

VERISIGN INC/CA  
Form 10-Q  
October 25, 2018

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 000-23593

VERISIGN, INC.

(Exact name of registrant as specified in its charter)

Delaware 94-3221585

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

12061 Bluemont Way, Reston, Virginia 20190

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (703) 948-3200

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES  NO

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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

Class Shares Outstanding as of October 19, 2018

Common stock, \$.001 par value 120,888,417



## TABLE OF CONTENTS

|  | Page      |
|--|-----------|
| <u>PART I—FINANCIAL INFORMATION</u>  |           |
| <u>Item 1. Financial Statements</u>  | <u>3</u>  |
| <u>Condensed Consolidated Balance Sheets as of September 30, 2018 and December 31, 2017</u>                                      | <u>3</u>  |
| <u>Condensed Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2018 and 2017</u> | <u>4</u>  |
| <u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2018 and 2017</u>                     | <u>5</u>  |
| <u>Notes to Condensed Consolidated Financial Statements</u>  | <u>6</u>  |
| <u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>                             | <u>13</u> |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>  | <u>21</u> |
| <u>Item 4. Controls and Procedures</u>   | <u>21</u> |
| <u>PART II—OTHER INFORMATION</u>   |           |
| <u>Item 1. Legal Proceedings</u>   | <u>22</u> |
| <u>Item 1A. Risk Factors</u>   | <u>22</u> |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>   | <u>34</u> |
| <u>Item 5. Other Information</u>   | <u>34</u> |
| <u>Item 6. Exhibits</u>  | <u>35</u> |
| <u>Signatures</u>  | <u>36</u> |

Table of Contents

## PART I—FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## VERISIGN, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except par value)

(Unaudited)

|   | September 30,<br>2018 | December 31,<br>2017 |
|---|-----------------------|----------------------|
| <b>ASSETS</b>   |                       |                      |
| Current assets:   |                       |                      |
| Cash and cash equivalents   | \$ 231,571            | \$ 465,851           |
| Marketable securities   | 947,395               | 1,948,900            |
| Other current assets  | 57,016                | 31,402               |
| Total current assets  | 1,235,982             | 2,446,153            |
| Property and equipment, net   | 256,269               | 263,513              |
| Goodwill  | 52,527                | 52,527               |
| Deferred tax assets   | 167,772               | 15,392               |
| Deposits to acquire intangible assets   | 145,000               | 145,000              |
| Other long-term assets  | 27,078                | 18,603               |
| Total long-term assets  | 648,646               | 495,035              |
| Total assets  | \$ 1,884,628          | \$ 2,941,188         |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>  |                       |                      |
| Current liabilities:  |                       |                      |
| Accounts payable and accrued liabilities  | \$ 176,121            | \$ 219,603           |
| Deferred revenues   | 737,515               | 713,309              |
| Subordinated convertible debentures   | —                     | 627,616              |
| Total current liabilities   | 913,636               | 1,560,528            |
| Long-term deferred revenues   | 286,735               | 286,097              |
| Senior notes  | 1,784,417             | 1,782,529            |
| Deferred tax liabilities  | —                     | 444,108              |
| Other long-term tax liabilities   | 300,941               | 128,197              |
| Total long-term liabilities   | 2,372,093             | 2,640,931            |
| Total liabilities   | 3,285,729             | 4,201,459            |
| Commitments and contingencies   |                       |                      |
| Stockholders' deficit:  |                       |                      |
| Preferred stock—par value \$.001 per share; Authorized shares: 5,000; Issued and outstanding shares: none   | —                     | —                    |
| Common stock—par value \$.001 per share; Authorized shares: 1,000,000; Issued shares: 352,260 at September 30, 2018 and 325,218 at December 31, 2017; Outstanding shares: 121,158 at September 30, 2018 and 97,591 at December 31, 2017 | 352                   | 325                  |
| Additional paid-in capital  | 15,873,534            | 16,437,135           |
| Accumulated deficit   | (17,271,984 )         | (17,694,790 )        |
| Accumulated other comprehensive loss  | (3,003 )              | (2,941 )             |
| Total stockholders' deficit   | (1,401,101 )          | (1,260,271 )         |
| Total liabilities and stockholders' deficit   | \$ 1,884,628          | \$ 2,941,188         |

See accompanying Notes to Condensed Consolidated Financial Statements.



Table of Contents

VERISIGN, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share data)

(Unaudited)

|   | Three Months Ended |           | Nine Months Ended |            |
|---|--------------------|-----------|-------------------|------------|
|   | September 30,      |           | September 30,     |            |
|   | 2018               | 2017      | 2018              | 2017       |
| Revenues                                  | \$305,777          | \$292,428 | \$907,517         | \$869,594  |
| Costs and expenses:                       |                    |           |                   |            |
| Cost of revenues                          | 48,249             | 47,333    | 143,766           | 145,646    |
| Sales and marketing                       | 13,868             | 18,667    | 47,712            | 56,463     |
| Research and development                  | 13,712             | 12,715    | 42,842            | 39,569     |
| General and administrative                | 34,951             | 32,654    | 99,771            | 96,626     |
| Total costs and expenses                  | 110,780            | 111,369   | 334,091           | 338,304    |
| Operating income                          | 194,997            | 181,059   | 573,426           | 531,290    |
| Interest expense                          | (22,631 )          | (37,756 ) | (92,211 )         | (95,869 )  |
| Non-operating income, net                 | 5,935              | 6,241     | 14,399            | 21,544     |
| Income before income taxes                | 178,301            | 149,544   | 495,614           | 456,965    |
| Income tax expense                        | (40,621 )          | (34,645 ) | (95,320 )         | (102,554 ) |
| Net income                                | 137,680            | 114,899   | 400,294           | 354,411    |
| Other comprehensive income                | (322 )             | (264 )    | (62 )             | 299        |
| Comprehensive income                      | \$137,358          | \$114,635 | \$400,232         | \$354,710  |
| Earnings per share:                       |                    |           |                   |            |
| Basic                                     | \$1.13             | \$1.15    | \$3.60            | \$3.51     |
| Diluted                                   | \$1.13             | \$0.93    | \$3.25            | \$2.85     |
| Shares used to compute earnings per share |                    |           |                   |            |
| Basic                                     | 121,682            | 99,614    | 111,046           | 101,036    |
| Diluted                                   | 122,261            | 124,074   | 123,079           | 124,162    |

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

VERISIGN, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (In thousands)  
 (Unaudited)

|   | Nine Months Ended<br>September 30, |              |
|---|------------------------------------|--------------|
|   | 2018                               | 2017         |
| Cash flows from operating activities:   |                                    |              |
| Net income  | \$400,294                          | \$354,411    |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                    |              |
| Depreciation of property and equipment  | 36,450                             | 37,665       |
| Stock-based compensation  | 41,406                             | 40,043       |
| Loss on debt extinguishment   | 6,554                              | —            |
| Gain on sale of business  | —                                  | (10,421 )    |
| Amortization of debt discount and issuance costs                                  | 6,428                              | 10,827       |
| Amortization of discount on investments in debt securities                        | (12,746 )                          | (9,092 )     |
| Other, net  | 1,770                              | 150          |
| Changes in operating assets and liabilities:                                      |                                    |              |
| Other assets  | (6,917 )                           | 4,566        |
| Accounts payable and accrued liabilities  | (29,478 )                          | (24,756 )    |
| Deferred revenues   | 24,844                             | 32,790       |
| Net deferred income taxes and other long-term tax liabilities                     | 10,662                             | 67,385       |
| Net cash provided by operating activities   | 479,267                            | 503,568      |
| Cash flows from investing activities:   |                                    |              |
| Proceeds from maturities and sales of marketable securities                       | 3,081,702                          | 3,895,675    |
| Purchases of marketable securities  | (2,067,498 )                       | (4,398,787 ) |
| Purchases of property and equipment   | (29,597 )                          | (40,609 )    |
| Other investing activities  | (160 )                             | 11,748       |
| Net cash provided by (used in) investing activities                               | 984,447                            | (531,973 )   |
| Cash flows from financing activities:   |                                    |              |
| Repayment of principal on subordinated convertible debentures                     | (1,250,009 )                       | —            |
| Proceeds from employee stock purchase plan  | 12,836                             | 12,915       |
| Repurchases of common stock   | (459,803 )                         | (474,290 )   |
| Proceeds from borrowings, net of issuance costs                                   | —                                  | 543,185      |
| Net cash (used in) provided by financing activities                               | (1,696,976 )                       | 81,810       |
| Effect of exchange rate changes on cash, cash equivalents, and restricted cash    | (985 )                             | 1,118        |
| Net (decrease) increase in cash, cash equivalents, and restricted cash            | (234,247 )                         | 54,523       |
| Cash, cash equivalents, and restricted cash at beginning of period                | 475,139                            | 241,581      |
| Cash, cash equivalents, and restricted cash at end of period                      | \$240,892                          | \$296,104    |
| Supplemental cash flow disclosures:   |                                    |              |
| Cash paid for interest  | \$87,184                           | \$86,622     |
| Cash paid for income taxes, net of refunds received                               | \$84,433                           | \$22,717     |
| See accompanying Notes to Condensed Consolidated Financial Statements.            |                                    |              |

Table of Contents

VERISIGN, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

Interim Financial Statements

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared by VeriSign, Inc. (“Verisign” or the “Company”) in accordance with the instructions to Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and, therefore, do not include all information and notes normally provided in audited financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and other adjustments) considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of, nor comparable to, the results of operations for any other interim period or for a full fiscal year. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and related notes contained in Verisign’s fiscal 2017 Annual Report on Form 10-K (the “2017 Form 10-K”) filed with the SEC on February 16, 2018.

Reclassifications

Certain reclassifications have been made to prior period amounts to conform to current period presentation. Such reclassifications have no effect on net income as previously reported.

Adoption of New Accounting Standards

Effective January 1, 2018, the Company adopted Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers, and several related amendments, issued by the Financial Accounting Standards Board (“FASB”). ASU 2014-09 replaces the previous numerous and disparate revenue recognition guidance, and provides companies with a single revenue recognition model for recognizing revenue from contracts with customers. The core principle of the new standard is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which it expects to be entitled in exchange for those goods or services. The adoption of ASU 2014-09 did not have any impact on our revenue recognition, but did result in a change in the accounting for costs incurred to obtain a contract. Pursuant to the new guidance, the Company recognizes the fees that it pays to ICANN for each annual increment of .com domain name registrations and renewals, as an asset which is amortized on a straight-line basis over the related domain name term. This change was adopted using the modified retrospective method. As a result, the Company recorded current and long-term assets of \$19.7 million and \$7.6 million, respectively, a deferred tax liability of \$4.8 million and a decrease to the opening balance of accumulated deficit of \$22.5 million.

Effective January 1, 2018, the Company adopted ASU 2016-18, Restricted Cash, issued by the FASB. ASU 2016-18 requires restricted cash to be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts set forth on the statement of cash flows instead of presenting changes in restricted cash in cash flows from investing activities. As a result of the adoption, the changes in restricted cash are included with cash and cash equivalents on the statement of cash flows for both periods presented. The change in the amounts presented for the prior period was not significant.

Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, Leases. The guidance introduces a lessee model that requires most leases to be reported on the balance sheet. This ASU will become effective for the Company on January 1, 2019. In July 2018, the FASB issued ASU 2018-11, Targeted Improvements to Topic 842 Leases, which allows for an alternative transition approach, which will not require adjustments to comparative prior period amounts.

Based on its current portfolio of leases, the Company does not expect the adoption of this standard to have a material impact on its consolidated financial statements.

Note 2. Revenue

Revenues are recognized when control of the promised services is transferred to our customers, in an amount that reflects the consideration we expect to be entitled to in exchange for those services.

The Company generates revenues in the U.S.; Europe, the Middle East and Africa (“EMEA”); China; and certain other countries, including, but not limited to Canada, Australia, and Japan.

Table of Contents

The following table presents our revenues disaggregated by geography, based on the billing addresses of our customers:

|                | Three Months Ended |            | Nine Months Ended |            |
|----------------|--------------------|------------|-------------------|------------|
|                | September 30,      |            | September 30,     |            |
|                | 2018               | 2017       | 2018              | 2017       |
|                | (in thousands)     |            |                   |            |
| U.S.           | \$ 190,980         | \$ 177,597 | \$ 563,981        | \$ 525,947 |
| EMEA           | 53,047             | 52,790     | 159,831           | 158,509    |
| China          | 27,094             | 27,177     | 79,502            | 80,680     |
| Other          | 34,656             | 34,864     | 104,203           | 104,458    |
| Total revenues | \$ 305,777         | \$ 292,428 | \$ 907,517        | \$ 869,594 |

Revenues for the Company's Registry Services business are attributed to the country of domicile and the respective regions in which registrars are located, however, this may differ from the regions where the registrars operate or where registrants are located. Revenue for each region may be impacted by registrars reincorporating, relocating, or from acquisitions or changes in affiliations of resellers. Revenue for each region may also be impacted by registrars domiciled in one region, registering domain names in another region.

**Registry Services**

Registry Services revenues primarily arise from fixed fees charged to registrars for the initial registration or renewal of .com, .net, and other domain names. Fees for domain name registrations and renewals are generally due at the time of registration or renewal. Domain name registration terms range from one year up to ten years.

Most customers either maintain a deposit with Verisign or provide an irrevocable letter of credit in excess of the amounts owed. New customers are subjected to a credit review process that evaluates the customer's financial condition and, ultimately, their ability to pay.

Verisign also offers promotional marketing programs to its registrars based upon market conditions and the business environment in which the registrars operate. Amounts payable to these registrars for such promotional marketing programs are usually recorded as a reduction of revenue. If Verisign obtains an identifiable benefit separate from the services it provides to the registrars, then amounts payable up to the fair value of the benefit received are recorded as advertising expenses and the excess, if any, is recorded as a reduction of revenue.

**Performance Obligations**

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. Each domain name registration or renewal is considered a separate optional purchase and represents a single performance obligation, which is to allow its registration and maintain that registration (by allowing updates, DNS resolution and Whois services) through the registration term. These services are provided continuously throughout each registration term, and as such, revenues from the initial registration or renewal of domain names are deferred and recognized ratably over the registration term. Fees for renewals and advance extensions to the existing term are deferred until the new incremental period commences. These fees are then recognized ratably over the renewal term.

**Security Services**

Following the revenue recognition criteria above, revenues from Security Services are usually deferred and recognized over the service term, generally one to two years. These revenues are not significant in relation to our consolidated revenues.

**Deferred Revenues**

As payment for domain name registrations and renewals are due in advance of our performance, we record these amounts as deferred revenue. The increase in the deferred revenue balance for the nine months ended September 30, 2018 is primarily driven by cash payments received or due for domain name registrations and renewals, offset by \$607.3 million of revenues recognized that were included in the deferred revenue balance at the beginning of the

period. The balance of deferred revenue as of September 30, 2018 represents our aggregate remaining performance obligations. Amounts included in current deferred revenue are all expected to be recognized in revenue within 12 months, except for a portion of deferred revenue that relates to domain name renewals that are deleted in the 45 day grace period following the transaction. The long-term deferred revenue amounts will be recognized in revenue over several years and in some cases up to ten years.

Historically, we have experienced higher domain name growth in the first quarter of the year compared to other quarters. Our quarterly revenue does not reflect these seasonal patterns because the preponderance of our revenue for each quarterly

Table of Contents

period is provided by the ratable recognition of our deferred revenue balance. The effect of this seasonality has historically resulted in the largest amount of growth in our deferred revenue balance occurring during the first quarter of the year compared to the other quarters.

**Costs Incurred to Obtain a Contract**

As discussed above, we recognize the fees that we pay to ICANN for each annual increment of domain name registrations and renewals, as an asset which will be amortized on a straight-line basis over the related registration term. These assets are included in Other current assets and Other long-term assets on the condensed consolidated balance sheet.

**Practical Expedients and Exemptions**

We recognize sales commissions for our Security Services contracts as expense when incurred because the amortization period for the majority of commissions would have been one year or less. These costs are not material for any period presented and are recorded within sales and marketing expenses.

**Note 3. Financial Instruments****Cash, Cash Equivalents, and Marketable Securities**

The following table summarizes the Company's cash, cash equivalents, and marketable securities and the fair value categorization of the financial instruments measured at fair value on a recurring basis:

|   | September<br>30,<br>2018 | December<br>31,<br>2017 |
|---|--------------------------|-------------------------|
|   | (In thousands)           |                         |
| Cash  | \$33,237                 | \$135,092               |
| Time deposits   | 4,069                    | 3,682                   |
| Money market funds (Level 1)                          | 178,299                  | 116,068                 |
| Debt securities issued by the U.S. Treasury (Level 1) | 972,682                  | 2,169,197               |
| Total   | \$1,188,287              | \$2,424,039             |
| <br>  |                          |                         |
| Cash and cash equivalents                             | \$231,571                | \$465,851               |
| Restricted cash (included in Other long-term assets)  | 9,321                    | 9,288                   |
| Total Cash, cash equivalents, and restricted cash     | 240,892                  | 475,139                 |
| Marketable securities                                 | 947,395                  | 1,948,900               |
| Total   | \$1,188,287              | \$2,424,039             |

The fair value of the debt securities held as of September 30, 2018 was \$972.7 million, including less than \$0.2 million of gross and net unrealized gains. All of the debt securities held as of September 30, 2018 are scheduled to mature in less than one year. The lower Cash and cash equivalents and Marketable securities balances at September 30, 2018 reflect the cash used to settle the principal amount of the Subordinated Convertible Debentures on May 1, 2018, as discussed in Note 8. "Debt and Interest Expense."

**Fair Value Measurements**

The fair value of the Company's investments in money market funds approximates their face value. Such instruments are included in Cash and cash equivalents. The fair value of the debt securities consisting of U.S. Treasury bills is based on their quoted market prices. Debt securities purchased with original maturities in excess of three months are included in Marketable securities. The fair value of all of these financial instruments are classified as Level 1 in the fair value hierarchy.

The Company's other financial instruments include cash, accounts receivable, restricted cash, and accounts payable. As of September 30, 2018, the carrying value of these financial instruments approximated their fair value. The fair values of the senior notes due 2023 (the "2023 Senior Notes"), the senior notes due 2025 (the "2025 Senior Notes"), and the senior notes due 2027 (the "2027 Senior Notes") were \$762.9 million, \$511.5 million, and \$536.1 million, respectively, as of September 30, 2018. The fair values of these debt instruments are based on available market information from public data sources and are classified as Level 2. As part of the settlement of the Subordinated Convertible Debentures

in the second quarter of 2018, the Company estimated the fair value of the liability component of the debentures, based on the present value of the remaining contractual cash flows, using a discount rate of 8.42% (the estimated borrowing rate for similar non-convertible debt). The fair value of the liability component at the time of extinguishment was \$651.3 million and is classified as Level 3.

Table of Contents

## Note 4. Other Balance Sheet Items

## Other Current Assets

Other current assets consist of the following:

|                            | September<br>30,<br>2018 | December<br>31,<br>2017 |
|----------------------------|--------------------------|-------------------------|
|                            | (In thousands)           |                         |
| Prepaid registry fees      | \$20,755                 | \$ —                    |
| Prepaid expenses           | 19,582                   | 15,787                  |
| Accounts receivable, net   | 8,397                    | 5,111                   |
| Income taxes receivable    | 3,672                    | 6,347                   |
| Other                      | 4,610                    | 4,157                   |
| Total other current assets | \$57,016                 | \$ 31,402               |

## Other Long-Term Assets

Other long-term assets consist of the following:

|                              | September<br>30,<br>2018 | December<br>31,<br>2017 |
|------------------------------|--------------------------|-------------------------|
|                              | (In thousands)           |                         |
| Prepaid registry fees        | \$7,752                  | \$ —                    |
| Restricted cash              | 9,321                    | 9,288                   |
| Other tax receivable         | 5,673                    | 5,673                   |
| Other                        | 4,332                    | 3,642                   |
| Total other long-term assets | \$27,078                 | \$ 18,603               |

The current and long-term prepaid registry fees in the tables above relate to the fees the Company pays to ICANN for each annual increment of .com domain name registrations and renewals which are deferred and amortized over the domain name registration term, upon adoption of ASU 2014-09 as discussed in Note 1. The amount of prepaid registry fees as of September 30, 2018 reflects amortization of \$8.3 million and \$24.5 million during the three and nine months ended September 30, 2018 which was recorded in Cost of Revenues.

## Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of the following:

|  | September<br>30,<br>2018 | December<br>31,<br>2017 |
|--|--------------------------|-------------------------|
|  | (In thousands)           |                         |
| Accounts payable                               | \$6,972                  | \$ 10,519               |
| Accrued employee compensation                  | 39,644                   | 51,481                  |
| Customer deposits, net                         | 46,890                   | 63,617                  |
| Interest payable                               | 33,171                   | 47,357                  |
| Accrued registry fees                          | 11,676                   | 10,404                  |
| Income taxes payable and other tax liabilities | 11,231                   | 13,477                  |
| Other accrued liabilities                      | 26,537                   | 22,748                  |
| Total accounts payable and accrued liabilities | \$176,121                | \$ 219,603              |

Accrued employee compensation primarily consists of liabilities for employee leave, salaries, payroll taxes, employee contributions to the employee stock purchase plan, and incentive compensation. Accrued employee incentive compensation as of December 31, 2017, was paid during the nine months ended September 30, 2018. Customer deposits primarily relate to advance payments to cover domain name registration activity by registrars. The balance of customer deposits can fluctuate significantly due to the timing of payments from large customers. Interest payable includes interest payable on the 2023 Senior Notes, the 2025 Senior Notes, and the 2027 Senior Notes. Interest

payable as of December 31, 2017 also includes interest payable on the Subordinated Convertible Debentures.

9

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Table of Contents

## Note 5. Stockholders' Deficit

On February 8, 2018, the Company's Board of Directors authorized the repurchase of approximately \$585.8 million of its common stock, in addition to the \$414.2 million remaining available for repurchase under the previous share repurchase program for a total repurchase authorization of up to \$1.0 billion of its common stock. The share repurchase program has no expiration date. Purchases made under the program can be made through open market transactions, block purchases, accelerated share repurchase agreements or other negotiated transactions. During the three and nine months ended September 30, 2018 the Company repurchased 1.1 million and 3.2 million shares of its common stock, respectively, at an average stock price of \$152.21 and \$133.30, respectively. The aggregate cost of the repurchases in the three and nine months ended September 30, 2018 was \$175.0 million and \$424.9 million, respectively. As of September 30, 2018, \$638.3 million remained available for further repurchases under the share repurchase program.

During the nine months ended September 30, 2018, the Company placed 0.3 million shares, at an average stock price of \$121.40, and for an aggregate cost of \$34.9 million, into treasury stock for purposes related to tax withholding upon vesting of Restricted Stock Units ("RSUs").

Since inception the Company has repurchased 231.1 million shares of its common stock for an aggregate cost of \$9.2 billion, which is presented as a reduction of Additional paid-in capital.

## Note 6. Calculation of Earnings per Share

The following table presents the computation of weighted-average shares used in the calculation of basic and diluted earnings per share:

|  | Three Months<br>Ended<br>September 30,<br>2018 |         | Nine Months<br>Ended<br>September 30,<br>2018 |         |
|--|--|---------|---|---------|
|  | 2017   | 2018    | 2017  | 2018    |
|  | (In thousands)                                 |         |   |         |
| Weighted-average shares of common stock outstanding              | 121,682  | 99,614  | 111,046                                       | 101,036 |
| Weighted-average potential shares of common stock outstanding:   |  |         |   |         |
| Conversion spread related to Subordinated Convertible Debentures | —  | 23,956  | 11,452  | 22,605  |
| Unvested RSUs and ESPP   | 579  | 504     | 581   | 521     |
| Shares used to compute diluted earnings per share                | 122,261  | 124,074 | 123,079                                       | 124,162 |

The weighted average shares of common stock outstanding for the three and nine months ended September 30, 2018, reflects the issuance of 26.1 million shares of common stock related to the settlement of the Subordinated Convertible Debentures on May 1, 2018. The dilutive impact of the conversion spread related to the Subordinated Convertible Debentures is included in the calculation for the nine months ended September 30, 2018, on a weighted-average basis for the period prior to conversion.

The calculation of diluted weighted average shares outstanding, excludes potentially dilutive securities, the effect of which would have been anti-dilutive, as well as performance-based RSUs granted by the Company for which the relevant performance criteria have not been achieved. The number of potential shares excluded from the calculation was not significant in any period presented.

## Note 7. Stock-based Compensation

Stock-based compensation is classified in the Condensed Consolidated Statements of Comprehensive Income in the same expense line items as cash compensation. The following table presents the classification of stock-based compensation:

|                     | Three Months<br>Ended<br>September 30,<br>2018 |         | Nine Months<br>Ended<br>September 30,<br>2018 |         |
|---------------------|--|---------|---|---------|
|                     | 2017   | 2018    | 2017  | 2018    |
|                     | (In thousands)                                 |         |   |         |
| Cost of revenues    | \$1,755  | \$1,774 | \$5,183                                       | \$5,311 |
| Sales and marketing | 1,451  | 1,369   | 4,393   | 4,255   |

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|  |          |          |          |          |
|--|----------|----------|----------|----------|
| Research and development               | 1,623    | 1,575    | 5,032    | 4,553    |
| General and administrative             | 10,301   | 9,387    | 26,798   | 25,924   |
| Total stock-based compensation expense | \$15,130 | \$14,105 | \$41,406 | \$40,043 |

10

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Table of Contents

The following table presents the nature of the Company's total stock-based compensation:

|  | Three Months   |          | Nine Months   |          |
|--|----------------|----------|---------------|----------|
|  | Ended          |          | Ended         |          |
|  | September 30,  |          | September 30, |          |
|  | 2018           | 2017     | 2018          | 2017     |
|  | (In thousands) |          |               |          |
| RSUs   | \$10,817       | \$10,556 | \$29,510      | \$28,930 |
| Performance-based RSUs                                   | 3,875          | 3,100    | 10,348        | 9,992    |
| ESPP   | 1,018          | 1,000    | 3,127         | 2,941    |
| Capitalization (included in Property and equipment, net) | (580 )         | (551 )   | (1,579 )      | (1,820 ) |
| Total stock-based compensation expense                   | \$15,130       | \$14,105 | \$41,406      | \$40,043 |

## Note 8. Debt and Interest Expense

The following table presents the components of the Company's interest expense:

|  | Three Months   |          | Nine Months   |          |
|--|----------------|----------|---------------|----------|
|  | Ended          |          | Ended         |          |
|  | September 30,  |          | September 30, |          |
|  | 2018           | 2017     | 2018          | 2017     |
|  | (In thousands) |          |               |          |
| Contractual interest on Senior Notes                                 | \$21,766       | \$21,403 | \$65,297      | \$51,872 |
| Contractual interest on Subordinated Convertible Debentures          | —              | 12,426   | 20,015        | 32,738   |
| Amortization of debt discount on Subordinated Convertible Debentures | —              | 3,034    | 4,236         | 8,916    |
| Amortization of debt issuance costs and other interest expense       | 865            | 893      | 2,663         | 2,343    |
| Total interest expense   | \$22,631       | \$37,756 | \$92,211      | \$95,869 |

On February 15, 2018, the Company called for the redemption of all the outstanding Subordinated Convertible Debentures with a redemption date of May 1, 2018. Substantially all of the holders elected to convert their debentures, and on May 1, 2018, the Company settled the \$1.25 billion principal value in cash, and issued 26.1 million shares of common stock for the \$3.17 billion excess of the conversion value over the principal amount. Of the total consideration transferred to settle the debentures, \$651.3 million was allocated to the liability component, and the remaining \$3.77 billion was allocated to the equity component. The fair value of the liability component exceeded the \$644.7 million carrying value, and therefore, resulted in a loss of \$6.6 million upon extinguishment of the Subordinated Convertible Debentures in the second quarter of 2018.

## Note 9. Non-operating Income, Net

The following table presents the components of Non-operating income, net:

|   | Three Months   |         | Nine Months   |          |
|---|----------------|---------|---------------|----------|
|   | Ended          |         | Ended         |          |
|   | September 30,  |         | September 30, |          |
|   | 2018           | 2017    | 2018          | 2017     |
|   | (In thousands) |         |               |          |
| Interest income   | \$5,823        | \$5,832 | \$19,894      | \$11,386 |
| Loss on extinguishment of Subordinated Convertible Debentures | —              | —       | (6,554 )      | —        |
| (Loss) gain on sale of business                               | —              | (186 )  | —             | 10,421   |
| Other, net  | 112            | 595     | 1,059         | (263 )   |
| Total non-operating income, net                               | \$5,935        | \$6,241 | \$14,399      | \$21,544 |

In the second quarter of 2018, the Company recognized a \$6.6 million loss on the extinguishment of the Subordinated Convertible Debentures. During the second quarter of 2017, the Company completed the sale of its iDefense business, which resulted in a net gain of approximately \$10.4 million.



Table of Contents

## Note 10. Income Taxes

The following table presents income tax expense and the effective tax rate:

|                    | Three Months Ended     |          | Nine Months Ended |           |
|--------------------|------------------------|----------|-------------------|-----------|
|                    | September 30,          |          | September 30,     |           |
|                    | 2018                   | 2017     | 2018              | 2017      |
|                    | (Dollars in thousands) |          |                   |           |
| Income tax expense | \$40,621               | \$34,645 | \$95,320          | \$102,554 |
| Effective tax rate | 23                     | % 23     | % 19              | % 22      |

The effective tax rate for the three months ended September 30, 2018 was higher than the statutory federal rate of 21% primarily due to state income taxes, partially offset by foreign income taxed at lower rates. The effective tax rate for the nine months ended September 30, 2018 was lower than the federal statutory rate, primarily due to \$12.6 million of tax benefits recognized related to changes to provisional amounts previously recognized for the impact of the Tax Act, \$7.2 million of excess tax benefits related to stock-based compensation and foreign income taxed at lower rates, partially offset by state income taxes. The effective tax rate for the three and nine months ended September 30, 2017 was lower than the statutory federal rate of 35% primarily due to tax benefits from foreign income taxed at lower rates, partially offset by state income taxes. Additionally, the effective tax rate for the nine months ended September 30, 2017 was reduced by \$8.2 million of excess tax benefits related to stock-based compensation.

The Tax Act was enacted on December 22, 2017, most provisions of which became effective starting in 2018. The Company recorded provisional amounts of deferred taxes for the impact of various parts of the Tax Act in 2017. These provisional amounts were adjusted in 2018, primarily due to new IRS guidance, resulting in an income tax benefit of \$12.6 million, and a reduction in the amount of foreign tax credit carryforwards reported as of December 31, 2017 to \$67.9 million. The Company has not completed its accounting for the tax effects of the enactment of the Tax Act. Specifically, the state income tax effects are provisional amounts based on the Company's estimates, which are expected to be finalized in the fourth quarter of 2018 as the state income tax returns are filed and additional guidance from the IRS, if any is received.

As a result of the Tax Act, the Company no longer intends to indefinitely reinvest the earnings of its foreign subsidiaries offshore, and accordingly, during the nine months ended September 30, 2018 the Company completed the repatriation of \$1.15 billion of cash held by foreign subsidiaries, net of \$60.7 million of foreign withholding taxes which was recorded in deferred tax liabilities in 2017.

As of September 30, 2018, the Company's Other long-term tax liabilities includes the \$81.0 million noncurrent liability for U.S. income taxes on accumulated foreign earnings, net of applicable foreign tax credits, while the \$4.8 million current portion of the liability is included in Accounts payable and accrued liabilities. Both the current and noncurrent portion of these liabilities in addition to the \$10.6 million paid through September 30, 2018, had been included in deferred tax liabilities as of December 31, 2017. Other long-term tax liabilities as of September 30, 2018 also reflects the reclassification of unrecognized tax benefits, as deferred tax assets related to tax credits and loss carryforwards are no longer available to offset the liabilities.

The excess interest deductions on the Subordinated Convertible Debentures that were converted will not be subject to recapture, and accordingly, the \$439.2 million deferred tax liability related to the debentures was reversed into Additional paid-in capital upon extinguishment of the debt. As a result of this decrease in deferred tax liabilities, the Company is in a net deferred tax asset position as of September 30, 2018 for every tax jurisdiction.

## Note 11. Subsequent Event

On October 24, 2018, the Company entered into an agreement with NeuStar, Inc. ("Neustar") to sell the rights, economic benefits, and obligations, in all customer contracts related to its Security Services business. The transaction includes the sale of customer agreements related to Verisign's DDoS Protection, Managed Domain Name System ("DNS"), DNS Firewall, and Recursive DNS services. As part of the transaction, the Company will continue to support the Security Services customers during the transition to Neustar, pursuant to a transition services agreement that is expected to be executed at closing. The transaction is subject to customary regulatory approval and is expected to close shortly following the receipt of such approval. The purchase price, subject to a cap of \$120.0 million, consists of

a payment of \$50.0 million, due at the time of closing, plus an additional contingent amount, due after the first anniversary of closing. The additional contingent amount, which cannot be negative, is based upon, among other things, the successful transition of customers to Neustar during the 12-month period following closing.

Table of Contents

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion in conjunction with the interim unaudited Condensed Consolidated Financial Statements and related notes.

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements involve risks and uncertainties, including, among other things, statements regarding our anticipated costs and expenses and revenue mix. Forward-looking statements include, among others, those statements including the words "expects," "anticipates," "intends," "believes" and similar language. Our actual results may differ significantly from those projected in the forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in the section titled "Risk Factors" in Part II, Item 1A of this Quarterly Report on Form 10-Q. You should also carefully review the risks described in other documents we file from time to time with the Securities and Exchange Commission, including the Quarterly Reports on Form 10-Q or Current Reports on Form 8-K that we file in 2018 and our 2017 Form 10-K, which was filed on February 16, 2018, which discuss our business in greater detail. You are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to update publicly or revise such statements, whether as a result of new information, future events, or otherwise, except as required by law.

## Overview

We are a global provider of domain name registry services and internet security, enabling internet navigation for many of the world's most recognized domain names and providing protection for websites and enterprises around the world. Our Registry Services ensure the security, stability, and resiliency of key internet infrastructure and services, including the .com and .net domains, two of the internet's root servers, and the operation of the Root Zone Maintainer function for the core of the internet's DNS. Our product suite also includes Security Services, consisting of DDoS Protection Services and Managed DNS Services. Revenues from Security Services are not significant in relation to our consolidated revenues. On October 24, 2018, we entered into an agreement with Neustar to sell the rights, economic benefits, and obligations, in all customer contracts related to our Security Services business. We will retain our proprietary technology, network assets, critical infrastructure, software, and public DNS service to focus solely on supporting our core mission: ensuring the security, stability, and resiliency of our core infrastructure.

As of September 30, 2018, we had approximately 151.7 million .com and .net registrations in the domain name base. The number of domain names registered is largely driven by continued growth in online advertising, e-commerce, and the number of internet users, which is partially driven by greater availability of internet access, as well as marketing activities carried out by us and our registrars. Growth in the number of domain name registrations under our management may be hindered by certain factors, including overall economic conditions, competition from ccTLDs, the introduction of new gTLDs, and ongoing changes in the internet practices and behaviors of consumers and businesses. Factors such as the evolving practices and preferences of internet users, and how they navigate the internet, as well as the motivation of domain name registrants and how they will manage their investment in domain names, can negatively impact our business and the demand for new domain name registrations and renewals.

## Business Highlights and Trends

We recorded revenues of \$305.8 million and \$907.5 million during the three and nine months ended September 30, 2018, an increase of 5% and 4%, respectively, compared to the same periods in 2017.

We recorded operating income of \$195.0 million and \$573.4 million during the three and nine months ended September 30, 2018. This represents an increase of 8% compared to each of the same periods in 2017.

We finished the third quarter with 151.7 million .com and .net registrations in the domain name base, which represents a 4% increase from September 30, 2017, and a net increase of 2.0 million domain name registrations from June 30, 2018.

- During the three months ended September 30, 2018, we processed 9.5 million new domain name registrations for .com and .net compared to 8.9 million for the same period in 2017.
-

The final .com and .net renewal rate for the second quarter of 2018 was 75.0% compared with 74.0% for the same quarter in 2017. Renewal rates are not fully measurable until 45 days after the end of the quarter. During the three months ended September 30, 2018, we repurchased 1.1 million shares of our common stock under the share repurchase program for \$175.0 million. As of September 30, 2018, \$638.3 million remained available for further repurchases under our share repurchase program.

Table of Contents

- We generated cash flows from operating activities of \$479.3 million during the nine months ended September 30, 2018, compared to \$503.6 million in the same period last year.

Pursuant to our agreements with ICANN, we make available on our website (at <https://www.Verisign.com/zone>) files containing all active domain names registered in the .com and .net registries. At the same website address, we make available a summary of the active zone count registered in the .com and .net registries and the number of .com and .net domain name registrations in the domain name base. The domain name base is the active zone plus the number of domain name registrations that are registered but not configured for use in the respective top level domain zone file plus the number of domain name registrations that are in a client or server hold status. These files and the related summary data are updated at least once per day. The update times may vary each day. The number of domain name registrations provided in this Form 10-Q are as of midnight of the date reported. Information available on, or accessible through, our website is not incorporated herein by reference.

## Results of Operations

The following table presents information regarding our results of operations as a percentage of revenues:

|                            | Three Months<br>Ended<br>September 30,<br>2018 |         | Nine Months<br>Ended<br>September 30,<br>2017 |         |
|----------------------------|--|---------|---|---------|
|                            | 2018   | 2017    | 2018  | 2017    |
| Revenues                   | 100.0 %  | 100.0 % | 100.0 %                                       | 100.0 % |
| Costs and expenses:        |  |         |   |         |
| Cost of revenues           | 15.8   | 16.2    | 15.8  | 16.7    |
| Sales and marketing        | 4.5  | 6.4     | 5.3   | 6.5     |
| Research and development   | 4.5  | 4.3     | 4.7   | 4.6     |
| General and administrative | 11.4   | 11.2    | 11.0  | 11.1    |
| Total costs and expenses   | 36.2   | 38.1    | 36.8  | 38.9    |
| Operating income           | 63.8   | 61.9    | 63.2  | 61.1    |
| Interest expense           | (7.4 )   | (12.9 ) | (10.2 )                                       | (11.0 ) |
| Non-operating income, net  | 1.9  | 2.1     | 1.6   | 2.5     |
| Income before income taxes | 58.3   | 51.1    | 54.6  | 52.6    |
| Income tax expense         | (13.3 )  | (11.8 ) | (10.5 )                                       | (11.8 ) |
| Net income                 | 45.0 %   | 39.3 %  | 44.1 %  | 40.8 %  |

## Revenues

Revenues related to our Registry Services are primarily derived from registrations for domain names in the .com and .net domain name registries. We also derive revenues from operating domain name registries for several other TLDs and from providing back-end registry services to a number of TLD registry operators, all of which are not significant in relation to our consolidated revenues. For domain names registered with the .com and .net registries we receive a fee from registrars per annual registration that is fixed pursuant to our agreements with ICANN. Individual customers, called registrants, contract directly with registrars or their resellers, and the registrars in turn register the domain names with Verisign. Changes in revenues are driven largely by changes in the number of new domain name registrations and the renewal rate for existing registrations as well as the impact of new and prior price increases, to the extent permitted by ICANN and the DOC. New registrations and the renewal rate for existing registrations are impacted by continued growth in online advertising, e-commerce, and the number of internet users, as well as marketing activities carried out by us and our registrars. We increased the annual fee for a .net domain name registration from \$7.46 to \$8.20 on February 1, 2017 and from \$8.20 to \$9.02 on February 1, 2018. We have the contractual right to increase the fees for .net domain name registrations by up to 10% each year during the term of our agreement with ICANN, through June 30, 2023. The annual fee for a .com domain name registration is \$7.85 for the duration of the current .com Registry Agreement through November 30, 2024, except that prices may be raised by up to 7% each year due to the imposition of any new Consensus Policy or documented extraordinary expense resulting from an attack or threat of attack on the Security and Stability (each as defined in the .com Registry Agreement) of the DNS, subject to approval of the DOC. We offer promotional marketing programs for our registrars based upon market

conditions and the business environment in which the registrars operate. All fees paid to us for .com and .net registrations are in U.S. dollars. Revenues from Security Services are not significant in relation to our total consolidated revenues.

Table of Contents

A comparison of revenues is presented below:

| Three Months Ended |             |      | Nine Months Ended |             |      |
|--------------------|-------------|------|-------------------|-------------|------|
| September 30,      |             |      | September 30,     |             |      |
| 2018               | %<br>Change | 2017 | 2018              | %<br>Change | 2017 |

(Dollars in thousands)

Revenues \$305,777 5 % \$292,428 \$907,517 4 % \$869,594

The following table compares the .com and .net domain name registrations in the domain name base managed by our Registry Services business:

|   | September 30, 2018 | %<br>Change | September 30, 2017 |
|---|--------------------|-------------|--------------------|
| .com and .net domain name registrations in the domain name base | 151.7 million      | 4 %         | 145.8 million      |

Revenues increased by \$13.3 million and \$37.9 million during the three and nine months ended September 30, 2018, respectively, as compared to the same periods last year, primarily due to an increase in revenues from the operation of the registries for the .com and .net TLDs, which was driven by a 5% increase in the domain name base for .com and the increase in the .net domain name registration fees in February 2017 and 2018, partially offset by a 6% decline in the domain name base for .net.

Growth in the domain name base has been primarily driven by continued internet growth and marketing activities carried out by us and our registrars. However, competitive pressure from ccTLDs, the introduction of new gTLDs, ongoing changes in internet practices and behaviors of consumers and business, as well as the motivation of existing domain name registrants and how they will manage their investment in domain names, and historical global economic uncertainty, has limited the rate of growth of the domain name base in recent years and may continue to do so in the remainder of 2018 and beyond.

We expect the rate of growth in revenues will remain consistent in the remainder of 2018 compared to the nine months ended September 30, 2018, as a result of continued growth in the aggregate number of .com domain names and increases in the .net domain name registration fees in current and prior years.

#### Geographic revenues

We generate revenues in the U.S.; Europe, the Middle East and Africa (“EMEA”); China; and certain other countries, including, but not limited to Canada, Australia, and Japan.

The following table presents a comparison of our geographic revenues:

| Three Months Ended |             |      | Nine Months Ended |             |      |
|--------------------|-------------|------|-------------------|-------------|------|
| September 30,      |             |      | September 30,     |             |      |
| 2018               | %<br>Change | 2017 | 2018              | %<br>Change | 2017 |

(Dollars in thousands)

|                |           |       |           |           |       |           |
|----------------|-----------|-------|-----------|-----------|-------|-----------|
| U.S.           | \$190,980 | 8 %   | \$177,597 | \$563,981 | 7 %   | \$525,947 |
| EMEA           | 53,047    | — %   | 52,790    | 159,831   | 1 %   | 158,509   |
| China          | 27,094    | — %   | 27,177    | 79,502    | (1 )% | 80,680    |
| Other          | 34,656    | (1 )% | 34,864    | 104,203   | — %   | 104,458   |
| Total revenues | \$305,777 |       | \$292,428 | 907,517   |       | 869,594   |

Revenues for our Registry Services business are attributed to the country of domicile and the respective regions in which our registrars are located, however, this may differ from the regions where the registrars operate or where registrants are located. Revenue growth for each region may be impacted by registrars reincorporating, relocating, or from acquisitions or changes in affiliations of resellers. Revenue growth for each region may also be impacted by registrars domiciled in one region, registering domain names in another region. In the three and nine months ended September 30, 2018, the majority of our revenue growth has come from increased sales to U.S. based registrars.

#### Cost of revenues

Cost of revenues consist primarily of salaries and employee benefits expenses for our personnel who manage the operational systems, depreciation expenses, operational costs associated with the delivery of our services, fees paid to

ICANN, customer support and training, consulting and development services, costs of facilities and computer equipment used in these activities, telecommunications expense and allocations of indirect costs such as corporate overhead.

15

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Table of Contents

A comparison of cost of revenues is presented below:

| Three Months Ended |             |      | Nine Months Ended |             |      |
|--------------------|-------------|------|-------------------|-------------|------|
| September 30,      |             |      | September 30,     |             |      |
| 2018               | %<br>Change | 2017 | 2018              | %<br>Change | 2017 |

(Dollars in thousands)

Cost of revenues \$48,249 (2 )% \$47,333 \$143,766 (1 )% \$145,646

Cost of revenues remained consistent during the three months ended September 30, 2018, compared to the same period last year.

Cost of revenues decreased by \$1.9 million during the nine months ended September 30, 2018, compared to the same period last year, primarily due to decreases in depreciation expenses and salary and employee benefits expenses, partially offset by an increase in telecommunications expenses. Depreciation expenses decreased by \$2.1 million as a result of lower average hardware purchases in recent years. Salary and employee benefits expenses decreased by \$1.7 million, primarily due to a reduction in average headcount resulting from the sale of the iDefense business in April 2017. Telecommunications expenses increased by \$2.1 million as a result of an increase in network costs supporting our operations.

We expect cost of revenues as a percentage of revenues to remain consistent during the remainder of 2018 compared to the nine months ended September 30, 2018.

#### Sales and marketing

Sales and marketing expenses consist primarily of salaries, sales commissions, sales operations and other personnel-related expenses, travel and related expenses, trade shows, costs of lead generation, costs of computer and communications equipment and support services, facilities costs, consulting fees, costs of marketing programs, such as online, television, radio, print and direct mail advertising costs, and allocations of indirect costs such as corporate overhead.

A comparison of sales and marketing expenses is presented below:

| Three Months Ended |             |      | Nine Months Ended |             |      |
|--------------------|-------------|------|-------------------|-------------|------|
| September 30,      |             |      | September 30,     |             |      |
| 2018               | %<br>Change | 2017 | 2018              | %<br>Change | 2017 |

(Dollars in thousands)

Sales and marketing \$13,868 (26 )% \$18,667 \$47,712 (15 )% \$56,463

Sales and marketing expenses decreased by \$4.8 million during the three months ended September 30, 2018, compared to the same period last year due to a \$4.4 million decrease in marketing activities and campaigns supporting our business.

Sales and marketing expenses decreased by \$8.8 million during the nine months ended September 30, 2018, compared to the same period last year, primarily due to decreases in advertising and marketing expenses and salary and employee benefits expenses. Advertising and marketing expenses decreased by \$6.1 million, primarily due to a decrease in marketing activities and campaigns supporting our business. Salary and employee benefits expenses decreased by \$2.7 million due to a decrease in commissions expenses and a reduction in average headcount.

We expect sales and marketing expenses as a percentage of revenues to remain consistent during the remainder of 2018, compared to the nine months ended September 30, 2018.

#### Research and development

Research and development expenses consist primarily of costs related to research and development personnel, including salaries and other personnel-related expenses, consulting fees, facilities costs, computer and communications equipment, support services used in our service and technology development, and allocations of indirect costs such as corporate overhead.

A comparison of research and development expenses is presented below:

| Three Months Ended |  | Nine Months Ended |  |
|--------------------|--|-------------------|--|
| September 30,      |  | September 30,     |  |

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| 2018 | %<br>Change | 2017 | 2018 | %<br>Change | 2017 |
|------|-------------|------|------|-------------|------|
|------|-------------|------|------|-------------|------|

(Dollars in thousands)

|                          |          |     |          |          |     |          |
|--------------------------|----------|-----|----------|----------|-----|----------|
| Research and development | \$13,712 | 8 % | \$12,715 | \$42,842 | 8 % | \$39,569 |
|--------------------------|----------|-----|----------|----------|-----|----------|

Research and development expenses remained consistent during the three months ended September 30, 2018, compared to the same period last year.

Table of Contents

Research and development expenses increased by \$3.3 million during the nine months ended September 30, 2018, compared to the same period last year, primarily due to a \$1.7 million decrease in capitalized labor.

We expect research and development expenses as a percentage of revenues to remain consistent during the remainder of 2018 compared to the nine months ended September 30, 2018.

General and administrative

General and administrative expenses consist primarily of salaries and other personnel-related expenses for our executive, administrative, legal, finance, information technology and human resources personnel, costs of facilities, computer and communications equipment, management information systems, support services, professional services fees, certain tax and license fees, and bad debt expense, offset by allocations of indirect costs such as facilities and shared services expenses to other cost types.

A comparison of general and administrative expenses is presented below:

| Three Months Ended |             | Nine Months Ended |             |
|--------------------|-------------|-------------------|-------------|
| September 30,      |             | September 30,     |             |
| 2018               | %<br>Change | 2017              | 2017        |
|                    |             | 2018              | %<br>Change |

(Dollars in thousands)

|                            |          |     |          |          |     |          |
|----------------------------|----------|-----|----------|----------|-----|----------|
| General and administrative | \$34,951 | 7 % | \$32,654 | \$99,771 | 3 % | \$96,626 |
|----------------------------|----------|-----|----------|----------|-----|----------|

General and administrative expenses increased by \$2.3 million during the three months ended September 30, 2018, compared to the same period last year, primarily due to an increase in salary and employee benefits expenses. Salary and employee benefits expenses increased by \$2.0 million due to an increase in average headcount and bonus expenses.

General and administrative expenses increased by \$3.1 million during the nine months ended September 30, 2018, compared to the same period last year, primarily due to a \$5.0 million increase in salary and employee benefits expenses, resulting from an increase in average headcount and bonus expenses.

We expect general and administrative expenses as a percentage of revenues to remain consistent during the remainder of 2018 compared to the nine months ended September 30, 2018.

Interest expense

The following table presents the components of Interest expense:

|  | Three Months                   |          | Nine Months                    |          |
|--|--------------------------------|----------|--------------------------------|----------|
|  | Ended<br>September 30,<br>2018 | 2017     | Ended<br>September 30,<br>2018 | 2017     |
|  | (In thousands)                 |          |                                |          |
| Contractual interest on Senior Notes                                 | \$21,766                       | \$21,403 | \$65,297                       | \$51,872 |
| Contractual interest on Subordinated Convertible Debentures          | —                              | 12,426   | 20,015                         | 32,738   |
| Amortization of debt discount on Subordinated Convertible Debentures | —                              | 3,034    | 4,236                          | 8,916    |
| Amortization of debt issuance costs and other interest expense       | 865                            | 893      | 2,663                          | 2,343    |
| Total interest expense   | \$22,631                       | \$37,756 | \$92,211                       | \$95,869 |

Contractual interest and amortization of debt discount on the Subordinated Convertible Debentures decreased in the three and nine months ended September 30, 2018 due to the settlement of the outstanding convertible debentures on May 1, 2018. Contractual interest on the Senior Notes increased during the nine months ended September 30, 2018, due to the interest expense recognized on the 2027 Senior Notes which were issued in July 2017.

We expect quarterly interest expense to decrease during the remainder of 2018 compared to the nine months ended September 30, 2018, due to the extinguishment of the Subordinated Convertible Debentures on May 1, 2018.

Table of Contents

## Non-operating income, net

The following table presents the components of Non-operating income, net:

|   | Three Months Ended |         | Nine Months Ended |          |
|---|--------------------|---------|-------------------|----------|
|   | September 30,      |         | September 30,     |          |
|   | 2018               | 2017    | 2018              | 2017     |
|   | (In thousands)     |         |                   |          |
| Interest income   | \$5,823            | \$5,832 | \$19,894          | \$11,386 |
| Loss on extinguishment of Subordinated Convertible Debentures | —                  | —       | (6,554 )          | —        |
| (Loss) gain on sale of business                               | —                  | (186 )  | —                 | 10,421   |
| Other, net  | 112                | 595     | 1,059             | (263 )   |
| Total non-operating income, net                               | \$5,935            | \$6,241 | \$14,399          | \$21,544 |

Interest income increased in the nine months ended September 30, 2018 due to an increase in interest rates on our investments in debt securities. On May 1, 2018, we settled all of the outstanding Subordinated Convertible Debentures, which resulted in a loss on extinguishment of approximately \$6.6 million recognized during the second quarter of 2018. During the second quarter of 2017, we completed the sale of our iDefense business, which resulted in a net gain of approximately \$10.4 million.

## Income tax expense

The following table presents income tax expense and the effective tax rate:

|                    | Three Months Ended     |          | Nine Months Ended |           |
|--------------------|------------------------|----------|-------------------|-----------|
|                    | September 30,          |          | September 30,     |           |
|                    | 2018                   | 2017     | 2018              | 2017      |
|                    | (Dollars in thousands) |          |                   |           |
| Income tax expense | \$40,621               | \$34,645 | \$95,320          | \$102,554 |
| Effective tax rate | 23                     | % 23     | % 19              | % 22      |

The effective tax rate for the three months ended September 30, 2018 was higher than the statutory federal rate of 21% primarily due to state income taxes, partially offset by foreign income taxed at lower rates. The effective tax rate for the nine months ended September 30, 2018 was lower than the federal statutory rate, primarily due to \$12.6 million of tax benefits recognized related to changes to provisional amounts previously recognized for the impact of the Tax Act, \$7.2 million of excess tax benefits related to stock-based compensation and foreign income taxed at lower rates, partially offset by state income taxes. For further discussion of the impact of the Tax Act, refer to Note 10 to our Notes to Condensed Consolidated Financial Statements. The effective tax rate for the three and nine months ended September 30, 2017 was lower than the statutory federal rate of 35% primarily due to tax benefits from foreign income taxed at lower rates, partially offset by state income taxes. Additionally, the effective tax rate for the nine months ended September 30, 2017 was reduced by \$8.2 million of excess tax benefits related to stock-based compensation.

Table of Contents

## Liquidity and Capital Resources

|                           | September<br>30,<br>2018 | December<br>31,<br>2017 |
|---------------------------|--------------------------|-------------------------|
|                           | (In thousands)           |                         |
| Cash and cash equivalents | \$231,571                | \$465,851               |
| Marketable securities     | 947,395                  | 1,948,900               |
| Total                     | \$1,178,966              | \$2,414,751             |

As of September 30, 2018, our principal source of liquidity was \$231.6 million of cash and cash equivalents and \$947.4 million of marketable securities. The marketable securities primarily consist of debt securities issued by the U.S. Treasury meeting the criteria of our investment policy, which is focused on the preservation of our capital through investment in investment grade securities. The cash equivalents consist of amounts invested in money market funds and U.S. Treasury bills purchased with original maturities of less than 90 days. As of September 30, 2018, all of our debt securities have contractual maturities of less than one year. Our cash and cash equivalents are readily accessible. For additional information on our investment portfolio, see Note 3, "Financial Instruments," of our Notes to Condensed Consolidated Financial Statements in Part I, Item I of this Quarterly Report on Form 10-Q.

As a result of the Tax Act, we no longer intend to indefinitely reinvest the earnings of our foreign subsidiaries offshore, and accordingly, during the first quarter of 2018 we completed the previously disclosed repatriation of \$1.15 billion of cash held by foreign subsidiaries, net of \$60.7 million of foreign withholding taxes which were accrued during 2017. As of September 30, 2018, the amount of cash and cash equivalents and marketable securities held by foreign subsidiaries was \$671.3 million.

We had historically derived significant tax savings from the Subordinated Convertible Debentures, as the interest deduction for tax purposes had exceeded the cash interest paid, due to the structure of the debentures and the related tax laws. However, as a result of the enactment of the Tax Act, which includes limits on interest deductibility and a lower U.S. federal income tax rate, these tax savings were expected to diminish. Due to the diminished tax savings and several other factors, on February 15, 2018 we called for the redemption of all the outstanding Subordinated Convertible Debentures, with a redemption date of May 1, 2018. Substantially all of the holders elected to convert their debentures, and upon conversion on May 1, 2018, the Company settled the \$1.25 billion principal value in cash, and issued 26.1 million shares of common stock for the \$3.17 billion excess of the conversion value over the principal amount. The excess interest deductions on the Subordinated Convertible Debentures that were converted, will not be subject to recapture, and accordingly, the \$439.2 million deferred tax liability related to the debentures was reversed into Additional paid-in capital upon extinguishment of the debt.

On February 8, 2018, our Board authorized the repurchase of approximately \$585.8 million of our common stock, in addition to the \$414.2 million of our common stock remaining available for repurchase under the previous share repurchase program, for a total repurchase authorization of up to \$1.0 billion of our common stock. During the three months ended September 30, 2018, we repurchased 1.1 million shares of our common stock under the share repurchase program for \$175.0 million. As of September 30, 2018, \$638.3 million remained available for further repurchases under our share repurchase program.

As of September 30, 2018, we had \$550.0 million principal amount outstanding of 4.75% senior unsecured notes due 2027, \$500.0 million principal amount outstanding of the 5.25% senior unsecured notes due 2025, and \$750.0 million principal amount outstanding of the 4.625% senior unsecured notes due 2023. As of September 30, 2018, there were no borrowings outstanding under the \$200.0 million unsecured revolving credit facility that will expire in 2020.

We believe existing cash, cash equivalents and marketable securities, and funds generated from operations, together with our borrowing capacity under the unsecured revolving credit facility should be sufficient to meet our working capital, capital expenditure requirements, and to service our debt for at least the next 12 months. We regularly assess our cash management approach and activities in view of our current and potential future needs.

Table of Contents

In summary, our cash flows for the nine months ended September 30, 2018 and 2017 are as follows:

|  | Nine Months Ended<br>September 30, |            |
|--|------------------------------------|------------|
|  | 2018                               | 2017       |
|  | (In thousands)                     |            |
| Net cash provided by operating activities                                      | \$479,267                          | \$503,568  |
| Net cash provided by (used in) investing activities                            | 984,447                            | (531,973 ) |
| Net cash (used in) provided by financing activities                            | (1,696,976)                        | 81,810     |
| Effect of exchange rate changes on cash, cash equivalents, and restricted cash | (985 )                             | 1,118      |
| Net (decrease) increase in cash, cash equivalents, and restricted cash         | \$(234,247)                        | \$54,523   |
| Cash flows from operating activities   |                                    |            |

Our largest source of operating cash flows is cash collections from our customers. Our primary uses of cash from operating activities are for personnel related expenditures, and other general operating expenses, as well as payments related to taxes, interest and facilities.

Net cash provided by operating activities decreased during the nine months ended September 30, 2018, compared to the same period last year, primarily due to increases in cash paid for income taxes, partially offset by increases in cash received from customers and interest income, and a decrease in cash paid to suppliers and employees. The increase in cash paid for income taxes was primarily due to the foreign withholding taxes paid on the repatriation of \$1.15 billion cash held by foreign subsidiaries to the U.S. in the first quarter of 2018, and U.S. income taxes paid on accumulated foreign earnings. Cash received from customers increased primarily due to higher domain name registrations and renewals, and the increases in the .net domain name registration fees in February 2018. Cash received from interest income increased due to increases in interest rates on our investments in debt securities. Cash paid to suppliers and employees decreased due to timing of certain vendor payments and a decrease in operating expenses.

#### Cash flows from investing activities

The changes in cash flows from investing activities primarily relate to purchases, maturities and sales of marketable securities, and purchases of property and equipment and proceeds from the sale of businesses.

We had net cash inflows from investing activities during the nine months ended September 30, 2018, compared to net cash outflows during the same period last year, primarily due to an increase in proceeds from sales and maturities of marketable securities, net of purchases, and a decrease in purchases of property and equipment, partially offset by a decrease in other investing activities including the proceeds received in the first quarter of 2017 from the sale of our iDefense business.

#### Cash flows from financing activities

The changes in cash flows from financing activities primarily relate to share repurchases, debt repayments, proceeds from borrowings, and our employee stock purchase plan.

We had net cash outflows from financing activities during the nine months ended September 30, 2018, compared to net cash inflows during the same period last year, primarily due to the repayment of the principal amount of the Subordinated Convertible Debentures during the second quarter of 2018 and the proceeds received from the issuance of the 4.75% senior notes due 2027 in the third quarter of 2017, partially offset by a decrease in share repurchases.

Table of Contents

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Other than the settlement of all the outstanding Subordinated Convertible Debentures in the second quarter of 2018, there have been no significant changes in our market risk exposures since December 31, 2017.

**ITEM 4. CONTROLS AND PROCEDURES**

Based on our management's evaluation, with the participation of our Chief Executive Officer (our principal executive officer) and our Chief Financial Officer (our principal financial officer), as of September 30, 2018, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

**Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the three months ended September 30, 2018 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Inherent Limitations of Disclosure Controls and Internal Control over Financial Reporting**

Because of their inherent limitations, our disclosure controls and procedures and our internal control over financial reporting may not prevent material errors or fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. The effectiveness of our disclosure controls and procedures and our internal control over financial reporting is subject to risks, including that the control may become inadequate because of changes in conditions or that the degree of compliance with our policies or procedures may deteriorate.

Table of Contents

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Verisign is involved in various investigations, claims and lawsuits arising in the normal conduct of its business, none of which, in its opinion, will have a material adverse effect on its financial condition, results of operations, or cash flows. The Company cannot assure you that it will prevail in any litigation. Regardless of the outcome, any litigation may require the Company to incur significant litigation expense and may result in significant diversion of management attention.

ITEM 1A. RISK FACTORS

In addition to other information in this Form 10-Q, the following risk factors should be carefully considered in evaluating us and our business because these factors currently have a significant impact or may have a significant impact on our business, operating results or financial condition. Actual results could differ materially from those projected in the forward-looking statements contained in this Form 10-Q as a result of the risk factors discussed below and elsewhere in this Form 10-Q and in other filings we make with the SEC.

Risks arising from our agreements governing our Registry Services business could limit our ability to maintain or grow our business.

We are parties to (i) a Cooperative Agreement (as amended) with the DOC with respect to the .com gTLD and (ii) Registry Agreements with ICANN for .com, .net, .name, and other gTLDs including our IDN gTLDs. As substantially all of our revenues are derived from our Registry Services business, limitations and obligations in, or changes or challenges to, these agreements, particularly the agreements that involve .com and .net, could have a material adverse impact on our business. Certain competing registries, such as the ccTLDs, do not face the same limitations or obligations that we face in our agreements.

**Modifications or Amendments.** In October 2016, the Company and ICANN entered into an amendment to extend the term of the .com Registry Agreement to November 30, 2024 (the “.com Amendment”). As part of the .com Amendment, the Company and ICANN agreed to negotiate in good faith to amend the terms of the .com Registry Agreement: (i) by October 20, 2018, to preserve and enhance the security and stability of the internet or the .com TLD, and (ii) as may be necessary for consistency with changes to, or the termination or expiration of, the Cooperative Agreement. We can provide no assurance that any new terms for the .com Registry Agreement that we agree to as a result of the above obligations will not have a material adverse impact on our business, operating results, financial condition, and cash flows.

The DOC approved the .com Amendment under amendment 34 to the Cooperative Agreement. The DOC did not extend the term of the Cooperative Agreement, which will expire on November 30, 2018, unless the DOC, in its sole discretion, extends the term. Under amendment 34, the DOC has the right to conduct a public interest review for the sole purpose of determining whether the DOC will exercise its right to extend the term of the Cooperative Agreement. In connection with the aforementioned review, we agreed to cooperate fully and to work in good faith to reach a mutual agreement with the DOC to resolve issues identified in such review and to work in good faith to implement any agreed upon changes as of the expiration of the current term of the Cooperative Agreement. In addition to the Cooperative Agreement expiring or the term extending as referenced above, the Company and the DOC could mutually agree to amend the Cooperative Agreement. We can provide no assurance that any changes that we agree to as a result of the above obligations will not have a material adverse impact on our business, operating results, financial condition, and cash flows.

In addition, our Registry Agreements for new gTLDs, including the Registry Agreements for our IDN gTLDs, include ICANN’s right to amend the agreements without our consent, which could impose unfavorable contract obligations on us that could impact our plans and competitive positions with respect to new gTLDs. At the time of renewal of our .com or .net Registry Agreements, ICANN might also attempt to impose this same unilateral right to amend these registry agreements under certain conditions. ICANN has also included new mandatory obligations on new gTLD registry operators, including us, that may increase the risks and potential liabilities associated with operating new

gTLDs. ICANN might seek to impose these new mandatory obligations in our other Registry Agreements under certain conditions. We can provide no assurance that any changes to our Registry Agreements as a result of the above obligations will not have a material adverse impact on our business, operating results, financial condition, and cash flows.

Pricing. Under the terms of the Cooperative Agreement with the DOC and the .com Registry Agreement with ICANN, we are restricted during the term of the Registry Agreement from increasing the price of registrations or renewals of .com domain names above \$7.85, except that we are entitled to increase the price up to 7%, with the prior approval of the DOC, due to the imposition of any new ICANN Consensus Policies, as established and defined under ICANN's bylaws and due process, and covering certain items listed in the .com Registry Agreement, or documented extraordinary expense resulting from an attack or threat of attack on the security and stability of the DNS. However, it is uncertain that such circumstances will arise, or if they do,

Table of Contents

whether we would seek, or the DOC would approve, any request to increase the price for .com domain name registrations. We also have the right under the Cooperative Agreement to seek the removal of these pricing restrictions if we demonstrate to the DOC that market conditions no longer warrant such restrictions. However, it is uncertain whether we will seek the removal of such restrictions, or whether the DOC would approve the removal of such restrictions. In comparison, under the terms of the .net and .name Registry Agreements with ICANN, we are permitted to increase the price of domain name registrations and renewals in these TLDs up to 10% per year. Additionally, ICANN's registry agreements for new gTLDs do not contain such pricing restrictions.

**Vertical integration.** Under the .com, .net, and .name Registry Agreements with ICANN, as well as the Cooperative Agreement with the DOC, we are not permitted to acquire, directly or indirectly, control of, or a greater than 15% ownership interest in, any ICANN-accredited registrar. Historically, all gTLD registry operators were subject to this vertical integration prohibition; however, ICANN has established a process whereby registry operators may seek ICANN's approval to remove this restriction, and ICANN has approved such removal in several instances. If we were to seek removal of the vertical integration restrictions contained in our agreements, it is uncertain whether ICANN and/or DOC approval would be obtained. Additionally, ICANN's registry agreement for new gTLDs generally permits such vertical integration, with certain limitations including ICANN's right, but not the obligation, to refer such vertical integration activities to competition authorities. Furthermore, such vertical integration restrictions do not generally apply to ccTLD registry operators. If registry operators of other TLDs are able to obtain competitive advantages through such vertical integration, it could materially harm our business.

**Renewal and Termination.** Our .com, .net, and .name Registry Agreements with ICANN contain "presumptive" rights of renewal upon the expiration of their current terms on November 30, 2024, June 30, 2023 and August 15, 2020, respectively. The Registry Agreements for our new gTLDs including our IDN gTLDs are subject to a 10-year term and contain similar "presumptive" renewal rights. If certain terms in our .com and .net Registry Agreements are not similar to such terms generally in effect in the registry agreements of the five largest gTLDs, then a renewal of these agreements shall be upon terms reasonably necessary to render such terms similar to the registry agreements for those other gTLDs. There can be no assurance that such terms, if they apply, will not have a material adverse impact on our business. A renewal of the .com Registry Agreement must be approved by the DOC, which, under certain circumstances, could refuse to grant its approval to the renewal of the .com Registry Agreement on similar terms, or at all. A failure (i) by ICANN or the DOC to approve the renewal of the .com Registry Agreement prior to the expiration of its current term on November 30, 2024, or (ii) by ICANN to approve the renewal of the .net Registry Agreement prior to or upon the expiration of its current term on June 30, 2023, would have, absent an extension, a material adverse effect on our business. ICANN could terminate or refuse to renew our .com or .net Registry Agreements if, upon proper notice, (i) we fail to cure a fundamental and material breach of certain specified obligations, and (ii) we fail to timely comply with a final decision of an arbitrator or court. ICANN's termination or refusal to renew either the .com or .net Registry Agreement would have a material adverse effect on our business.

**Consensus Policies.** Our Registry Agreements with ICANN require us to implement Consensus Policies and specifications or policies established on a temporary basis ("Temporary Policies"). ICANN could adopt Consensus Policies or Temporary Policies that are unfavorable to us as the registry operator of .com, .net and our other gTLDs, that are inconsistent with our current or future plans, that impose substantial costs on our business, that subject the Company to additional legal risks, or that affect our competitive position. Such Consensus Policies or Temporary Policies could have a material adverse effect on our business. As an example, ICANN has adopted a Consensus Policy that requires Verisign to receive and display Thick WHOIS data for .com and .net. In addition, ICANN has recently adopted a new Temporary Specification that establishes temporary requirements for registry operators and registrars regarding the collection, display and disclosure of Thick WHOIS data pending ICANN's establishment of a permanent Consensus Policy. The costs of complying or failing to comply with these policies as well as laws and regulations regarding personally identifiable information and data privacy, such as domestic and various foreign privacy regimes, could expose us to compliance costs and substantial liability, and result in costly and time-consuming investigations or litigation.

**Technical Standards.** Our Registry Agreements with ICANN require Verisign to implement and comply with various technical standards and specifications published by the Internet Engineering Task Force ("IETF"). ICANN could impose

requirements on us through changes to IETF standards that are inconsistent with our current or future plans, that impose substantial costs on our business, that subject the Company to additional legal risks, or that affect our competitive position. Such changes to such IETF standards could have a material adverse effect on our business.

**Legal Challenges.** Our Registry Agreements have faced, and could face in the future, challenges, including possible legal challenges, resulting from our activities or the activities of ICANN, registrars, registrants, and others, and any adverse outcome from such challenges could have a material adverse effect on our business.

Governmental regulation and the application of new and existing laws in the U.S. and overseas may slow business growth, increase our costs of doing business, create potential liability and have an adverse effect on our business.

Table of Contents

Application of new and existing laws and regulations in the U.S. or overseas to the internet and communications industry can be unclear. The costs of complying or failing to comply with these laws and regulations could limit our ability to operate in our current markets, expose us to compliance costs and substantial liability, and result in costly and time-consuming litigation. For example, the government of China has indicated that it will issue, and in some instances has begun to issue, new regulations, and has begun to enforce existing regulations, that impose additional costs on, and risks to, our provision of Registry Services in China and could impact the growth or renewal rates of domain name registrations in China. In addition to registry operators, certain of such regulations also require registrars to obtain a government-issued license for each TLD whose domain name registrations they intend to sell directly to registrants. Any failure to obtain the required licenses, or to comply with any license requirements or any updates thereto, by us or our registrars could impact the growth of our business in China.

Foreign, federal or state laws could have an adverse impact on our business, financial condition, results of operations and cash flows, and our ability to conduct business in certain foreign countries. For example, laws designed to restrict who can register and who can distribute domain names, the online distribution of certain materials deemed harmful to children, online gambling, counterfeit goods, and intellectual property violations such as cybersquatting; laws designed to require registrants to provide additional documentation or information in connection with domain name registrations; and laws designed to promote cyber security may impose significant additional costs on our business or subject us to additional liabilities. We have a contract pursuant to which we provide services to the U.S. government and it imposes compliance costs, including compliance with the Federal Acquisition Regulation, which could be significant to the Company.

To conduct our operations, we regularly move data across national borders and receive data originating from different jurisdictions, and consequently are subject to a variety of continuously evolving and developing laws and regulations in the United States and abroad regarding privacy, data protection and data security. The scope of the laws that may be applicable to us is often uncertain and may be conflicting, particularly with respect to foreign laws. For example, the European Union's General Data Protection Regulation, which greatly increases the jurisdictional reach of European Union law and adds a broad array of requirements for handling personal data, including the public disclosure of significant data breaches, and significant penalties, became effective in May 2018. Other countries have enacted or are enacting data localization laws that require data to stay within their borders. All of these evolving compliance and operational requirements can impose significant costs for us that are likely to increase over time.

Due to the nature of the internet, it is possible that federal, state or foreign governments might attempt to regulate internet transmissions or prosecute us for violations of laws. We might unintentionally violate such laws, such laws may be modified or enforced using new or novel legal theories, and new laws may be enacted in the future. In addition, as we launch our IDN gTLDs and increase our marketing efforts of our other TLDs in foreign countries, we may raise our profile in certain foreign countries thereby increasing the regulatory and other scrutiny of our operations. Any such developments could increase the costs of regulatory compliance for us, affect our reputation, expose us to liability, penalties or fines, force us to change our business practices or otherwise materially harm our business. In addition, any such laws could impede growth of or result in a decline in domain name registrations, as well as impact the demand for our services.

Undetected or unknown defects in our service, security breaches, defects in the technologies and services in our supply chain, and DDoS attacks could expose us to liability and harm our business and reputation.

Services as complex as those we offer or develop could contain undetected defects or errors. Despite testing, defects or errors may occur in our existing or new services, which could result in compromised customer data, including DNS data, diversion of development resources, injury to our reputation, tort or contract claims, increased insurance costs or increased service costs, any of which could harm our business. Performance of our services could have unforeseen or unknown adverse effects on the networks over which they are delivered as well as, more broadly, on internet users and consumers, and third-party applications and services that utilize our services, which could result in legal claims against us, harming our business. Our failure to identify, remediate and mitigate security vulnerabilities and breaches or our inability to meet customer expectations in a timely manner could also result in loss of or delay in revenues, failure to meet contracted service level obligations, loss of market share, failure to achieve market acceptance, injury to our reputation and increased costs.

In addition to undetected defects or errors, we are also subject to cyber-attacks and attempted security breaches. We retain certain customer and employee information in our data centers and various domain name registration systems. It is critical to our business strategy as well as fulfilling our obligations as the registry operator for .com and .net, that our facilities and infrastructure remain secure, that we continue to meet our service level agreements and we maintain the public's trust in the internet services that we provide. The Company, as an operator of critical internet infrastructure, is frequently targeted and experiences a high rate of attacks. These include the most sophisticated forms of attacks, such as advanced persistent threat attacks and zero-hour threats. These forms of attacks involve situations where the threat is not compiled or has been previously unobserved within our observation and threat indicators space until the moment it is launched. In addition, these forms of attacks may target specific unidentified or unresolved vulnerabilities that exist only within the target's supply chain or operating environment, making these attacks virtually impossible to anticipate and difficult to defend against. In addition to external

Table of Contents

threats, we may be subject to insider threats, including those from third-party suppliers such as consultants and advisors, SaaS providers, hardware, software, and network systems manufacturers, and other outside vendors, or from current, former or contract employees; these threats can be realized from intentional or unintentional actions. The Shared Registration System, the root zone servers, the root zone file, the Root Zone Management System, the TLD name servers and the TLD zone files that we operate are critical to our Registry Services operations. As a result of our Registry Services operations, attacks against third-party suppliers could also impact our infrastructure. Despite the significant time and money expended on our security measures, we have been subject to a security breach, as disclosed in our Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, and our infrastructure may in the future be vulnerable to physical break-ins, disruptions resulting from destructive malware, hardware or enabling software defects, computer viruses, attacks by hackers or nefarious actors or similar disruptive problems, including hacktivism. It is possible that we may have to expend additional financial and other resources to address such problems. Any physical or electronic break-in or other security breach or compromise of the information stored at our data centers or domain name registration systems may cause an outage of, or jeopardize the security of, information stored on our premises or in the computer systems and networks of our customers. In such an event, we could face significant liability, fail to meet contracted service level obligations, customers could be reluctant to use our services and we could be at risk for loss of various security and standards-based compliance certifications needed for operation of our businesses, all or any of which could adversely affect our reputation and harm our business. Such an occurrence could also result in adverse publicity and therefore adversely affect the market's perception of the security of e-commerce and communications over the internet as well as of the security or reliability of our services.

We use externally developed technology, systems and services including both hardware and software, for a variety of purposes, including, without limitation, compute, storage, encryption and authentication, back-office support, and other functions. While we have developed operational policies and procedures to reduce the impact of security vulnerabilities in system components as well as at any vendors where Company data is stored or processed, such measures cannot provide absolute security. Vulnerabilities in, and exploits leading to breaches of our vendors' technology, systems or services could expose us or our customers to a risk of loss or misuse of Company data, including but not limited to sensitive personally identifiable information.

Additionally, our networks have been, and likely will continue to be, subject to DDoS attacks. Recent attacks have demonstrated that DDoS attacks continue to grow in size and sophistication and have an ability to widely disrupt internet services. Particularly since 2016, the size of DDoS attacks has grown rapidly, and we have successfully mitigated DDoS attacks during this time frame that are significantly larger than those we have historically experienced. While we have adopted mitigation techniques, procedures and strategies to defend against such attacks, there can be no assurance that we will be able to defend against every attack, especially as the attacks increase in size and sophistication. Any attack, even if only partially successful, could disrupt our networks, increase response time, negatively impact our ability to meet our contracted service level obligations, and generally hamper our ability to provide reliable service to our Registry Services customers and the broader internet community. We have historically incurred, and will continue to incur, significant costs to ensure that our infrastructure can process levels of attack traffic that are significant multiples of our normal transaction volume. Further, we sell DDoS protection services to our Security Services customers. Although we increase our knowledge of and develop new techniques in the identification and mitigation of attacks through the protection of our Security Services customers, the DDoS protection services share some of the infrastructure used in our Registry Services business. Therefore the provision of such services might expose our critical Registry Services infrastructure to temporary degradations or outages caused by DDoS attacks against those customers, in addition to any attacks directed specifically against us and our networks. Changes to the multi-stakeholder model of internet governance could materially and adversely impact our business. The internet is governed under a multi-stakeholder model comprising civil society, the private sector including for-profit and not-for-profit organizations such as ICANN, governments including the U.S. government, academia, non-governmental organizations and international organizations.

Role of the U.S. Government. In the fourth quarter of 2016, the United States government completed a transition to the multi-stakeholder community of the historical role played by NTIA in the coordination of the DNS. Changes arising from this transition to the multi-stakeholder model of internet governance could materially and adversely

impact our business. For example, ICANN has adopted bylaws that are designed, in part, to enhance accountability through a new organization called the Empowered Community, which is comprised of a cross section of stakeholders. ICANN or the Empowered Community may assert positions that could negatively impact our strategy or our business. By completing the transition discussed above, the U.S. Government through the NTIA has ended its coordination and management of important aspects of the DNS including the IANA functions and the root zone. There can be no assurance that the removal of the U.S. Government oversight of these key functions will not negatively impact our business.

Role of ICANN. ICANN plays a central coordination role in the multi-stakeholder system. ICANN is mandated through its bylaws to uphold a private sector-led multi-stakeholder approach to internet governance for the public benefit. If ICANN or the

## Table of Contents

Empowered Community fails to uphold or significantly redefines the multi-stakeholder model, it could harm our business. Additionally, the Empowered Community could adversely impact ICANN, which could negatively impact its ability to coordinate the multi-stakeholder system of governance, or negatively affect our interests. Also, legal, regulatory or other challenges could be brought challenging the legal authority underlying the roles and actions of ICANN, the Empowered Community or us.

Role of Foreign Governments. Some governments and members of the multi-stakeholder community have questioned ICANN's role with respect to internet governance and, as a result, could seek a multilateral oversight body as a replacement. Additionally, the role of ICANN's Governmental Advisory Committee, which is comprised of representatives of national governments, could change, giving governments more control of certain aspects of internet governance. Some governments and governmental authorities outside the U.S. have in the past disagreed, and may in the future disagree, with the actions, policies or programs of ICANN, the U.S. Government and us relating to the DNS. Changes to the roles that foreign governments play in internet governance could materially and adversely impact our business.

We face risks from our operation of two root zone servers and performance of the Root Zone Maintainer functions under the RZMA.

We operate two of the 13 root zone servers. Root zone servers are name servers that contain authoritative data for the very top of the DNS hierarchy. These servers have the software and DNS configuration data necessary to locate name servers that contain authoritative data for the TLDs. These root zone servers are critical to the functioning of the internet. We also have an important operational role in support of a key IANA function as the Root Zone Maintainer. In this role, we provision and publish the authoritative root zone data and make it available to all root server operators under an agreement with ICANN, the Root Zone Maintainer Service Agreement ("RZMA").

As we perform the Root Zone Maintainer functions under the RZMA, we may be subject to significant claims challenging the agreement or our performance under the agreement, and we may not have immunity from, or sufficient indemnification for, such claims.

For example, DNSSEC enabled in the root zone and at other levels of the DNS requires new preventative maintenance, including root key signing key ("KSK") rollover, necessitating functions and complex operational practices that did not exist prior to the introduction of DNSSEC. Any failure by us, ICANN, external DNS vendors and service providers, or other relying parties to comply with stated practices, such as those outlined in relevant DNSSEC Practice Statements and internet standards, introduces risk to DNSSEC relying parties and other internet users and consumers of the DNS, which could have a material adverse impact on our business. In particular, because root KSK rollover involves updates both to certain keys managed by us in our role as Root Zone Maintainer and to corresponding keys maintained by external DNS vendors and service providers' DNSSEC implementations, if such external parties are not adequately prepared for and/or do not appropriately effectuate root key updates, any root KSK rollover, including the initial rollover that occurred on October 11, 2018 at ICANN's direction, may introduce substantial risk to relying parties. Even where we have correctly implemented our key updates, we could face potential legal claims and reputational harm if the failures described occur.

Additionally, over 1,200 new gTLDs have already been delegated into the root zone in the current round of new gTLDs. ICANN plans on offering a subsequent round of new gTLDs, the timing of which remains uncertain. As set forth in the Verisign Labs Technical Report #1130007 version 2.2: New gTLD Security and Stability Considerations released on March 28, 2013, and expanded upon in subsequent publications, we continue to believe there are potential security and stability issues that could involve the root zone and at other levels of the DNS from the deployment of the new gTLDs that should have been addressed before any new gTLDs were delegated, and despite our and others' efforts, some of these issues have not been addressed by ICANN sufficiently, if at all. For example, domain name collisions have been reported to ICANN, which have resulted in various network interruptions for enterprises as well as confusion and usability issues that have led to phishing and other cyber-attacks. It is anticipated that as additional new gTLDs are delegated now, or in subsequent rounds, more domain name collisions and associated security issues will occur.

The evolution of internet practices and behaviors and the adoption of substitute technologies may impact the demand for domain names.

Domain names and the domain name system have been used by consumers and businesses to access or disseminate information, conduct e-commerce, and develop an online identity for many years. The growth of technologies such as social media, mobile devices, apps and the dominance of search engines has evolved and changed the internet practices and behaviors of consumers and businesses alike. These changes can impact the demand for domain names by those who purchase domain names for personal, commercial and investment reasons. Factors such as the evolving practices and preferences of internet users and how they navigate the internet as well as the motivation of domain name registrants and how they will monetize their investment in domain names can negatively impact our business. Some domain name registrars and registrants seek to purchase and resell domain names following an increase in their value. Adverse changes in the resale value of domain names, changes in

Table of Contents

the business models for such domain name registrars and registrants, or other factors could result in a decrease in the demand and/or renewal rates for domain names in our TLDs. The resulting decrease in demand and/or renewal rates could negatively impact the volume of new domain name registrations, our renewal rates and our associated revenue growth.

Some domain name registrants use a domain name to access or disseminate information, conduct e-commerce, and develop an online identity. Currently, internet users often navigate to a website either by directly typing its domain name into a web browser, the use of an app on their smart phone or mobile device, the use of a voice recognition technology such as Alexa, Cortana, Google Assistant, or Siri, or through the use of a search engine. If (i) web browser or internet search technologies were to change significantly; (ii) internet users' preferences or practices shift away from recognizing and relying on web addresses for navigation through the use of new and existing technologies; (iii) internet users were to significantly decrease the use of web browsers in favor of applications to locate and access content; (iv) internet users were to significantly decrease the use of domain names to develop and protect their online identity; or (v) internet users were to increasingly use third level domains or alternate identifiers, such as social networking and microblogging sites, in each case the demand for domain names in our TLDs could decrease. This may trigger current or prospective customers and parties in our target markets to reevaluate their need for registration or renewal of domain names.

Some domain name registrars and registrants seek to generate revenue through advertising on their websites; changes in the way these registrars and registrants are compensated (including changes in methodologies and metrics) by advertisers and advertisement placement networks, such as Google, Yahoo!, Baidu and Bing, have, and may continue to, adversely affect the market for those domain names favored by such registrars and registrants which has resulted in, and may continue to result in, a decrease in demand and/or the renewal rate for those domain names. For example, according to published reports, Google has in the past changed (and may change in the future) its search algorithm, which may decrease site traffic to certain websites and provide less pay-per-click compensation for certain types of websites. This has made such websites less profitable which has resulted in, and may continue to result in, fewer domain registrations and renewals. In addition, as a result of the general economic environment, spending on online advertising and marketing may not increase or may be reduced, which in turn, may result in a further decline in the demand for those domain names.

If any of the above factors negatively impact the renewal of domain names or the demand for new domain names, we may experience material adverse impacts on our business, operating results, financial condition and cash flows.

Many of our markets are evolving, and if these markets fail to develop or if our products and services are not widely accepted in these markets, our business could be harmed.

We seek to serve many new, developing and emerging markets in foreign countries to grow our business. These markets are rapidly evolving, and may not grow. Even if these markets grow, our services may not be widely used or accepted. Accordingly, the demand for our services in these markets is very uncertain. The factors that may affect market acceptance or adoption of our services in these markets include the following:

- regional internet infrastructure development, expansion, penetration and adoption;
- market acceptance and adoption of substitute products and services that enable online presence without a domain, including social media, ecommerce platforms, website builders and mobile applications;
- public perception of the security of our technologies and of IP and other networks;
  - the introduction and consumer acceptance of new generations of mobile devices, and in particular the use of internet navigation mobile applications as the primary engagement mechanism;
- increasing cyber threats and the associated customer need and demand for our Security Services offerings;
- government regulations affecting internet access and availability, domain name registrations or the provision of registry services, data security or data localization, or e-commerce and telecommunications over the internet;
- the maturity and depth of the sales channels within developing and emerging markets and their ability and motivation to establish and support sales for domain names;
- preference by markets for the use of their own country's ccTLDs as a substitute or alternative to our TLDs; and
- increased acceptance and use of new gTLDs as substitutes for established gTLDs.

If the market for e-commerce and communications over IP and other networks does not grow or these services are not widely accepted in the market, our business could be materially harmed.

27

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Table of Contents

The business environment is highly competitive and, if we do not compete effectively, we may suffer lower demand for our products, reduced gross margins and loss of market share.

The internet and communications network services industries are characterized by rapid technological change and frequent new product and service announcements which require us continually to improve the performance, features and reliability of our services, particularly in response to competitive offerings or alternatives to our products and services. In order to remain competitive and retain our market position, we must continually improve our access to technology and software, support the latest transmission technologies, and adapt our products and services to changing market conditions and our customers' and internet users' preferences and practices, or launch entirely new products and services such as new gTLDs in anticipation of, or in response to, market trends. We cannot assure that competing technologies developed by others or the emergence of new industry standards will not adversely affect our competitive position or render our services or technologies noncompetitive or obsolete. In addition, our markets are characterized by announcements of collaborative relationships involving our competitors. The existence or announcement of any such relationships could adversely affect our ability to attract and retain customers. As a result of the foregoing and other factors, we may not be able to compete effectively with current or future competitors, and competitive pressures that we face could materially harm our business.

We face competition in the domain name registry space from other gTLD and ccTLD registries that are competing for the business of entities and individuals that are seeking to obtain a domain name registration and/or establish a web presence. We have been designated as the registry operator for certain new gTLDs including certain IDN gTLDs; however, there is no guarantee that such new gTLDs will be as or more successful than the new gTLDs obtained by our competitors. For example, some of the new gTLDs, including our new gTLDs, may face additional universal acceptance and usability challenges in that current desktop and mobile device software does not ubiquitously recognize these new gTLDs and developers of desktop and mobile device software may be slow to adopt standards or support these gTLDs, even if demand for such products is strong. This is particularly true for IDN gTLDs, but applies to conventional gTLDs as well. As a result of these challenges, it is possible that resolution of domain names within some of these new gTLDs may be blocked within certain state or organizational environments, challenging universal resolvability of these strings and their general acceptance and usability on the internet.

See the "Competition" section in Part I, Item 1 of our Annual Report on Form 10-K for the year ended December 31, 2017 for further information.

We must establish and maintain strong relationships with registrars and their resellers to maintain their focus on marketing our products and services otherwise our Registry Service business could be harmed.

All of our domain name registrations occur through registrars. Registrars and their resellers utilize substantial marketing efforts to increase the demand and/or renewal rates for domain names as well as their own associated offerings. Consolidation in the registrar or reseller industry or changes in ownership, management, or strategy among individual registrars or resellers could result in significant changes to their business, operating model and cost structure. Such changes could include reduced marketing efforts or other operational changes that could adversely impact the demand and/or the renewal rates for domain names.

With the introduction of new gTLDs, many of our registrars have chosen to, and may continue to choose to, focus their short or long-term marketing efforts on these new offerings and/or reduce the prominence or visibility of our products and services on their e-commerce platforms. Our registrars and resellers sell domain name registrations of other competing registries, including the new gTLDs, and some also sell and support their own services for websites such as email, website hosting, as well as other services. Therefore, our registrars and resellers may be more motivated to sell to registrants to whom they can also market their own services. To the extent that registrars and their resellers focus more on selling and supporting their services and less on the registration and renewal of domain names in our TLDs, our revenues could be adversely impacted. Our ability to successfully market our services to, and build and maintain strong relationships with, new and existing registrars or resellers is a factor upon which successful operation of our business is dependent. If we are unable to keep a significant portion of their marketing efforts focused on selling registrations of domain names in our TLDs as opposed to other competing TLDs, including the new gTLDs, or their own services, our business could be harmed.

If we encounter system interruptions or failures, we could be exposed to liability and our reputation and business could suffer.

We depend on the uninterrupted operation of our various systems, secure data centers and other computer and communication networks. Our systems and operations are vulnerable to damage or interruption from:

- power loss, transmission cable cuts and other telecommunications failures;
- damage or interruption caused by fire, earthquake, and other natural disasters;
- attacks, including hacktivism, by miscreants or other nefarious actors;

Table of Contents

- computer viruses, software defects, or hardware defects, both in our systems and those of our service providers and suppliers;
- physical or electronic break-ins, sabotage, intentional acts of vandalism, terrorist attacks, unintentional mistakes or errors, and other events beyond our control;
- risks inherent in or arising from the terms and conditions of our agreements with service providers to operate our networks and data centers;
- state suppression of internet operations; and
- any failure to implement effective and timely remedial actions in response to any damage or interruption.

Most of the computing infrastructure for our Shared Registration System is located at, and most of our customer information is stored in, our facilities in New Castle, Delaware; Dulles, Virginia; and Fribourg, Switzerland. To the extent we are unable to partially or completely switch over to our primary alternate or tertiary sites, any damage or failure that causes interruptions in any of these facilities or our other computer and communications systems could materially harm our business. Although we carry insurance for property damage, we do not carry insurance or financial reserves for such interruptions, or for potential losses arising from terrorism.

In addition, our Registry Services business and certain of our other services depend on the secure and efficient operation of the internet connections to and from customers to our Shared Registration System residing in our secure data centers. These connections depend upon the secure and efficient operation of internet service providers, internet exchange point operators, and internet backbone service providers, some or all of which have had periodic operational problems or experienced outages in the past beyond our scope of control. In addition, if these service providers do not protect, maintain, improve, and reinvest in their networks or present inconsistent data regarding the DNS through their networks, our business could be harmed.

A failure in the operation or update of the root zone servers, the root zone file, the Root Zone Management System, the TLD name servers, or the TLD zone files that we operate, including, for example, our operation of the .gov registry, or other network functions, could result in a DNS resolution or other service outage or degradation; the deletion of one or more TLDs from the internet; the deletion of one or more second-level domain names from the internet for a period of time; or a misdirection of a domain name to a different server. A failure in the operation or update of the supporting cryptographic and other operational infrastructure that we maintain could result in similar consequences. A failure in the operation of our Shared Registration System could result in the inability of one or more registrars to register or maintain domain names for a period of time. In the event that a registrar has not implemented back-up services in conformance with industry best practices, the failure could result in permanent loss of transactions at the registrar during that period. Any of these problems or outages could create potential liability and exposure, including from a failure to meet our service level agreements in our Registry Agreements, and could decrease customer satisfaction, harming our business or resulting in adverse publicity and damage to our reputation that could adversely affect the market's perception of the security of e-commerce and communications over the internet as well as of the reliability of our services or call into question our ability to preserve the security and stability of the internet. Our operating results may be adversely affected as a result of unfavorable market, economic, social and political conditions.

An unfavorable global market, economic, social and political environment has impacted or may negatively impact, among other things:

- our customers' continued growth and development of their businesses, or their ability to maintain their businesses and continue as going concerns, which could affect demand for our products and services;
- current and future demand for our services, including decreases as a result of reduced spending on information technology and communications by our customers;
- price competition for our products and services;
- the price of our common stock;
- our liquidity and our associated ability to execute on any share repurchase plans; and
- our ability to service our debt, to obtain financing or assume new debt obligations.

In addition, to the extent that the market, economic, social and political environment impacts specific industry and geographic sectors in which many of our customers are concentrated, that may have a disproportionate negative

impact on our business.

29

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Table of Contents

Our international operations subject our business to additional economic, legal and political risks that could have an adverse impact on our revenues and business.

A significant portion of our revenues is derived from customers outside the U.S. Doing business in international markets has required and will continue to require significant management attention and resources. We may also need to tailor some of our services for a particular market and to enter into international distribution and operating relationships. We may fail to maintain our ability to conduct business, including potentially material business operations in some international locations, or we may not succeed in expanding our services into new international markets or expand our presence in existing markets. Failure to do so could materially harm our business. Moreover, local laws and customs in many countries differ significantly from those in the U.S. In many foreign countries, particularly in those with developing economies, it is common for others to engage in business practices that are prohibited by our internal policies and procedures or U.S. law or regulations applicable to us. There can be no assurance that our employees, contractors and agents will not take actions in violation of such policies, procedures, laws and/or regulations. Violations of laws, regulations or internal policies and procedures by our employees, contractors or agents could result in financial reporting problems, investigations, fines, penalties, or prohibition on the importation or exportation of our products and services and could have a material adverse effect on our business. In addition, we face risks inherent in doing business on an international basis, including, among others:

- competition with foreign companies or other domestic companies entering the foreign markets in which we operate, as well as foreign governments actively promoting their ccTLDs, which we do not operate;
- legal uncertainty regarding liability, enforcing our contracts, and compliance with foreign laws;
- economic tensions between governments and changes in international trade policies;
- tariffs and other trade barriers and restrictions;
- difficulties in staffing and managing foreign operations;
- currency fluctuations;
- potential problems associated with adapting our services to technical conditions existing in different countries;
- difficulty of verifying customer information, including complying with the customer verification requirements of certain countries;
- more stringent privacy and data localization policies in some foreign countries;
- additional vulnerability from terrorist groups targeting U.S. interests abroad;
- potentially conflicting or adverse tax consequences;
- reliance on third parties in foreign markets in which we only recently started doing business; and
- potential concerns of international customers and prospects regarding doing business with U.S. technology companies due to alleged U.S. government data collection policies.

We rely on our intellectual property rights to protect our proprietary assets, and any failure by us to protect or enforce, or any misappropriation of, our intellectual property could harm our business.

Our success depends in part on our internally developed technologies and related intellectual property. Despite our precautions, it may be possible for an external party to copy or otherwise obtain and use our intellectual property without authorization. Furthermore, the laws of foreign countries may not protect our proprietary rights in those countries to the same extent U.S. law protects these rights in the U.S. In addition, it is possible that others may independently develop substantially equivalent intellectual property. If we do not effectively protect our intellectual property, our business could suffer. Additionally, we have filed patent applications with respect to some of our technology in the U.S. Patent and Trademark Office and patent offices outside the U.S. Patents may not be awarded with respect to these applications and even if such patents are awarded, third parties may seek to oppose or otherwise challenge our patents, and such patents' scope may differ significantly from what was requested in the patent applications and may not provide us with sufficient protection of our intellectual property. In the future, we may have to resort to litigation to enforce and protect our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. This type of litigation is inherently unpredictable and, regardless of its outcome, could result in substantial costs and diversion of management attention and technical resources. Some of the software and protocols used in our business are based on standards set by standards setting organizations such as the Internet Engineering Task Force. To the extent any of our patents are considered "standards

essential patents,” in some cases we may be required to license such patents to our competitors on reasonable and non-discriminatory terms.

We also license externally developed technology that is used in some of our products and services to perform key functions. These externally developed technology licenses may not continue to be available to us on commercially reasonable

30

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Table of Contents

terms or at all. The loss of or our inability to obtain or maintain any of these technology licenses could hinder or increase the cost of our launching new products and services, entering into new markets and/or otherwise harm our business. Some of the software and protocols used in our Registry Services business are in the public domain or may otherwise become publicly available, which means that such software and protocols are equally available to our competitors.

We rely on the strength of our Verisign brand to help differentiate Verisign in the marketing of our products. Dilution of the strength of our brand could harm our business. We are at risk that we will be unable to fully register, build equity in, or enforce the Verisign logo in all markets where Verisign products and services are sold. In addition, in the U.S. and most other countries, word marks solely for TLDs have currently not been successfully registered as trademarks. Accordingly, we may not be able to fully realize or maintain the value of these intellectual property assets.

We could become subject to claims of infringement of intellectual property of others, which could be costly to defend and could harm our business.

We cannot be certain that we do not and will not infringe the intellectual property rights of others. Claims relating to infringement of intellectual property of others or other similar claims have been made against us in the past and could be made against us in the future. It is possible that we could become subject to additional claims for infringement of the intellectual property of other parties. The international use of our logo could present additional potential risks for external party claims of infringement. Any claims, with or without merit, could be time consuming, result in costly litigation and diversion of technical and management personnel attention, cause delays in our business activities generally, or require us to develop a non-infringing logo or technology or enter into royalty or licensing agreements. Royalty or licensing agreements, if required, may not be available on acceptable terms or at all. If a successful claim of infringement were made against us, we could be required to pay damages or have portions of our business enjoined. If we could not identify and adopt an alternative non-infringing logo, develop non-infringing technology or license the infringed or similar technology on a timely and cost-effective basis, our business could be harmed.

An external party could claim that the technology we license from other parties infringes a patent or other proprietary right. Litigation between the licensor and a third party or between us and a third party could lead to royalty obligations for which we are not indemnified or for which indemnification is insufficient, or we may not be able to obtain any additional license on commercially reasonable terms or at all.

In addition, legal standards relating to the validity, enforceability, and scope of protection of intellectual property rights in internet-related businesses, including patents related to software and business methods, are uncertain and evolving. Because of the growth of the internet and internet-related businesses, patent applications are continuously being filed in connection with internet-related technology. There are a significant number of U.S. and foreign patents and patent applications in our areas of interest, and we believe that there has been, and is likely to continue to be, significant litigation in the industry regarding patent and other intellectual property rights.

We could become involved in claims, lawsuits, audits or investigations that may result in adverse outcomes.

In addition to possible intellectual property litigation and infringement claims, we are, and may in the future, become involved in other claims, lawsuits, audits and investigations, including with respect to the RZMA. Such proceedings may initially be viewed as immaterial but could prove to be material. Litigation is inherently unpredictable, and excessive verdicts do occur. Adverse outcomes in lawsuits, audits and investigations could result in significant monetary damages, including indemnification payments, or injunctive relief that could adversely affect our ability to conduct our business and may have a material adverse effect on our financial condition, results of operations and cash flows. Given the inherent uncertainties in litigation, even when we are able to reasonably estimate the amount of possible loss or range of loss and therefore record an aggregate litigation accrual for probable and reasonably estimable loss contingencies, the accrual may change in the future due to new developments or changes in approach. In addition, such claims, lawsuits, audits and investigations could involve significant expense and diversion of management's attention and resources from other matters.

We continue to explore new strategic initiatives, the pursuit of any of which may pose significant risks and could have a material adverse effect on our business, financial condition and results of operations.

We explore possible strategic initiatives which may include, among other things, the investment in, and the pursuit of, new revenue streams, services or products, changes to our offerings, initiatives to leverage our patent portfolio, back-end registry services and IDN gTLDs. In addition, we have evaluated and are pursuing and will continue to evaluate and pursue acquisitions of TLDs that are currently in operation and those that have not yet been awarded or delegated as long as they support our growth strategy.

Any such strategic initiative may involve a number of risks, including: the diversion of our management's attention from our existing business to develop the initiative, related operations and any requisite personnel; possible regulatory scrutiny or third-party claims; possible material adverse effects on our results of operations during and after the development process; our

Table of Contents

possible inability to achieve the intended objectives of the initiative; as well as damage to our reputation if we are unsuccessful in pursuing a strategic initiative. Such initiatives may result in a reduction of cash or increased costs. We may not be able to successfully or profitably develop, integrate, operate, maintain and manage any such initiative and the related operations or employees in a timely manner or at all. Furthermore, under our agreements with ICANN, we are subject to certain restrictions in the operation of .com, .net, .name and other TLDs, including required ICANN approval of new registry services for such TLDs. If any new initiative requires ICANN review or ICANN determines that such a review is required, we cannot predict whether this process will prevent us from implementing the initiative in a timely manner or at all. Any strategic initiative to leverage our patent portfolio will likely increase litigation risks from potential licensees and we may have to resort to litigation to enforce our intellectual property rights.

We depend on key employees to manage our business effectively, and we may face difficulty attracting and retaining qualified leaders.

We operate in a unique competitive and highly regulated environment, and we depend on the knowledge, experience, and performance of our senior management team and other key employees in this regard and otherwise. We periodically experience changes in our management team. If we are unable to attract, integrate, retain and motivate these key individuals as well as other highly skilled employees, and implement succession plans for these personnel, our business may suffer. For example, our service products are highly technical and require individuals skilled and knowledgeable in unique platforms, operating systems and software development tools.

Changes in, or interpretations of, tax rules and regulations or our tax positions may adversely affect our income taxes. We are subject to income taxes in both the U.S. and numerous foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. Our effective tax rates may fluctuate significantly on a quarterly basis because of a variety of factors, including changes in the mix of earnings and losses in countries with differing statutory tax rates, changes in our business or structure, or the expiration of or disputes about certain tax agreements in a particular country. We are subject to audit by various tax authorities. In accordance with U.S. GAAP, we recognize income tax benefits, net of required valuation allowances and accrual for uncertain tax positions. For example, we claimed a worthless stock deduction on our 2013 federal income tax return and recorded a net income tax benefit of \$380.1 million. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different than that which is reflected in historical income tax provisions and accruals. Should additional taxes be assessed as a result of an audit or litigation, an adverse effect on our results of operations, financial condition and cash flows in the period or periods for which that determination is made could result.

The Tax Cuts and Jobs Act (“Tax Act”) was enacted on December 22, 2017. The Tax Act significantly revamped U.S. taxation of corporations, including a reduction of the federal income tax rate from 35% to 21%, a limitation on interest deductibility, and a new tax regime for foreign earnings. Our decision to redeem the convertible debentures, the new U.S. taxes on accumulated and future foreign earnings, other adverse changes resulting from the Tax Act, or a change in the mix of domestic and foreign earnings, might offset the benefit from the reduced tax rate, and our future effective tax rates and/or cash taxes may increase, even significantly, or not decrease much, compared to recent or historical trends. Many of the provisions of the Tax Act are highly complex and may be subject to further interpretive guidance from the IRS or others. Some of the provisions of the Tax Act may be changed by a future Congress or challenged by the World Trade Organization (“WTO”) or be subject to trade or tax retaliation by other countries. Although we cannot predict the nature or outcome of such future interpretive guidance, or actions by a future Congress, WTO or other countries, they could adversely impact our financial condition, results of operations and cash flows. Income tax expense on accumulated foreign earnings recorded as a result of the Tax Act is a provisional amount and reflects our current best estimate, which may be adjusted over the course of 2018 and materially impact our results of operations. Our marketable securities portfolio could experience a decline in market value, which could materially and adversely affect our financial results.

As of September 30, 2018, we had \$1.19 billion in cash, cash equivalents, marketable securities and restricted cash, of which \$947.4 million was invested in marketable securities. The marketable securities consist primarily of debt securities issued by the U.S. Treasury meeting the criteria of our investment policy, which is focused on the

preservation of our capital through the investment in investment grade securities. We currently do not use derivative financial instruments to adjust our investment portfolio risk or income profile.

## Table of Contents

These investments, as well as any cash deposited in bank accounts, are subject to general credit, liquidity, market and interest rate risks, which may be exacerbated by financial market credit and liquidity events. If the global credit or liquidity market deteriorates or other events negatively impact the market for U.S. Treasury securities, our investment portfolio may be impacted and we could determine that some of our investments have experienced an other-than-temporary decline in fair value, requiring an impairment charge which could adversely impact our results of operations and cash flows.

We are subject to the risks of owning real property.

We own the land and building in Reston, Virginia, which constitutes our headquarters facility. Ownership of this property, as well as our data centers in Dulles, Virginia and New Castle, Delaware, may subject us to risks, including: adverse changes in the value of the properties, due to interest rate changes, changes in the commercial property markets, easements or other encumbrances, a government exercising its right of eminent domain, or other factors; ongoing maintenance expenses and costs of improvements; the possible need for structural improvements in order to comply with environmental, health and safety, zoning, seismic, disability law, or other requirements; the possibility of environmental contamination or notices of violation from federal or state environmental agencies; and possible disputes with neighboring owners, tenants, service providers or others.

We have anti-takeover protections that may discourage, delay or prevent a change in control that could benefit our stockholders.

Our amended and restated Certificate of Incorporation and Bylaws contain provisions that could make it more difficult for an outside party to acquire us without the consent of our Board of Directors (“Board”). These provisions include: our stockholders may take action only at a duly called meeting and not by written consent; special meetings of our stockholders may be called only by the chairman of the board of directors, the president, our Board, or the secretary (acting as a representative of the stockholders) whenever a stockholder or group of stockholders owning at least twenty-five percent (25%) in the aggregate of the capital stock issued, outstanding and entitled to vote, and who held that amount in a net long position continuously for at least one year, so request in writing; vacancies on our Board can be filled until the next annual meeting of stockholders by a majority of directors then in office; and our Board has the ability to designate the terms of and issue new series of preferred stock without stockholder approval.

In addition, Section 203 of the General Corporation Law of Delaware prohibits a publicly held Delaware corporation from engaging in a business combination with an interested stockholder, generally a person which together with its affiliates owns or within the last three years has owned 15% or more of our voting stock, for a period of three years after the date of the transaction in which the person became an interested stockholder, unless in the same transaction the interested stockholder acquired 85% ownership of our voting stock (excluding certain shares) or the business combination is approved in a prescribed manner. Section 203 therefore may impact the ability of an acquirer to complete an acquisition of us after a successful tender offer and accordingly could discourage, delay or prevent an acquirer from making an unsolicited offer without the approval of our Board.

Our financial condition and results of operations could be adversely affected if we do not effectively manage our indebtedness.

We have a significant amount of outstanding debt, and we periodically reassess our capital structure and may incur additional indebtedness in the future. Our substantial indebtedness, including any future indebtedness, requires us to dedicate a significant portion of our cash flow from operations or to arrange alternative liquidity sources to make principal and interest payments, when due, or to repurchase or settle our debt, if triggered, by certain corporate events, or certain events of default. It could also limit our flexibility in planning for or reacting to changes in our business and our industry, or make required capital expenditures and investments in our business; make it difficult or more expensive to refinance our debt or obtain new debt; trigger an event of default; and increase our vulnerability to adverse changes in general economic and industry conditions. Some of our debt contains covenants which may limit

our operating flexibility, including restrictions on share repurchases, dividends, prepayment or repurchase of debt, acquisitions, disposing of assets, if we do not continue to meet certain financial ratios. Any rating assigned to our debt securities could be lowered or withdrawn by a rating agency, which could make it more difficult or more expensive for us to obtain additional debt financing in the future. The occurrence of any of the foregoing factors could have a material adverse effect on our business, cash flows, results of operations and financial condition.

Table of Contents

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table presents the share repurchase activity during the three months ended September 30, 2018:

|                        | Total Number<br>of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share<br>Purchased | Total Number<br>of Shares<br>Purchased as<br>Part of Publicly<br>Announced<br>Plans or<br>Programs (1) | Approximate<br>Dollar Value of<br>Shares That<br>May<br>Yet Be<br>Purchased<br>Under the Plans<br>or<br>Programs (1) |
|------------------------|---|---|--|--|
|                        | (Shares in thousands)                     |   |  |  |
| July 1 - 31, 2018      | 402                                       | \$ 145.20                                       | 402  | \$754.9 million  |
| August 1 - 31, 2018    | 418                                       | \$ 152.68                                       | 418  | \$691.1 million  |
| September 1 - 30, 2018 | 330                                       | \$ 160.16                                       | 330  | \$638.3 million  |
|                        | 1,150                                     |   | 1,150  |  |

(1) Effective February 8, 2018, our Board authorized the repurchase of approximately \$585.8 million of our common stock, in addition to the \$414.2 million of our common stock remaining available for repurchase under the previous share repurchase program, for a total repurchase authorization of up to \$1.0 billion of our common stock. The share repurchase program has no expiration date. Purchases made under the program can be made through open market transactions, block purchases, accelerated share repurchase agreements or other negotiated transactions.

## ITEM 5. OTHER INFORMATION

On October 24, 2018, Verisign entered into an agreement (the "Purchase Agreement") with NeuStar, Inc., a Delaware corporation ("Neustar" or "Buyer"), to sell the rights, economic benefits, and obligations, in all customer contracts related to its Security Services business. The transaction includes the sale of customer agreements related to Verisign's DDoS Protection, Managed DNS, DNS Firewall, and Recursive DNS services to Buyer. The purchase price, subject to a cap of \$120.0 million, consists of a payment of \$50.0 million, due at the time of closing, plus an additional contingent amount, due after the first anniversary of closing. The additional contingent amount, which cannot be negative, is based upon, among other things, the successful transition of customers to Neustar during the 12-month period following closing. In addition, Verisign has agreed not to compete with the divested business for a period of 36 months. The Purchase Agreement contains customary representations and warranties, closing conditions and indemnification provisions. The closing is expected to occur shortly following the receipt of customary regulatory approval.

Table of Contents

## ITEM 6. EXHIBITS

As required under Item 6—Exhibits, the exhibits filed as part of this report are provided in this separate section. The exhibits included in this section are as follows:

| Exhibit<br>Number | Exhibit Description   | Incorporated by<br>Reference<br>FormDateNumber | Filed<br>Herewith |
|-------------------|---|--|-------------------|
| 31.01             | <u>Certification of Principal Executive Officer pursuant to Exchange Act Rule 13a-14(a).</u>  |  | X                 |
| 31.02             | <u>Certification of Principal Financial Officer pursuant to Exchange Act Rule 13a-14(a).</u>  |  | X                 |
| 32.01             | <u>Certification of Principal Executive Officer pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the U.S. Code (18 U.S.C. 1350). *</u> |  | X                 |
| 32.02             | <u>Certification of Principal Financial Officer pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the U.S. Code (18 U.S.C. 1350). *</u> |  | X                 |
| 101.INS           | XBRL Instance Document  |  | X                 |
| 101.SCH           | XBRL Taxonomy Extension Schema  |  | X                 |
| 101.CAL           | XBRL Taxonomy Extension Calculation Linkbase  |  | X                 |
| 101.DEF           | XBRL Taxonomy Extension Definition Linkbase   |  | X                 |
| 101.LAB           | XBRL Taxonomy Extension Label Linkbase  |  | X                 |
| 101.PRE           | XBRL Taxonomy Extension Presentation Linkbase   |  | X                 |

As contemplated by SEC Release No. 33-8212, these exhibits are furnished with this Quarterly Report on Form \*10-Q and are not deemed filed with the SEC and are not incorporated by reference in any filing of VeriSign, Inc. under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in such filings.

Table of Contents

SIGNATURES

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

VERISIGN, INC.

Date: October 25, 2018 By: /S/ D. JAMES BIDZOS  
D. James Bidzos  
Chief Executive Officer

Date: October 25, 2018 By: /S/ GEORGE E. KILGUSS, III  
George E. Kilguss, III  
Chief Financial Officer