded as a result of our acquisition of Kasamba in October 2007 and Proficient in July 2006. This decrease is attributable to the fact that the intangible assets related to the Proficient acquisition were fully amortized in 2009. Additional amortization expense in the amount of \$1.2 million is included in cost of revenue for the years ended December 31, 2010 and 2009. Amortization expense is expected to be approximately \$964,000 in the year ended December 31, 2011.

*Other (Expense) Income.* Financial expense was \$106,000 and \$80,000 in the twelve months ended December 31, 2010 and 2009 respectively, and relates to unfavorable currency rate movements, related to our Israeli operations. Interest income was \$99,000 and \$94,000 in the twelve months ended December 31, 2010 and 2009 respectively, and consists of interest earned on cash and cash equivalents. These increases are primarily attributable to our increases in cash and cash equivalents partially offset to decreases in short term interest rates.

*(Provision for) Income Taxes.* For the year ended December 31, 2010, our effective tax rate was 35.4% resulting in a provision for income taxes of \$5.1 million. For the year ended December 31, 2009, our effective tax rate was 39.4% resulting in a provision for income taxes of \$5.0 million in 2009. The decrease in effective tax rate is primarily due to an increase in deductible expenses resulting from disqualifying dispositions from the exercise of incentive stock options in the year ended December 31, 2010.

*Net Income.* We had net income of \$9.3 million in 2010 compared to net income of \$7.8 million in 2009. Revenue increased \$22.4 million while operating expenses increased by \$20.8 million, contributing to a net increase in income from operations of \$1.6 million.

## **Liquidity and Capital Resources**

As of December 31, 2011, we had approximately \$93.3 million in cash and cash equivalents, an increase of approximately \$31.9 million from December 31, 2010. This increase is primarily attributable to net cash provided by



operating activities and, to a lesser extent, proceeds from the issuance of common stock in connection with the exercise of stock options by employees and the excess tax benefit from the exercise of employee stock options, partially offset by the purchases of fixed assets for our collocation facility and to the build-out of new office space in New York and Israel. We invest our cash in short-term money market funds.

Net cash provided by operating activities was \$25.1 million in the year ended December 31, 2011 and consisted of net income, non-cash expenses related to ASC-718-10, amortization of intangibles and depreciation and increases in deferred revenue, accounts payable and accrued expenses, deferred income taxes and a decrease in prepaid expenses, partially offset by an increase in accounts receivable. Net cash provided by operating activities was \$15.5 million in the year ended December 31, 2010 and consisted of net income,

## TABLE OF CONTENTS

non-cash expenses related to ASC-718-10, amortization of intangibles and depreciation and increases in deferred revenue, accounts payable and accrued expenses, deferred income taxes, partially offset by an increase in accounts receivable, prepaid expenses and other current assets.

Net cash used in investing activities was \$7.3 million in the year ended December 31, 2011 and was due primarily to build-out of new office space in New York and Israel and to a lesser extent, to purchases of fixed assets for our collocation facilities. Net cash used in investing activities was \$8.9 million in the year ended December 31, 2010 and was due primarily to purchase of fixed assets for our collocation facilities.

Net cash provided by financing activities was \$14.3 million in the year ended December 31, 2011 and consisted primarily of the proceeds from the issuance of common stock in connection with the exercise of stock options by employees and the excess tax benefit from exercise of employee stock options. Net cash provided by financing activities was \$9.2 million in the year ended December 31, 2010 and consisted primarily of the proceeds from the issuance of common stock in connection with the exercise of stock options by employees and the excess tax benefit from exercise of employee stock options, partially offset by the repurchase of common stock.

We have incurred significant expenses to develop our technology and services, to hire employees in our customer service, sales, marketing and administration departments, and for the amortization of intangible assets, as well as non-cash compensation costs. Historically, we incurred significant quarterly net losses from inception through June 30, 2003, significant negative cash flows from operations in our quarterly periods from inception through December 31, 2002 and negative cash flows from operations of \$124,000 in the three month period ended March 31, 2004. As of December 31, 2011, we had an accumulated deficit of approximately \$88.1 million. These losses have been funded primarily through the issuance of common stock in our initial public offering in 2000 and, prior to the initial public offering, the issuance of convertible preferred stock.

We anticipate that our current cash and cash equivalents will be sufficient to satisfy our working capital and capital requirements for at least the next 12 months. However, we cannot assure you that we will not require additional funds prior to such time, and we would then seek to sell additional equity or debt securities through public financings, or seek alternative sources of financing. We cannot assure you that additional funding will be available on favorable terms, when needed, if at all. If we are unable to obtain any necessary additional financing, we may be required to further reduce the scope of our planned sales and marketing and product development efforts, which could materially adversely affect our business, financial condition and operating results. In addition, we may require additional funds in order to fund more rapid expansion, to develop new or enhanced services or products or to invest in complementary businesses, technologies, services or products.

## **Contractual Obligations and Commitments**

We do not have any special purposes entities, and other than operating leases, which are described below. We do not engage in off-balance sheet financing arrangements.

We lease facilities and certain equipment under agreements accounted for as operating leases. These leases generally require us to pay all executory costs such as maintenance and insurance. Rental expense for operating leases for the years ended December 31, 2011 and 2010 was approximately \$6.6 million and \$6.4 million, respectively.

As of December 31, 2011, our principal commitments were approximately \$19.1 million under various operating leases, of which approximately \$7.1 million is due in 2012. We currently expect that our principal commitments for the year ending December 31, 2012 will not exceed \$8.0 million in the aggregate.



TABLE OF CONTENTS

Our contractual obligations at December 31, 2011 are summarized as follows:

Contractual Obligations	Payments Due by Period (In Thousands)				
	Total	Less Than 1 Year	1 3 Years	3 5 Years	More Than 5 Years
Operating leases	\$ 19,096	\$ 7,126	\$ 9,398	\$ 1,752	\$ 820
Total	\$ 19,096	\$ 7,126	\$ 9,398	\$ 1,752	\$ 820

**Capital Expenditures**

During 2007, we began to build a collocation facility in the eastern U.S. to host the Business and Consumer services.

During 2010, the Company began to build additional collocation facilities in Europe to host the LivePerson and Consumer services. Through December 31, 2011, we spent approximately \$21.4 million for servers, network components and related hardware and software. Though we expect to incur additional costs in 2012 related to the continued build-out of our collocation facilities and similar backup facilities to support disaster recovery capabilities in the U.S and U.K, our total capital expenditures are not currently expected to exceed \$10.0 million in 2012. We anticipate that our current cash and cash equivalents from operations will be sufficient to complete the build-out.

**Indemnifications**

We enter into service and license agreements in the ordinary course of business. Pursuant to some of these agreements, we agree to indemnify certain customers from and against certain types of claims and losses suffered or incurred by them as a result of using our products.

We also have agreements whereby our executive officers and directors are indemnified for certain events or occurrences while the officer or director is, or was serving, at our request in such capacity. The maximum potential amount of future payments we could be required to make under these indemnification agreements is unlimited; however, we have a directors and officers insurance policy that reduces our exposure and enables us to recover a portion of any future amounts paid. As a result of our insurance policy coverage, we believe the estimated fair value of these indemnification agreements is minimal. Currently, we have no liabilities recorded for these agreements as of December 31, 2011.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk****Currency Rate Fluctuations**

As a result of the expanding scope of our Israeli operations, our currency rate fluctuation risk associated with the exchange rate movement of the U.S. dollar against the New Israeli Shekel ( NIS ) has increased. For the year ended December 31, 2011, the U.S dollar appreciated approximately 8% as compared to the NIS. This fluctuation decreased the value of our NIS deposits which caused a non-cash re-measurement charge in the amount of \$548,000. For the year ended December 31, 2011, expenses generated by our Israeli operations totaled approximately \$37.8 million. We do not currently hedge our foreign currency risk exposure. We actively monitor the movement of the U.S. dollar against the NIS and U.K. pound and have considered the use of financial instruments, including but not limited to derivative financial instruments, which could mitigate such risk. If we determine that our risk of exposure materially

exceeds the potential cost of derivative financial instruments, we may in the future enter in to these types of investments. The functional currency of our wholly-owned Israeli subsidiaries, LivePerson Ltd. (formerly HumanClick Ltd.) and Kasamba Ltd., is the U.S. dollar and the functional currency of our operations in the United Kingdom is the U.K. pound.

TABLE OF CONTENTS

## **Collection Risk**

Our accounts receivable are subject, in the normal course of business, to collection risks. We regularly assess these risks and have established policies and business practices to protect against the adverse effects of collection risks. During 2011, we increased our allowance for doubtful accounts \$290,000 to approximately \$851,000, principally due to an increase in accounts receivable as a result of increased sales and, to a lesser extent, to an increase in the proportion of our receivables due from customers with greater credit risk. We wrote off approximately \$163,000 of previously reserved accounts, leaving a net allowance for doubtful accounts of approximately \$688,000. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles. During 2010, we increased our allowance for doubtful accounts by \$166,000 to approximately \$561,000, principally due to an increase in accounts receivable as a result of increased sales. A larger proportion of receivables are due from larger corporate customers that typically have longer payment cycles.

## **Interest Rate Risk**

Our investments consist of cash and cash equivalents. Therefore, changes in the market's interest rates do not affect in any material respect the value of the investments as recorded by us.

TABLE OF CONTENTS

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

**INDEX**

	Page
<u>Report of BDO USA, LLP, Independent Registered Public Accounting Firm</u>	<u>48</u>
<u>Consolidated Balance Sheets as of December 31, 2011 and 2010</u>	<u>49</u>
<u>Consolidated Statements of Income for the years ended December 31, 2011, 2010 and 2009</u>	<u>50</u>
<u>Consolidated Statements of Comprehensive Income for the years ended December 31, 2011, 2010 and 2009</u>	<u>51</u>
<u>Consolidated Statements of Stockholders' Equity for the years ended December 31, 2011, 2010 and 2009</u>	<u>52</u>
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2011, 2010 and 2009</u>	<u>53</u>
<u>Notes to Consolidated Financial Statements</u>	<u>55</u>

---

47

TABLE OF CONTENTS

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
LivePerson, Inc.  
New York, NY

We have audited the accompanying consolidated balance sheets of LivePerson, Inc. as of December 31, 2011 and 2010 and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2011. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of LivePerson, Inc. at December 31, 2011 and 2010, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), LivePerson, Inc.'s internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 13, 2012 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

New York, New York  
March 13, 2012



TABLE OF CONTENTS**LIVEPERSON, INC.****CONSOLIDATED BALANCE SHEETS  
(In Thousands, Except Share and per Share Data)**

	December 31,	
	2011	2010
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$93,278	\$61,336
Accounts receivable, net of allowance for doubtful accounts of \$688 and \$561, in 2011 and 2010, respectively	20,999	16,491
Prepaid expenses and other current assets	5,390	6,341
Deferred tax assets, net	2,342	1,529
Total current assets	122,009	85,697
Property and equipment, net	13,879	12,762
Intangibles, net	1,095	2,124
Goodwill	24,090	24,015
Deferred tax assets, net	2,829	3,876
Deferred implementation costs, net of current	247	164
Security deposits	356	499
Other assets	1,546	2,006
Total assets	\$ 166,051	\$ 131,143
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$8,258	\$6,416
Accrued expenses	12,019	12,111
Deferred revenue	5,378	5,570
Total current liabilities	25,655	24,097
Deferred revenue, net of current	1,152	513
Other liabilities	1,546	1,890
Total liabilities	28,353	26,500
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$.001 par value per share; 5,000,000 shares authorized, 0 shares issued and outstanding at December 31, 2011 and 2010		
Common stock, \$.001 par value per share; 100,000,000 shares authorized, 54,090,344 shares issued and outstanding at December 31, 2011; 51,753,842 shares issued and outstanding at December 31, 2010	54	52
Additional paid-in capital	226,113	205,063
Accumulated deficit	(88,135 )	(100,173 )
Accumulated other comprehensive loss	(334 )	(299 )
Total stockholders' equity	137,698	104,643

Total liabilities and stockholders' equity	\$ 166,051	\$ 131,143
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*See accompanying notes to consolidated financial statements.*

TABLE OF CONTENTS**LIVEPERSON, INC.****CONSOLIDATED STATEMENTS OF INCOME  
(In Thousands, Except Share and per Share Data)**

	Year Ended December 31,		
	2011	2010	2009
Revenue	\$133,089	\$109,862	\$87,490
Operating expenses:			
Cost of revenue	33,195	29,640	21,076
Product development	20,222	15,711	12,111
Sales and marketing	38,884	32,835	27,355
General and administrative	21,044	17,077	13,417
Amortization of intangibles	109	259	745
Total operating expenses	113,454	95,522	74,704
Income from operations	19,635	14,340	12,786
Other (expense) income:			
Financial expense	(548 )	(106 )	(80 )
Interest income	63	99	94
Total other (expense) income, net	(485 )	(7 )	14
Income before provision for income taxes	19,150	14,333	12,800
Provision for income taxes	7,112	5,074	5,037
Net income	12,038	9,259	7,763
Basic net income per common share	\$0.23	\$0.18	\$0.16
Diluted net income per common share	\$0.22	\$0.18	\$0.16
Weighted average shares outstanding used in basic net income per common share calculation	52,876,999	50,721,880	47,962,688
Weighted average shares outstanding used in diluted net income per common share calculation	55,008,742	52,907,541	49,008,440

*See accompanying notes to consolidated financial statements.*

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE  
INCOME  
(In Thousands)**

	Year Ended December 31,		
	2011	2010	2009
Net income	\$ 12,038	\$ 9,259	\$ 7,763
Foreign currency translation adjustment	(35 )	(127 )	(34 )
Comprehensive income	\$ 12,003	\$ 9,132	\$ 7,729

*See accompanying notes to consolidated financial statements.*

TABLE OF CONTENTS**LIVEPERSON, INC.**

**CONSOLIDATED STATEMENTS OF STOCKHOLDERS  
EQUITY  
(In Thousands, Except Share Data)**

	Common Stock Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
Balance at December 31, 2008	47,357,017	\$ 47	\$ 180,869	\$(117,195)	\$(138)	\$63,583
Repurchase of common stock	(16,223)		(28)			(28)
Common stock issued upon exercise of stock options	2,094,888	2	4,189			4,191
Stock-based compensation			4,726			4,726
Tax benefit from exercise of employee stock options			936			936
Net Income				7,763		7,763
Other comprehensive loss					(34)	(34)
Balance at December 31, 2009	49,435,682	49	190,692	(109,432)	(172)	81,137
Repurchase of common stock	(534,496)		(3,649)			(3,649)
Common stock issued upon exercise of stock options	2,843,547	3	11,407			11,410
Stock-based compensation			5,142			5,142
Common stock issued under Employee Stock Purchase Plan	9,109		74			74
Tax benefit from exercise of employee stock options			1,397			1,397
Net income				9,259		9,259
Other comprehensive loss					(127)	(127)
Balance at December 31, 2010	51,753,842	52	205,063	(100,173)	(299)	104,643
Common stock issued upon exercise of stock options	2,278,451	2	9,706			9,708
Stock-based compensation			6,771			6,771
Common stock issued under Employee Stock Purchase Plan	58,051		572			572
Tax benefit from exercise of employee stock options			4,001			4,001
Net income				12,038		12,038
Other comprehensive loss					(35)	(35)
Balance at December 31, 2011	54,090,344	\$ 54	\$ 226,113	\$(88,135)	\$(334)	\$ 137,698

*See accompanying notes to consolidated financial statements.*

TABLE OF CONTENTS**LIVEPERSON, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In Thousands)**

	Year Ended December 31,		
	2011	2010	2009
Cash flows from operating activities:			
Net income	\$12,038	\$9,259	\$7,763
Adjustments to reconcile net income to net cash provided by operating activities:			
Stock-based compensation expense	6,771	5,142	4,726
Depreciation	6,563	5,791	3,347
Amortization of intangibles	1,029	1,486	1,973
Provision for doubtful accounts, net	290	166	68
Deferred income taxes	229	832	2,865
Changes in operating assets and liabilities, net of acquisition:			
Accounts receivable	(4,798 )	(6,391 )	(2,760 )
Prepaid expenses and other current assets	665	(2,687 )	(1,948 )
Deferred implementation costs	(84 )	(28 )	12
Security deposits	146	(174 )	23
Other assets	116		(116 )
Accounts payable	1,451	45	1,836
Accrued expenses	211	1,224	2,367
Deferred revenue	447	884	866
Net cash provided by operating activities	25,074	15,549	21,022
Cash flows from investing activities:			
Purchases of property and equipment, including capitalized software	(7,268 )	(8,002 )	(5,442 )
Acquisition of NuConomy, net of cash acquired		(789 )	
Acquisition of Proficient	(75 )	(95 )	(98 )
Acquisition of patents			(475 )
Net cash used in investing activities	(7,343 )	(8,886 )	(6,015 )
Cash flows from financing activities:			
Repurchase of common stock		(3,649 )	(28 )
Excess tax benefit from the exercise of employee stock options and warrants	4,001	1,397	936
Proceeds from issuance of common stock in connection with the exercise of options and warrants	10,280	11,484	4,191
Net cash provided by financing activities	14,281	9,232	5,099
Effect of foreign exchange rate changes on cash and cash equivalents	(70 )	(131 )	(34 )
Net increase in cash and cash equivalents	31,942	15,764	20,072
Cash and cash equivalents at the beginning of the year	61,336	45,572	25,500
Cash and cash equivalents at the end of the year	\$93,278	\$61,336	\$45,572

*See accompanying notes to consolidated financial statements.*



TABLE OF CONTENTS

**LIVEPERSON, INC.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In Thousands, Except Share Data)**

**Supplemental disclosure of non-cash investing and financing activities:**

Cash flows from investing activities for the years ended December 31, 2011, 2010 and 2009 do not include the purchases of approximately \$1,631, \$1,259 and \$259, respectively of capitalized equipment related to the Company's collocation facilities because the corresponding invoices are included in accounts payable for the corresponding year end period, and therefore did not have an impact on cash flows.

During the years ended December 31, 2011, 2010 and 2009, total net cash paid for income taxes were \$2,579, \$3,800 and \$2,000, respectively.

During the year ended December 31, 2009, the Company settled a pre-acquisition contingency related to the Kasamba acquisition resulting in a decrease in accrued expenses in the amount of \$566.

*See accompanying notes to consolidated financial statements.*

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(1) Summary of Operations and Significant Accounting Policies**

**(a) Summary of Operations**

LivePerson, Inc. (the Company or LivePerson ) provides online engagement solutions that facilitate real-time assistance and expert advice. Connecting businesses and independent service providers with individual consumers seeking help on the Web, the Company s hosted software platform creates more relevant, compelling and personalized online experiences. The Company was incorporated in 1995 and commenced operations in 1996.

The Company s primary revenue source is from the sale of LivePerson services to businesses of all sizes. The Company also facilitates online transactions between independent service providers ( Experts ) who provide online advice to individual consumers ( Users ). Headquartered in New York City, the Company s product development staff, help desk, and online sales support are located in Israel. The Company also maintains sales and professional services offices in Atlanta, London, San Francisco and Melbourne.

**(b) Principles of Consolidation**

The consolidated financial statements reflect the operations of LivePerson and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

**(c) Use of Estimates**

The preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the U.S. requires the Company s management to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amount of goodwill, intangibles, stock-based compensation, valuation allowances for deferred income tax assets, accounts receivable, the expected term of a customer relationship, and accruals. Actual results could differ from those estimates.

**(d) Cash and Cash Equivalents**

The Company considers all highly liquid securities with original maturities of three months or less when acquired to be cash equivalents. Cash equivalents, which primarily consist of money market funds, are recorded at cost, which approximates fair value.

### **(e) Property and Equipment**

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the related assets, generally three to five years for equipment and software. Leasehold improvements are depreciated using the straight-line method over the shorter of the lease term or the estimated useful life of the asset. Total depreciation for the years ended December 31, 2011, 2010 and 2009 was \$6,563, \$5,791, and \$3,347, respectively.

### **(f) Impairment of Long-Lived Assets**

In accordance with the Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) 360-10, Accounting for the Impairment or Disposal of Long-lived Assets, long-lived assets, such as property, plant and equipment and purchased intangibles subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying value of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying value of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying value of the asset exceeds the fair value of the asset. Assets to be disposed of

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(1) Summary of Operations and Significant Accounting Policies  
(continued)**

would be separately presented in the balance sheet and reported at the lower of the carrying value or the fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

**(g) Accounts Receivable**

Accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company determines the allowance based on historical write-off experience. The Company reviews its allowance for doubtful accounts monthly. Past due balances over 90 days and over a specified amount are reviewed individually for collectability. All other balances are reviewed on a pooled basis. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance sheet credit exposure related to its customers.

**(h) Revenue Recognition**

The majority of the Company's revenue is generated from monthly service revenues and related professional services from the sale of the LivePerson services. Because the Company provides its application as a service, the Company follows the provisions of FASB ASC 605-10-S99, Revenue Recognition and ASC 605-25, Revenue Recognition with Multiple-Element Arrangements. The Company charges a monthly fee, which varies by type of service, the level of customer usage and website traffic, and in some cases, the number of orders placed via the Company's online engagement solutions.

For certain of the Company's larger customers, the Company may provide call center labor through an arrangement with one or more of several qualified vendors. For most of these customers, the Company passes the fee it incurs with the labor provider and its fee for the hosted services through to its customers in the form of a fixed fee for each order placed via the Company's online engagement solutions. For these Pay for Performance ( PFP ) arrangements, the Company recognizes revenue net of the labor provider's fee in accordance with ASC 605-45, Principal Agent Considerations, due primarily to the fact that the call center labor vendor is the primary obligor with respect to the labor services provided. Additionally, the Company performs as an agent without risk of loss for collection and does not bear inventory risk with respect to the outsourced labor services. Finally, the Company does not provide any part of the labor services, has no latitude in establishing prices for the labor services and generally does not have discretion in selecting the vendor.

The majority of the Company's larger customers also pay a professional services fee related to implementation. The Company defers these implementation fees and associated direct costs and recognizes them ratably over the expected term of the customer relationship upon commencement of the hosting services. The Company may also charge professional service fees related to additional training, business consulting and analysis in support of the LivePerson services.

The Company also sells certain of the LivePerson services directly via Internet download. These services are marketed as LivePerson Pro and LivePerson Contact Center for small and mid-sized businesses (SMBs), and are paid for almost exclusively by credit card. Credit card payments accelerate cash flow and reduce the Company's collection risk, subject to the merchant bank's right to hold back cash pending settlement of the transactions. Sales of LivePerson Pro and LivePerson Contact Center may occur with or without the assistance of an online sales representative, rather than through face-to-face or telephone contact that is typically required for traditional direct sales.

56

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TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(1) Summary of Operations and Significant Accounting Policies  
(continued)**

The Company recognizes monthly service revenue based upon the fee charged for the LivePerson services, provided that there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable. The Company's service agreements typically have twelve month terms and, in some cases, are terminable or may terminate upon 30 to 90 days notice without penalty. When professional service fees add value to the customer on a standalone basis, the Company recognizes professional service fees upon completion and customer acceptance in accordance with FASB Accounting Standards Update 2009-13. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) estimates. If a professional services arrangement does not qualify for separate accounting, the Company recognizes the fees, and the related labor costs, ratably over a period of 48 months, representing the Company's current estimate of the term of the customer relationship.

For revenue generated from online transactions between Experts and Users, the Company recognizes revenue net of the Expert fees in accordance with ASC 605-45, Principal Agent Considerations, due primarily to the fact that the Expert is the primary obligor. Additionally, the Company performs as an agent without any risk of loss for collection, and is not involved in selecting the Expert or establishing the Expert's fee. The Company collects a fee from the User and retains a portion of the fee, and then remits the balance to the Expert. Revenue from these transactions is recognized when there is persuasive evidence of an arrangement, no significant Company obligations remain, collection of the resulting receivable is probable and the amount of fees to be paid is fixed or determinable.

**(i) Income Taxes**

Income taxes are accounted for under the asset and liability method. 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 rates is recognized in results of operations in the period that the tax change occurs. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

**(j) Advertising Costs**

The Company expenses the cost of advertising and promoting its services as incurred. Such costs totaled approximately \$6,310, \$6,132, and \$6,098 for the years ended December 31, 2011, 2010 and 2009, respectively.

## **(k) Financial Instruments and Concentration of Credit Risk**

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable which approximate fair value at December 31, 2011 because of the short-term nature of these instruments. The Company invests its cash and cash equivalents with financial institutions that it believes are of high quality, and performs periodic evaluations of these instruments and the relative credit standings of the institutions with which it invests. At certain times, the Company's cash balances with any one financial institution may exceed Federal Deposit Insurance Corporation insurance limits. The Company believes it mitigates its risk by depositing its cash balances with high credit, quality financial institutions.

57

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TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

The Company's customers are located primarily in the United States. The Company performs ongoing credit evaluations of its customers' financial condition (except for customers who purchase the LivePerson services by credit card via Internet download) and has established an allowance for doubtful accounts based upon factors surrounding the credit risk of customers, historical trends and other information. Concentration of credit risk is limited due to the Company's large number of customers. No single customer accounted for or exceeded 10% of revenue in 2011, 2010 or 2009. One customer accounted for approximately 18% and 22% of accounts receivable at December 31, 2011 and 2010, respectively.

**(I) Stock-based Compensation**

The Company follows FASB ASC 718-10, Stock Compensation, which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. ASC 718-10 requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). Incremental compensation costs arising from subsequent modifications of awards after the grant date must be recognized.

The following table summarizes stock-based compensation expense related to employee stock options under ASC 718-10 included in Company's Statement of Income for the years ended December 31, 2011, 2010 and 2009:

	December 31,		
	2011	2010	2009
Cost of revenue	\$1,023	\$ 866	\$ 790
Product development expense	1,703	1,329	1,402
Sales and marketing expense	1,668	1,371	1,337
General and administrative expense	2,377	1,576	1,197
Total stock based compensation included in operating expenses	\$6,771	\$ 5,142	\$ 4,726

The per share weighted average fair value of stock options granted during the years ended December 31, 2011, 2010 and 2009 was \$6.47, \$3.89 and \$1.53, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for the years ended December 31, 2011, 2010 and 2009:



	December 31,					
	2011		2010		2009	
Dividend yield	0.0%		0.0%		0.0%	
Risk-free interest rate	0.9%	3.7%	2.6%	3.8%	2.8%	3.9
Expected life (in years)	5.0		5.0		5.0	
Historical volatility	60.1%	61.5%	60.3%	61.9%	61.3%	68.2%

### (m) Basic and Diluted Net Income per Share

The Company calculates earnings per share ( EPS ) in accordance with the provisions of ASC 260-10 and the guidance of SEC Staff Accounting Bulletin ( SAB ) No. 98. Under ASC 260-10, basic EPS excludes dilution for common stock equivalents and is computed by dividing net income or loss attributable to common shareholders by the weighted average number of common shares outstanding for the period. All options, warrants or other potentially dilutive instruments issued for nominal consideration are required to be included in the calculation of basic and diluted net income attributable to common stockholders. Diluted EPS is

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

calculated using the treasury stock method and reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock and resulted in the issuance of common stock.

Diluted net income per common share for the year ended December 31, 2011 includes the effect of options to purchase 5,235,305 shares of common stock with a weighted average exercise price of \$4.94. Diluted net income per common share for the year ended December 31, 2011 does not include the effect of options to purchase 3,608,110 shares of common stock as the effect of their inclusion is anti-dilutive. Diluted net income per common share for the year ended December 31, 2010 includes the effect of options to purchase 5,294,867 shares of common stock with a weighted average exercise price of \$3.61. Diluted net income per common share for the year ended December 31, 2010 does not include the effect of options to purchase 3,524,395 shares of common stock as the effect of their inclusion is anti-dilutive. Diluted net income per common share for the year ended December 31, 2009 includes the effect of options to purchase 3,358,569 shares of common stock with a weighted average exercise price of \$2.04. Diluted net income per common share for the year ended December 31, 2009 does not include the effect of options to purchase 5,353,242 shares of common stock as the effect of their inclusion is anti-dilutive.

A reconciliation of shares used in calculating basic and diluted earnings per share follows:

	Year Ended December 31,		
	2011	2010	2009
Basic	52,876,999	50,721,880	47,962,688
Effect of assumed exercised options	2,131,743	2,185,661	1,045,752
Diluted	55,008,742	52,907,541	49,008,440

**(n) Segment Reporting**

The Company accounts for its segment information in accordance with the provisions of ASC 280-10, Segment Reporting. ASC 280-10 establishes annual and interim reporting standards for operating segments of a company. ASC 280-10 requires disclosures of selected segment-related financial information about products, major customers, and geographic areas based on the Company's internal accounting methods. The Company is organized into two operating segments for purposes of making operating decisions and assessing performance. The Business segment supports and manages real-time online interactions—chat, voice/click-to-call, email and self-service/knowledgebase and sells its products and services to global corporations of all sizes. The Consumer segment facilitates online transactions between Experts and Users and sells its services to consumers. Both segments currently generate their revenue primarily in the U.S. The chief operating decision-makers evaluate performance, make operating decisions, and

allocate resources based on the operating income of each segment. The reporting segments follow the same accounting policies used in the preparation of the Company's consolidated financial statements which are described in the summary of significant accounting policies. The Company allocates cost of revenue, sales and marketing and amortization of purchased intangibles to the segments, but it does not allocate product development expenses, general and administrative expenses and income tax expense because management does not use this information to measure performance of the operating segments. There are currently no intersegment sales.

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

Summarized financial information by segment for the year ended December 31, 2011, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows:

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services Business	\$ 111,934	\$	\$ 111,934	\$
Hosted services Consumer	14,522			14,522
Professional services	6,633		6,633	
Total revenue	133,089		118,567	14,522
Cost of revenue	33,195		29,793	3,402
Sales and marketing	38,884		32,690	6,194
Amortization of intangibles	109		109	
Unallocated corporate expenses	41,266	41,266		
Operating income (loss)	\$ 19,635	\$ (41,266)	\$ 55,975	\$ 4,926

Summarized financial information by segment for the year ended December 31, 2010, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows:

	Consolidated	Corporate	Business	Consumer
Revenue:				
Hosted services Business	\$ 91,262	\$	\$ 91,262	\$
Hosted services Consumer	14,195			14,195
Professional services	4,405		4,405	
Total revenue	109,862		95,667	14,195
Cost of revenue	29,640		25,863	3,777
Sales and marketing	32,835		26,184	6,651
Amortization of intangibles	259		43	216
Unallocated corporate expenses	32,788	32,788		
Operating income (loss)	\$ 14,340	\$ (32,788)	\$ 43,577	\$ 3,551

Summarized financial information by segment for the year ended December 31, 2009, based on the Company's internal financial reporting system utilized by the Company's chief operating decision makers, follows:

Consolidated	Corporate	Business	Consumer
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Revenue:					
Hosted services	Business	\$ 72,372	\$	\$ 72,372	\$
Hosted services	Consumer	11,942			11,942
Professional services		3,176		3,176	
Total revenue		87,490		75,548	11,942
Cost of revenue		21,076		17,522	3,554
Sales and marketing		27,355		20,350	7,005
Amortization of intangibles		745		457	288
Unallocated corporate expenses		25,528	25,528		
Operating income (loss)		\$ 12,786	\$ (25,528 )	\$ 37,219	\$ 1,095

60

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TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

Revenues attributable to domestic and foreign operations follows:

	December 31,		
	2011	2010	2009
United States	\$ 101,519	\$ 84,725	\$ 67,244
United Kingdom	18,250	14,110	9,650
Other Countries	13,320	11,027	10,596
Total revenue	\$ 133,089	\$ 109,862	\$ 87,490

Long-lived assets by geographic region follows:

	December 31,	
	2011	2010
United States	\$ 28,626	\$ 29,319
Israel	13,167	13,736
United Kingdom	2,249	2,391
Total long-lived assets	\$ 44,042	\$ 45,446

**(o) Comprehensive Loss**

ASC 220-10, Reporting Comprehensive Income, requires the Company to report in its consolidated financial statements, in addition to its net income, comprehensive loss, which includes all changes in equity during a period from non-owner sources including, as applicable, foreign currency items, minimum pension liability adjustments and unrealized gains and losses on certain investments in debt and equity securities. The Company's comprehensive loss for all periods presented is related to the effect of foreign translation losses.

**(p) Computer Software**

The Company follows the provisions of ASC 350-40, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. ASC 350-40 provides guidance for determining whether computer software is internal-use software and on accounting for the proceeds of computer software originally developed or obtained for internal use and then subsequently sold to the public. It also provides guidance on capitalization of the costs incurred for computer software developed or obtained for internal use. The Company capitalized \$1,086 as of December 31, 2011 and \$536 as of December 31, 2010. Software costs are included in Property and equipment, net on the Company's balance sheet and are depreciated using the straight-line method over their estimated useful life, generally three years.

## **(q) Goodwill and Intangible Assets**

In accordance with ASC 350, Goodwill and Other Intangible Assets, goodwill and indefinite-lived intangible assets are not amortized, but reviewed for impairment upon the occurrence of events or changes in circumstances that would reduce the fair value below its carrying amount. Goodwill is required to be tested for impairment at least annually. In

September 2011, the FASB issued ASU No. 2011-08, Intangibles – Goodwill and Other (Topic 350). ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. If it is determined that the fair value of a reporting unit is more likely than not to be less than its carrying value (including unrecognized intangible assets) then it is necessary to perform the second step of the goodwill impairment test. The second step of the goodwill impairment test is judgmental in nature and often involves the use of significant estimates and assumptions. Similarly, estimates and assumptions are used in determining the fair value of other intangible assets. These estimates and assumptions

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(1) Summary of Operations and Significant Accounting Policies  
(continued)**

could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. The Company performs internal valuation analyses and considers other market information that is publicly available. Estimates of fair value are primarily determined using discounted cash flows and market comparisons. These approaches use significant estimates and assumptions including projected future cash flows (including timing), discount rates reflecting the risk inherent in future cash flows, perpetual growth rates, determination of appropriate market comparables and the determination of whether a premium or discount should be applied to comparables. ASC 350-10 also requires that intangible assets with estimatable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with ASC 360-10-35, Accounting for Impairment or Disposal of Long-Lived Assets.

**(r) Deferred Rent**

The Company records rent expense on a straight-line basis over the term of the related lease. The difference between the rent expense recognized for financial reporting purposes and the actual payments made in accordance with the lease agreement is recognized as deferred rent liability on the Company's balance sheet.

**(s) Foreign Currency Translation**

Assets and liabilities in foreign functional currencies are translated at the exchange rate as of the balance sheet date. Translation adjustments are recorded as a separate component of stockholders' equity. Revenue, costs and expenses denominated in foreign functional currencies are translated at the weighted average exchange rate for the period. The translation adjustment of \$35, \$127 and \$34 for the years ended December 31, 2011, 2010 and 2009, respectively, is related to the Company's wholly-owned United Kingdom subsidiary. The functional currency of the Company's wholly-owned Israeli subsidiaries is the U.S. dollar.

**(t) Recently Issued Accounting Standards**

In December 2011, the FASB issued ASU No. 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities. This ASU is intended to provide enhanced disclosures that will enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities within the scope of this update. The amendments require enhanced disclosures by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either Section 210-20-45 or Section 815-10-45.



An entity is required to apply this amendment for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. ASU No. 2011-11 relates specifically to disclosures, it will not have an impact on the Company's consolidated financial statements.

In September 2011, the FASB issued ASU No. 2011-08, Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment. This ASU is intended to simplify how entities test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, Intangibles—Goodwill and Other. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. This update is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

annual or interim period have not yet been issued. The Company elected early adoption of this update and it had no impact on its consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. This ASU represents the converged guidance of the FASB and the IASB (the Boards) on fair value measurement. The collective efforts of the Boards and their staffs, reflected in ASU 2011-04, have resulted in common requirements for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning of the term fair value. The

Boards have concluded the common requirements will result in greater comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and IFRSs. The amendments to the FASB Accounting Standards Codification (Codification) in this ASU are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011. Early application by public entities is not permitted. The Company is currently assessing the impact of this update on its consolidated financial statements.

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

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties. Cash and cash equivalents, accounts receivable, security deposits and accounts payable carrying amounts approximate fair value because of the short maturity of these instruments.

**(v) Goodwill and Intangible Assets**

The changes in the carrying amount of goodwill for the year ended December 31, 2011 are as follows:

	Total	Business	Consumer
Balance as of December 31, 2010	\$ 24,015	\$ 15,991	\$ 8,024
Adjustments to goodwill:			
Contingent earnout payments	75	75	
Balance as of December 31, 2011	\$ 24,090	\$ 16,066	\$ 8,024

The changes in the carrying amount of goodwill for the year ended December 31, 2010 are as follows:

Total	Business	Consumer
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Balance as of December 31, 2009	\$ 23,920	\$ 15,896	\$ 8,024
Adjustments to goodwill:			
Contingent earnout payments	95	95	
Balance as of December 31, 2010	\$ 24,015	\$ 15,991	\$ 8,024

---

63

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(1) Summary of Operations and Significant Accounting Policies  
(continued)**

Intangible assets are summarized as follows (see Note 2):

**Acquired Intangible Assets**

	As of December 31, 2011		
	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization
Amortizing intangible assets:			
Technology	\$ 6,199	3.8 years	\$ 5,474
Customer contracts	2,400	3.0 years	2,400
Trade names	630	3.0 years	630
Non-compete agreements	410	1.2 years	410
Patents	475	11.0 years	105
Other	235	3.0 years	235
Total	\$ 10,349		\$ 9,254

	As of December 31, 2010		
	Gross Carrying Amount	Weighted Average Amortization Period	Accumulated Amortization
Amortizing intangible assets:			
Technology	\$ 6,199	3.8 years	\$ 4,489
Customer contracts	2,400	3.0 years	2,400
Trade names	630	3.0 years	630
Non-compete agreements	410	1.2 years	410
Patents	475	11.0 years	61
Other	235	3.0 years	235
Total	\$ 10,349		\$ 8,225

Amortization expense is calculated on a straight-line basis over the estimated useful life of the asset. Aggregate amortization expense for intangible assets was \$1,029, \$1,486 and \$1,973 for the years ended December 31, 2011, 2010 and 2009, respectively. For the years ended December 31, 2011 and 2010, a portion of this amortization is

included in cost of revenue. Estimated amortization expense for the next five years is: \$306 in 2012, \$306 in 2013, \$240 in 2014, \$43 in 2015, \$43 in 2016 and \$157 thereafter.

## **(2) Acquisitions**

### **Proficient Systems**

On July 18, 2006, the Company acquired Proficient Systems, Inc. ( Proficient ), a provider of hosted proactive chat solutions that help companies generate revenue on their web sites. This transaction was accounted for under the purchase method of accounting and, accordingly, the operating results of Proficient were included in the Company's consolidated results of operations from the date of acquisition. The acquisition added several U.K. based financial services customers and provided an innovative product marketing team. During the twelve months ended December 31, 2011, 2010 and 2009, the Company incurred additional costs related to the earn-out litigation in the amount of \$75, \$95, \$98, respectively, resulting in an increase in goodwill. See Legal Proceedings and Note 9 of our consolidated financial statements for additional information regarding the Proficient litigation.

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(2) Acquisitions (continued)**

Based on the achievement of certain revenue targets as of March 31, 2007, LivePerson was contingently required to issue up to an additional 2,050,000 shares of common stock. Based on these targets, the Company issued 1,127,985 shares of common stock valued at \$8,894, based on the quoted market price of the Company's common stock on the date the contingency was resolved, and made a cash payment of \$20 related to this contingency. At March 31, 2007, the value of these shares has been allocated to goodwill with a corresponding increase in equity. In accordance with the purchase agreement, the earn-out consideration was subject to review by Proficient's Shareholders' Representative. On July 31, 2007, the Company was served with a complaint filed in the United States District Court for the Southern District of New York by the Shareholders' Representative of Proficient (Plaintiff). The complaint filed by the Shareholders' Representative sought certain documentation relating to calculation of the earn-out consideration, and demanded payment of damages on the grounds that substantially all of the remaining contingently issuable earn-out shares should have been paid. The Company believes the claims are without merit. The case proceeded to trial, which ended on November 4, 2010. Post-trial filings were made on November 19, 2010. The Court has still not issued its ruling in this case. In the event that the Court finds in whole or in part for Plaintiff, the Company would be required to pay monetary damages in the amount held by the Court to have been underpaid in the earn-out. The Company is presently unable to reasonably estimate the amount of actual damages, if any, that will be awarded by the Court. If the Court were to find in favor of Plaintiff on every claim at issue in the litigation, the maximum potential damages award would be approximately \$6,000. Should the Company be required to pay any damages award, the associated expense would be allocated to goodwill in connection with Proficient acquisition.

**NuConomy Ltd.**

On April 13, 2010, the Company acquired all of the outstanding shares of NuConomy Ltd. (NuConomy), an Israeli-based development-stage company whose web analytics and optimization platform is intended to help companies better assess and understand website and social marketing performance, in exchange for aggregate cash consideration of \$800. This transaction was accounted for as an asset purchase. The net asset was allocated to Intangibles, net.

**(3) Balance Sheet Components**

**Property and Equipment**

Property and equipment is summarized as follows:

December 31,  
2011      2010

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Computer equipment and software	\$ 30,182	\$ 25,002
Furniture, equipment and building improvements	4,356	1,856
	34,538	26,858
Less accumulated depreciation	20,659	14,096
Total	\$ 13,879	\$ 12,762

65

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TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(3) Balance Sheet Components (continued)****Accrued Expenses**

Accrued expenses consist of the following:

	December 31,	
	2011	2010
Payroll and other employee related costs	\$ 6,435	\$ 6,973
Professional services, consulting and other vendor fees	4,686	4,211
Sales commissions	446	565
Other	452	362
Total	\$ 12,019	\$ 12,111

**(4) Capitalization**

On May 14, 2010, our Board of Directors approved a stock repurchase program through June 30, 2012.

Under the stock repurchase program, the Company is authorized to repurchase shares of its common stock, in the open market or privately negotiated transactions, at times and prices considered appropriate by the Board of Directors depending upon prevailing market conditions and other corporate considerations, up to an aggregate purchase price of \$10,000. As of December 31, 2010, the Company had repurchased 534,496 shares of its common stock for an aggregate cost of approximately \$3,600. No shares were repurchased under this program during 2011.

**(5) Stock Options and Employee Stock Purchase Plan**

During 1998, the Company established the Stock Option and Restricted Stock Purchase Plan (the 1998 Plan ). Under the 1998 Plan, the Board of Directors could issue incentive stock options or nonqualified stock options to purchase up to 5,850,000 shares of common stock. The 2000 Stock Incentive Plan (the 2000 Plan ) succeeded the 1998 Plan. Under the 2000 Plan, the options which had been outstanding under the 1998 Plan were incorporated in the 2000 Plan increasing the number of shares available for issuance under the plan by approximately 4,150,000, thereby reserving for issuance 10,000,000 shares of common stock in the aggregate.

The Company established the 2009 Stock Incentive Plan (as amended and restated, the 2009 Plan ) as a successor to the 2000 Plan. Under the 2009 Plan, the options which had been outstanding under the 2000 Plan were incorporated into the 2009 Plan and the Company increased the number of shares available for issuance under the plan by 6,000,000, thereby reserving for issuance 19,567,744 shares of common stock in the aggregate. Options to acquire common stock granted thereunder have ten-year terms. As of December 31, 2011, approximately 12,810,000 shares of



common stock were reserved for issuance under the 2009 Plan (taking into account all option exercises through December 31, 2011). As of December 31, 2011, there was approximately \$26,491 of total unrecognized compensation cost related to nonvested share-based compensation arrangements. That cost is expected to be recognized over a weighted average period of approximately 2.2 years.

In March 2000, the Company adopted the 2000 Employee Stock Purchase Plan with 450,000 shares of common stock initially reserved for issuance (the 2000 ESPP ). The 2000 ESPP expired on its terms on the last day of April 2010.

In June 2010, our stockholders approved the 2010 Employee Stock Purchase Plan with 1,000,000 shares of common stock initially reserved for issuance. As of December 31, 2011, approximately 933,000 shares of common stock were reserved for issuance under the Employee Stock Purchase Plan (taking into account all share purchases through December 31, 2011).

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(5) Stock Options and Employee Stock Purchase Plan  
(continued)**

A summary of the Company's stock option activity and weighted average exercise prices follows:

	Options	Weighted Average Exercise Price
Options outstanding at December 31, 2008	9,939,045	\$ 3.67
Options granted	1,960,500	2.66
Options exercised	(2,094,888)	2.06
Options cancelled	(1,092,849)	3.65
Options outstanding at December 31, 2009	8,711,808	3.82
Options granted	3,809,380	7.13
Options exercised	(2,843,547)	4.10
Options cancelled	(860,881)	5.09
Options outstanding at December 31, 2010	8,816,760	5.04
Options granted	3,642,600	12.24
Options exercised	(2,278,451)	4.28
Options cancelled	(1,337,496)	7.03
Options outstanding at December 31, 2011	8,843,413	\$ 7.91
Options exercisable at December 31, 2009	4,463,915	\$ 4.03
Options exercisable at December 31, 2010	3,097,748	\$ 3.93
Options exercisable at December 31, 2011	2,805,399	\$ 4.63

The total value of stock options exercised during the years ended December 31, 2011, 2010 and 2009 was approximately \$17,174, \$11,050 and \$6,204, respectively. The total intrinsic value of options exercisable at December 31, 2011, 2010 and 2009 was approximately \$21,890, \$22,491 and \$12,799, respectively. The total intrinsic value of nonvested options at December 31, 2011, 2010 and 2009 was approximately \$19,839, \$32,420 and \$14,318, respectively. The total intrinsic value of all outstanding options at December 31, 2011, 2010 and 2009 was approximately \$41,729, \$54,911 and \$27,117, respectively.

A summary of the status of the Company's nonvested options as of December 31, 2009, and changes during the years ended December 31, 2010 and 2011 is as follows:

Shares	Weighted
--------	----------

		Average Grant-Date Fair Value
Nonvested Shares at January 1, 2010	4,247,893	\$ 2.13
Granted	3,809,380	3.89
Vested	(1,521,951)	2.41
Cancelled	(816,310 )	2.83
Nonvested Shares at December 31, 2010	5,719,012	\$ 3.13
Nonvested Shares at January 1, 2011	5,719,012	\$ 3.13
Granted	3,642,600	6.47
Vested	(1,967,639)	3.00
Cancelled	(1,355,959)	3.83
Nonvested Shares at December 31, 2011	6,038,014	\$ 5.04

67

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(6) Valuation and Qualifying Accounts**

	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions / Write-Offs	Balance at End of Period
For the year ended December 31, 2011 Allowance for doubtful accounts	\$ 561	\$ 290	\$ (163 )	\$ 688
For the year ended December 31, 2010 Allowance for doubtful accounts	\$ 395	\$ 166	\$	\$ 561
For the year ended December 31, 2009 Allowance for doubtful accounts	\$ 340	\$ 68	\$ (13 )	\$ 395

**(7) Income Taxes**

Income taxes are accounted for under the asset and liability method. 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. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are expected to become deductible.

Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. The Company includes interest accrued on the underpayment of income taxes in interest expense and penalties, if any, related to unrecognized tax benefits in general and administrative expenses.

Under Section 382 of the Internal Revenue Code of 1986, as amended, the Company's use of its federal net operating loss ( NOL ) carryforwards may be limited if the Company experiences an ownership change, as defined in Section 382. Such an annual limitation could result in the expiration of the net operating loss carryforwards before utilization.

As of December 31, 2011, the Company had approximately \$7,279 of federal NOL carryforwards available to offset future taxable income. Included in this amount is \$6,124 of federal NOL carryovers from the Company's acquisition of Proficient. These carryforwards expire in various years through 2027.

The domestic and foreign components of income before provision for income taxes consist of the following:

	Year Ended December 31,		
	2011	2010	2009
United States	\$ 16,495	\$ 12,478	\$ 10,972
Foreign	2,655	1,855	1,828
	\$ 19,150	\$ 14,333	\$ 12,800

No additional provision has been made for U.S. income taxes on the undistributed earnings of its Israeli subsidiary, LivePerson Ltd (formerly HumanClick Ltd.), as such earnings have been taxed in the U.S. and accumulated earnings of the Company's other foreign subsidiaries are immaterial through December 31, 2011.

TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(7) Income Taxes (continued)**

The provision for income taxes consists of the following:

	Year Ended December 31,		
	2011	2010	2009
Current income taxes:			
U.S. Federal	\$ 5,839	\$ 3,554	\$ 1,418
State and local	600	473	516
Foreign	444	215	238
Total current income taxes	6,883	4,242	2,172
Deferred income taxes:			
U.S. Federal	232	694	2,719
State and local	(38 )	(60 )	21
Foreign	35	198	125
Total deferred income taxes	229	832	2,865
Total income taxes	\$ 7,112	\$ 5,074	\$ 5,037

The difference between the total income taxes computed at the federal statutory rate and the benefit from income taxes consists of the following:

	Year Ended December 31,		
	2011	2010	2009
Federal Statutory Rate	34.48 %	34.30 %	34.00 %
State taxes, net of federal benefit	2.56 %	2.27 %	2.80 %
Non-deductible expenses ISO	0.47 %	(0.88 )%	2.19 %
Non-deductible expenses Other	0.51 %	0.43 %	0.26 %
Foreign taxes	(0.13 )%	(0.08 )%	(0.44 )%
Other	(0.76 )%	(0.64 )%	0.54 %
Total provision	37.13 %	35.40 %	39.35 %

The effects of temporary differences and tax loss carryforwards that give rise to significant portions of federal deferred tax assets and deferred tax liabilities at December 31, 2011 and 2010 are presented below:

	2011	2010
Deferred tax assets:		
Net operating loss carryforwards	\$ 2,504	\$ 2,720
Accounts payable and accrued expenses	424	317

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Non-cash compensation	2,582	2,177
Goodwill and intangibles amortization	1,462	1,632
Allowance for doubtful accounts	260	208
Net deferred tax assets	7,232	7,054
Deferred tax liabilities:		
Plant and equipment	(2,061 )	(1,443 )
Intangibles related to the Kasamba acquisition		(206 )
Total deferred tax liabilities	(2,061 )	(1,649 )
Net deferred assets	\$ 5,171	\$ 5,405

69

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TABLE OF CONTENTS**LIVEPERSON, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)****(8) Commitments and Contingencies**

The Company leases facilities and certain equipment under agreements accounted for as operating leases. These leases generally require the Company to pay all executory costs such as maintenance and insurance. Rental expense for operating leases for the years ended December 31, 2011, 2010 and 2009 was approximately \$6,615, \$6,428 and \$4,855, respectively.

Future minimum lease payments under non-cancelable operating leases (with an initial or remaining lease terms in excess of one year) are as follows:

Year ending December 31,	Operating Leases
2012	\$ 7,126
2013	4,427
2014	2,766
2015	2,205
2016	570
Thereafter	2,002
Total minimum lease payments	\$ 19,096

**Capital Expenditures**

During 2007, the Company began to build a collocation facility in the eastern U.S. to host the LivePerson and Consumer services. During 2010, the Company began to build additional collocation facilities in Europe to host the LivePerson and Consumer services. Through December 31, 2011, the Company spent approximately \$21,350 for servers, network components and related hardware and software. This amount is included in Assets Property and equipment, net on our December 31, 2011 balance sheet. Though the Company expects to incur additional costs in 2012 related to the continued build-out of our collocation facilities and similar backup facilities to support disaster recovery capabilities in the U.S. and U.K., its total capital expenditures are not currently expected to exceed \$10,000 in 2012. The Company anticipates that our current cash and cash equivalents and cash from operations will be sufficient to complete the build-out.

**Employee Benefit Plans**

The Company has a 401(k) defined contribution plan covering all eligible employees. The Company provides for employer matching contributions equal to 50% of employee contributions, up to the lesser of 5% of eligible compensation or \$6. Matching contributions are deposited in to the employees 401(k) account and are subject to 5 year graded vesting. Salaries and related expenses include \$545 and \$436 of employer matching contributions for the



years ended December 31, 2011 and 2010, respectively.

## **Indemnifications**

The Company enters into service and license agreements in its ordinary course of business. Pursuant to some of these agreements, the Company agrees to indemnify certain customers from and against certain types of claims and losses suffered or incurred by them as a result of using the Company's products.

The Company also has agreements whereby its executive officers and directors are indemnified for certain events or occurrences while the officer or director is, or was serving, at the Company's request in such capacity. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has a directors and officers insurance policy that reduces its exposure and enables the Company to recover a portion of any future amounts paid. As a result of its insurance policy coverage, the Company believes the estimated fair value of these indemnification agreements is minimal. Currently, the Company has no liabilities recorded for these agreements as of December 31, 2011.

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(9) Legal Matters**

On July 31, 2007, the Company was served with a complaint filed in the United States District Court for the Southern District of New York by the Shareholders Representative of Proficient Systems, Inc. In connection with the July 2006 acquisition of Proficient, the Company was contingently required to issue up to 2,050,000 shares of common stock based on the terms of an earn-out provision in the merger agreement. In accordance with the terms of the earn-out provision, the Company issued 1,127,985 shares of LivePerson common stock in the second quarter of 2007 to the former shareholders of Proficient. The amended complaint filed by the Shareholders Representative, or Plaintiff, on May 12, 2009 alleges that the Company breached the merger agreement by failing to properly account for net annualized revenue, and demands payment of damages on the grounds that substantially all of the remaining contingently issuable earn-out shares should have been paid. The Company believes the claims are without merit. The case proceeded to trial, which ended on November 4, 2010. Post-trial filings were made on November 19, 2010. The Court has still not issued its ruling in this case. In the event that the Court finds in whole or in part for Plaintiff, the Company would be required to pay monetary damages in the amount held by the Court to have been underpaid in the earn-out. The Company is presently unable to reasonably estimate the amount of actual damages, if any, that will be awarded by the Court. If the Court were to find in favor of Plaintiff on every claim at issue in the litigation, the maximum potential damages award would be approximately \$6,000. Should the Company be required to pay any damages award, the associated payment would be allocated to goodwill in connection with Proficient acquisition.

On November 3, 2010, Gemini IP LLC filed an amended complaint in a suit pending in the United States District Court for the Eastern District of Texas, adding patent infringement allegations against the Company and various other defendants, including LANDesk Software, Inc., Saba Software, Inc., Genesys S.A. d/b/a Genesys Conferencing, Genesys Conferencing, Inc., Avaya Inc., Best Buy Co., Inc., Bomgar Corporation, ConnectWise, Inc., Elsinore Technologies Inc., GFI Software Ltd., GFI USA, Inc., GFI Software Development, Ltd., LogMeIn, Inc., N-able Technologies Incorporated, NTR Global, Venti Solutions, LLC, Zoho Corporation, Zenith Infotech Ltd., International Business Machines Corp., Samsung Electronics America, Inc., Samsung Electronics Co., Ltd., Samsung Telecommunications America, LLC, AT&T, Inc., Sony Corporation, and Sony Corporation of America. On August 26, 2011, Gemini and LivePerson jointly filed a motion asking the Court to dismiss all claims with prejudice. The Court has not yet ruled on that motion.

On June 15, 2011, the Company filed suit against Lodsys, LLC, in the United States District Court for the Northern District of Illinois, seeking a declaratory judgment that the Company's products do not infringe four patents which Lodsys had previously asserted were infringed by the Company's customers, as well as a declaratory judgment that those four patents are invalid. On July 5, 2011, Lodsys moved to dismiss the Illinois case based on lacking personal jurisdiction, and also countersued the Company and other plaintiffs in similarly-situated declaratory judgment actions, including DriveTime Automotive Group, Inc., ESET, LLC, ForeSee Results, LLC, OpinionLab, Inc., and The New York Times Company, in the United States District Court for the Eastern District of Texas. In the Texas case, Lodsys alleges that the Company infringes one of the patents involved in the co-pending Illinois case, and seeks damages for past infringement, and an injunction against future infringement. The Company believes Lodsys's claims are without

merit. On October 25, 2011 the Court granted the parties' joint motion to transfer the cases from Illinois to the Eastern District of Wisconsin, and all pending motions were withdrawn, including Lodsys's pending motion to dismiss. On January 6, 2012 Lodsys filed a motion to dismiss the Wisconsin case, or, in the alternative, for a more definite statement. On January 27, 2012 the Company filed an amended complaint in the Wisconsin case. On February 10, 2012 Lodsys filed a motion to dismiss the Wisconsin case, or, in the alternative, to transfer or stay. On January 23, 2012, the Company moved to dismiss the Texas case in favor of the first-filed Wisconsin case. On February 9, 2012 Lodsys filed its opposition to the Company's motion, and the Company filed its reply on February 21, 2012. This motion is fully briefed.

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(9) Legal Matters (continued)**

On February 7, 2012, the Company filed suit against Pragmatus Telecom LLC in the District of Delaware, seeking a declaratory judgment that the Company's products do not infringe three patents owned by Pragmatus which Pragmatus had previously asserted were infringed by certain of the Company's customers, as well as a declaratory judgment that those four patents are invalid.

Although the Company currently does not expect that the outcome in any of these matters, individually or collectively, will have a material adverse effect on its financial condition or results of operations, litigation is inherently unpredictable. Therefore, judgments could be rendered or settlements entered, that could adversely affect the Company's operating results or cash flows in a particular period. The Company routinely assesses all of its litigation and threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss in situations where it assesses the likelihood of loss as probable.

From time to time, the Company is involved in other legal proceedings arising in the ordinary course of its business, which may arise from direct legal claims brought by or against the Company, or from claims brought against the Company's customers for which the Company has a contractual indemnification obligation.

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**(10) Unaudited Supplementary Financial Information    Quarterly  
Results of Operations**

The following table sets forth, for the periods indicated, the Company's financial information for the eight most recent quarters ended December 31, 2011. In the Company's opinion, this unaudited information has been prepared on a basis consistent with the annual consolidated financial statements and includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the unaudited information for the periods presented. This information should be read in conjunction with the consolidated financial statements, including the related notes, included herein.

TABLE OF CONTENTS

**LIVEPERSON, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Share and per Share Data)**

**Item 9. Changes in and Disagreements With Accountants on  
Accounting and Financial Disclosure**

Not Applicable.

**Item 9A. Controls and Procedures**

**Management's Annual Report on Internal Control over Financial  
Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as that term is defined in Rule 13a-15(f) promulgated under the Exchange Act. Our internal control system is designed to provide reasonable assurance to our management and Board of Directors regarding the preparation and fair presentation of published financial statements. Our management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our internal control over financial reporting as of December 31, 2011 based on the framework established in Internal Control - Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on management's evaluation described above, our management concluded that our internal control over financial reporting was effective as of December 31, 2011.

The effectiveness of our internal control over financial reporting as of December 31, 2011 has been audited by BDO USA, LLP, an independent registered public accounting firm. Their attestation is included herein.

**Limitations of the Effectiveness of Internal Control**

A control system, no matter how well conceived and operated, can only provide reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of the inherent limitations of any internal control system, no evaluation of controls can provide absolute assurance that all control issues, if any, have been detected.

**Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2011 identified in connection with the evaluation thereof by our management, including the Chief Executive Officer and Chief Financial Officer, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Evaluation of Disclosure Controls and Procedures

Our management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures, as that term is defined in Rule 13a-15(e) promulgated under the Exchange Act, as of December 31, 2011. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2011 to ensure that the information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms, and to ensure that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

74

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TABLE OF CONTENTS

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
LivePerson, Inc.  
New York, NY

We have audited LivePerson, Inc.'s internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). LivePerson, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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

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

In our opinion, LivePerson, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of LivePerson, Inc.'s as of December 31, 2011 and 2010, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2011 and our report dated March 13, 2012 expressed an unqualified opinion



thereon.

/s/ BDO USA, LLP

New York, New York  
March 13, 2012

75

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TABLE OF CONTENTS

**Item 9B. Other Information**

None.

**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance**

The information required by this Item 10 is incorporated by reference to the sections captioned to Matters to be Considered at Annual Meeting Election of Directors, Executive Officers, Board Committees and Meetings Audit Committee, Codes of Conduct and Corporate Governance Documents and Section 16(a) Beneficial Ownership Reporting Compliance in the definitive proxy statement for our 2012 Annual Meeting of Stockholders.

There have been no changes to the procedures by which stockholders may recommend nominees to our Board of Directors since our last disclosure of such procedures, which appeared in the definitive proxy statement for our 2011 Annual Meeting of Stockholders.

We have adopted a Code of Ethics that applies to our Chief Executive Officer, who is our principal executive officer, and other senior financial officers. Our Code of Ethics is available at: [www.liveperson.com](http://www.liveperson.com) under Investor Relations / Corporate Governance. *The Company's web site address provided above is not intended to function as a hyperlink, and the information on the Company's web site is not and should not be considered part of this Annual Report on Form 10-K and is not incorporated by reference herein.* The Company will post on this website any amendments to our Code of Ethics.

**Item 11. Executive Compensation**

The information required by this Item 11 is incorporated by reference to the sections captioned Compensation Discussion and Analysis, Compensation Committee Report (which information shall be deemed furnished in this Annual Report on Form 10-K), Executive and Director Compensation and Compensation Committee Interlocks and Insider Participation in the definitive proxy statement for our 2012 Annual Meeting of Stockholders.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this Item 12 is incorporated by reference to the sections captioned Ownership of Securities and Potential Payments Upon Termination or Change-in-Control in the definitive proxy statement for our 2012 Annual Meeting of Stockholders.

The following table provides certain information regarding the common stock authorized for issuance under our equity compensation plans, as of December 31, 2011:

Plan Category

	Number of Securities to Be Issued Upon Exercise of Outstanding Options, (a)	Weighted-Average Price of Outstanding Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans <sup>(2)</sup> (c)
Equity compensation plans approved by stockholders <sup>(1)</sup>	8,843,413	\$ 7.91	3,966,822
Equity compensation plans not approved by stockholders			
Total	8,843,413	\$ 7.91	3,966,822

(1) Our equity compensation plans which were approved by our stockholders are the 2009 Stock Incentive Plan and the 2010 Employee Stock Purchase Plan.

(2) Excludes securities reflected in column (a). Also see Note 5 to our consolidated financial statements.

76

TABLE OF CONTENTS

## **Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this Item 13 is incorporated by reference to the sections captioned Certain Relationships and Related Transactions and Director Independence in the definitive proxy statement for our 2012 Annual Meeting of Stockholders.

## **Item 14. Principal Accountant Fees and Services**

The information required by this Item 14 is incorporated by reference to the section captioned Independent Registered Public Accounting Firm Fees and Pre-Approval Policies and Procedures in the definitive proxy statement for our 2012 Annual Meeting of Stockholders.

77

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TABLE OF CONTENTS

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

The following documents are filed as part of this Annual Report on Form 10-K:

1. Financial Statements.  
Incorporated by reference to the index of consolidated financial statements included in Item 8 of this Annual Report on Form 10-K.
2. Financial Statement Schedules.  
None.
3. Exhibits.  
Incorporated by reference to the Exhibit Index immediately preceding the exhibits attached to this Annual Report on Form 10-K.

TABLE OF CONTENTS

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on March 13, 2012.

**LIVEPERSON, INC.**

By:

/s/ Robert P. LoCascio

Name: Robert P. LoCascio

Title: Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on March 13, 2012.

Signature	Title(s)
/s/ Robert P. LoCascio Robert P. LoCascio	Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)
/s/ Daniel R. Murphy Daniel R. Murphy	Chief Financial Officer (Principal Financial and Accounting Officer)
/s/ Peter Block Peter Block	Director
/s/ Kevin C. Lavan Kevin C. Lavan	Director
/s/ David Vaskevitch David Vaskevitch	Director
/s/ William G. Wesemann William G. Wesemann	Director

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TABLE OF CONTENTS

**EXHIBIT INDEX**

Number	Description
2.1	Agreement and Plan of Merger, dated as of June 22, 2006, among LivePerson, Inc., Soho Acquisition Corp., Proficient Systems, Inc. and Gregg Freishtat as Shareholders Representative (incorporated by reference to the identically numbered exhibit in the Current Report on Form 8-K filed on June 22, 2006)
3.1	Fourth Amended and Restated Certificate of Incorporation (incorporated by reference to the identically-numbered exhibit to LivePerson's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 and filed March 30, 2001 (the 2000 Form 10-K))
3.2	Second Amended and Restated Bylaws, as amended (incorporated by reference to the identically-numbered exhibit to the 2000 Form 10-K)
4.1	Specimen common stock certificate (incorporated by reference to the identically-numbered exhibit to LivePerson's Registration Statement on Form S-1, as amended (Registration No. 333-96689) (Registration No. 333-96689))
4.2	Second Amended and Restated Registration Rights Agreement, dated as of January 27, 2000, by and among LivePerson, the several persons and entities named on the signature pages thereto as Investors, and Robert LoCascio (incorporated by reference to the identically-numbered exhibit to Registration No. 333-96689)
10.1*	2009 Stock Incentive Plan (incorporated by reference to Exhibit 99.1 to LivePerson's Registration Statement on Form S-8 filed on June 9, 2009) and Forms of Grant Agreements under the 2009 Stock Incentive Plan (incorporated by reference to Exhibit 10.1 to LivePerson's Quarterly Report on Form 10-Q filed on May 6, 2011)
10.2*	LivePerson, Inc. 2010 Employee Stock Purchase Plan (incorporated by reference to Exhibit 99.1 to the LivePerson's Registration Statement on Form S-8 filed on August 19, 2010)
10.3*	Employment Agreement between LivePerson and Robert P. LoCascio, dated as of January 1, 1999 (incorporated by reference to Exhibit 10.1 to Registration No. 333-96689)
10.4(a)*	Employment Agreement between LivePerson and Timothy E. Bixby, dated as of June 23, 1999 (incorporated by reference to Exhibit 10.3 to Registration No. 333-96689)
10.4(b)*	Modification to Employment Agreement between LivePerson and Timothy E. Bixby, dated as of April 1, 2003 (incorporated by reference to Exhibit 10.2.1 to LivePerson's Quarterly Report on Form 10-Q for the quarter ended June 30, 2003 and filed August 13, 2003)
10.4(c)*	Separation Agreement and General Release between LivePerson and Timothy E. Bixby, dated as of November 2, 2010 (incorporated by reference to Exhibit 10.4(c) to LivePerson's Annual Report on Form 10-K for the year ended December 31, 2010 and filed March 15, 2011)
10.5*	Agreement between LivePerson and Dan Murphy, dated as of March 27, 2011
10.6*	Form of Indemnification Agreement entered into with Executive Officers and Directors of LivePerson
10.7*	Agreement between LivePerson and Eli Campo, dated as of December 22, 2006
10.8*	Agreement between LivePerson and Monica L. Greenberg, dated as of October 25, 2006
10.9*	Agreement between LivePerson and Michael Kovach, dated as of November 6, 2009
21.1	Subsidiaries
23.1	Consent of BDO USA, LLP
31.1	Certification by Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	

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Certification by Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1\*\*

Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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TABLE OF CONTENTS

Number	Description
32.2**	Certification by Chief 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 Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

\* Management contract or compensatory plan or arrangement

The certifications attached as Exhibit 32.1 and Exhibit 32.2 accompany the Annual Report on Form 10-K pursuant \*\*to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

Pursuant to applicable securities laws and regulations, the Registrant is deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and is not subject to liability under any anti-fraud provisions of the federal securities laws as long as the Registrant has made a good faith attempt to comply with the submission requirements and promptly amends the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. These interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections.

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