

GLOBAL MED TECHNOLOGIES INC
Form 10-Q
May 13, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1934
For the Quarterly Period Ended March 31, 2008.

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

GLOBAL MED TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

Colorado

(State or other jurisdiction of
incorporation or organization)

0-22083

(Commission File No.)

84-1116894

(I.R.S. Employer
Identification No.)

12600 West Colfax, Suite C-420, Lakewood, Coloardo,

(Address of principal executive offices)

80215

(Zip Code)

(303) 238-2000

(Registrant's telephone number, including area code)

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 the filing requirements for at least the past 90 days.

Yes No

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

Large Accelerated Filer

Non-Accelerated Filer

Accelerated Filer

Smaller Reporting Company

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

As of May 6, 2008 the registrant had 27,829,153 common shares outstanding.

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FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2008
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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2008	December 31, 2007
	(Unaudited)	
<u>ASSETS</u>		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 7,385	\$ 6,748
Accounts receivable-trade, net	2,332	3,029
Accrued revenues, net	697	822
Prepaid expenses and other assets	529	316
Deferred tax asset	538	740
Total current assets	11,481	11,655
Equipment, furniture and fixtures, net	375	342
Capitalized Software Development Costs	228	173
Total assets	\$ 12,084	\$ 12,170

See accompanying notes to unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)
(In thousands)

	March 31, 2008 (Unaudited)	December 31, 2007
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 784	\$ 322
Accrued expenses and other current liabilities	2,629	3,377
Deferred revenue	4,198	4,475
Capital lease obligation and note payable, current portions	53	36
Total current liabilities	7,664	8,210
Litigation accrual	1,004	1,004
Capital lease obligation and note payable, less current portions	--	26
Total liabilities	8,668	9,240
COMMITMENT AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Convertible Preferred Stock Series A, \$.01 par value:		
Authorized shares 100; 7 and 8 outstanding at March 31, 2008 and December 31, 2007, respectively	7,460	7,735
Convertible Preferred Stock Series BB, \$.01 par value:		
Authorized shares 675; none outstanding	---	---
Preferred stock, \$.01 par value: Authorized shares - 5,725;		
None issued or outstanding	---	---
Common stock, \$.01 par value: Authorized shares 90,000; Issued and outstanding shares 27,779 and 26,674 at March 31, 2008 and December 31, 2007, respectively		
	278	267
Additional paid-in capital	54,678	54,288
Accumulated deficit	(59,000)	(59,360)
Total stockholders' equity	3,416	2,930
Total liabilities and stockholders' equity	\$ 12,084	\$ 12,170

See accompanying notes to unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share information)

	Three months ended September 30,	
	2008 (Unaudited)	2007 (Unaudited)
Revenues	\$ 4,593	\$ 3,719
Cost of revenues	1,558	1,139
Gross profit	3,035	2,580
OPERATING EXPENSES:		
General and administrative	919	806
Sales and marketing	704	516
Research and development	741	924
Depreciation and software amortization	46	38
Total operating expenses	2,410	2,284
Income from operations	625	296
OTHER INCOME (EXPENSE):		
Interest income	34	16
Interest expense	(4)	(3)
Total other income (expense)	30	13
Income before provision for income tax	655	309
Income tax expense	(295)	(22)
Net income	\$ 360	\$ 287
Basic and Diluted net income per common share		
Basic	\$ 0.01	\$ 0.01
Diluted	\$ 0.01	\$ 0.01
Weighted average number of common shares outstanding		
Basic	26,935	23,212
Diluted	44,915	38,561

See accompanying notes to unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDER S EQUITY
(In thousands)

	Preferred Stock		Common Stock		Additional	Accumulated	Total
	Shares	Amount	Shares	Amount	Paid-in Capital	Deficit	
Balances, December 31, 2007	8	\$ 7,735	26,674	\$ 267	\$ 54,288	\$ (59,360)	\$ 2,930
Expense associated with issuance of options for services to employees or consultants, (unaudited)	---	---	---	---	106	---	106
Exercise of options (unaudited)	---	---	28	---	20	---	20
Cashless exercise of warrant	---	---	695	7	(7)	---	---
Conversion of Series A Preferred Stock to Common shares (unaudited)	(1)	(275)	382	4	271	---	---
Net income (unaudited)	---	---	---	---	--	360	360
Balances, March 31, 2008 (unaudited)	7	\$ 7,460	27,779	\$ 278	\$ 54,678	\$ (59,000)	\$ 3,416

See accompanying notes to unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Three months ended	
	March 31,	
	2008	2007
	(Unaudited)	(Unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 360	\$ 287
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of software development costs	46	38
Bad debt expense	18	47
Common stock, options and warrants issued for services and other, net	106	51
Changes in operating assets and liabilities:		
Accounts receivable-trade, net	679	1,026
Accrued revenues, net	125	(97)
Prepaid expenses and other assets	(106)	(52)
Deferred tax asset	293	---
Accounts payable	462	(83)
Accrued expenses and other current liabilities	(839)	(254)
Deferred revenue	(277)	(459)
Net cash provided by operating activities	867	504
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of equipment, furniture and fixtures	(75)	(37)
Capitalized software development	(59)	---
Pre-acquisition costs	(107)	---
Net cash (used in) provided by investing activities	(241)	(37)

See accompanying notes to the unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(CONTINUED)
(In thousands)

	Three months ended	
	March 31, 2008	
	2008	2007
	(Unaudited)	(Unaudited)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowing, notes payable and principal payments on debt and capital lease obligations	\$ (9)	\$ (8)
Exercise of options for cash	20	---
Net cash provided by (used in) financing activities	11	(8)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	637	459
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	6,748	2,554
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 7,385	\$ 3,013
SUPPLEMENTAL DISCLOSURES		
Cash paid for the period:		
Interest on note payable and capital lease	\$ 4	\$ 3
Income taxes	\$ 745	\$ 175
Non-cash financing activity:		
Conversion of Series A Preferred Stock to common shares	\$ 275	\$ --

See accompanying notes to the unaudited condensed consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2008

1. BASIS OF PRESENTATION

Basis of Consolidation

The accompanying unaudited condensed consolidated financial statements of Global Med Technologies, Inc. and Subsidiary (the Company or Global Med) have been prepared by management in accordance with generally accepted accounting principles for interim financial information and with the regulations of the Securities and Exchange Commission. Accordingly, they do not include all information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of only normal recurring adjustments) considered necessary for a fair presentation of their financial position as of March 31, 2008 and the results of their operations and cash flows for the three months ended March 31, 2008 and 2007 have been included.

While management believes the disclosures presented are adequate to prevent misleading information, it is suggested that the accompanying unaudited consolidated financial statements be read in conjunction with the audited consolidated financial statements and the notes thereto contained in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2007, as filed with the Securities and Exchange Commission. The interim results of operations for the three months ended March 31, 2008 are not necessarily indicative of the results that may be expected for any other interim period of 2008 or for the year ending December 31, 2008.

Recent Development

On March 26, 2008, the Company signed a Stock Purchase Agreement (the Purchase Agreement) to acquire Inlog, SA, a French company, and its subsidiaries (Inlog) for a maximum of \$11.5 million in a combination of cash, stock and earnout payments. Inlog, based in Lyon, France, is a leading European provider of donor center and transfusion information management systems as well as laboratory information systems and other ancillary medical software systems. Prior to closing, the Purchase Agreement requires that the buyer, Global Med, be able to obtain financing acceptable to the buyer, the seller, Inlog, deliver U.S. GAAP financials to the buyer, and the Company's Board of Directors finalize the acquisition, at their sole discretion. None of these conditions precedent to closing have occurred. There can be no assurance that the Company will be able to obtain the financing necessary for this acquisition on terms acceptable to it or at all. In the event the acquisition occurs, the Company plans to finance this transaction through a combination of existing cash, new debt, and the issuance of additional equity to the owners of Inlog.

Inlog's product line consists of five (5) primary products: EdgeBlood (for the donor center marketplace), EdgeTrace (for the hospital transfusion marketplace), EdgeLab (a LIS), EdgeCell (cellular therapy for tissue banks, stem cell centers and cord blood centers) and SAPA (supports regulatory compliance and document management). Inlog is ISO 9001:2000 certified and its products have received the NF/ISO 25051/12119 certification guaranteeing the highest level of quality regarding the design, testing and validation of its software, its documentation quality and the quality of its product support and maintenance.

Inlog has been developing, implementing, and supporting its blood bank information management solutions since 1992 and supplies over 700 sites in fifteen (15) countries with its products. Inlog recently completed the national installation of its EdgeBlood product in France. All 2.5 million French blood donations flow through Inlog's products in France including blood collections, infectious disease testing, component manufacturing and distribution. In addition to France, Inlog provides its software applications in Germany, Austria, Belgium and Switzerland, as well as installations in Greece and Monaco.

In the event that the Company and Inlog finalize the aforementioned transaction, the Company's software applications will have a presence in twenty (20) countries (including the United States, Canada, Caribbean, European Union, Africa, French Polynesia, and New Caledonia). The Company believes that the acquisition of Inlog is strategically important as Inlog's existing international marketplace may provide a platform for the Company's continued growth.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2008

Critical Accounting Policies

The Company's software products typically have warranties. These warranties generally require that the Company make changes to the software due to defects or other factors that might impact the Company's regulatory compliance after the date of product shipment. Generally, the Company does not accrue for product warranties but defers revenue recognition on a component of the original software fee that is associated with the correction of errors and continued updates to regulatory requirements during the warranty period. The Company believes this allocation adequately reflects the timing of revenues and costs associated with these warranties.

During the three months ended March 31, 2008, the Company increased its accounts receivable reserves by \$18 thousand to \$199 thousand. The Company believes that its reserve for accounts receivable is appropriate. The Company may make changes to its revenue recognition practices with respect to specific customers as its assessment of collectability changes. These changes are typically not material to the financial statements.

For those customer accounts for which revenue has been earned with the exception that collectability of the amount is not deemed reasonably assured, the Company recognizes revenues related to these accounts in the period cash is received.

Significant Customers

During the three months ended March 31, 2008 and 2007, there were no customers accounting for more than 10% of revenues. Although the Company had no individual customers accounting for more than 10% of revenues, one of the Company's marketing partners that sells the Company's products directly to its customers accounted for 26.1% and 31.2% of revenues for the three months ended March 31, 2008 and 2007, respectively. In addition, this same marketing partner accounted for 29.5% and 56.3% of gross accounts receivable as of March 31, 2008 and December 31, 2007, respectively.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is required to the extent any deferred tax assets may not be realizable. While the Company has net operating loss (NOLs) carryforwards related to certain tax jurisdictions, the Company has limited or no NOLs in others.

Prior to the fourth quarter of 2007, the deferred tax asset related to the net operating loss carry forward was fully reserved by a valuation allowance due to the uncertainty of the Company generating future taxable income. During the fourth quarter of 2007, the Company reassessed its valuation allowance and decreased it by \$740 thousand to reflect higher than anticipated net deferred tax asset utilization. As a result of this reassessment in the fourth quarter of 2007 and the reduction in the valuation allowance, the Company's provision for income taxes increased significantly for the three months ended March 31, 2008 when compared with the comparable period in 2007.

Effective January 2007, the Company adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, or FIN 48. In accordance with FIN 48, the Company is required to disclose its practice related to recognizing interest and/or penalties related to tax positions taken with uncertainty. The Company records interest and penalties related to tax positions with uncertainty in income tax expense. The Company had no such interest or penalties for the three months ended March 31, 2008 and 2007.

Recently Issued Accounting Standards

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The adoption of SFAS No. 157 did not have a material impact on our consolidated financial statements.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
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MARCH 31, 2008

Pre-Acquisition Costs

As of March 31, 2008, the Company had capitalized \$255 thousand of pre-acquisition costs related to Inlog. These costs are in the Company's balance sheet in prepaid expenses and other assets. In the event that the acquisition is unsuccessful, the Company would be required to expense these costs. Expensing these costs could have a material impact on the Company's operating results for that period. See the *Recent Developments* section of this note 1 for further discussion related to this potential acquisition.

In February 2008, the FASB issued FASB Staff Position No. 157-2, *Effective Date of FASB Statement No. 157* (FSP 157-2), which delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities. Therefore, the Company has delayed application of SFAS 157 to its nonfinancial assets and nonfinancial liabilities, which include assets and liabilities acquired in connection with a business combination, goodwill, intangible assets and asset retirement obligations recognized in connection with final capping, closure and post-closure landfill obligations, until January 1, 2009. The Company is currently evaluating the impact of SFAS 157 for nonfinancial assets and liabilities on the Company's financial position and results of operations.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 permits companies to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The adoption of SFAS No. 159 did not have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (R), *Business Combinations*, and SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements*. SFAS No. 141 (R) requires an acquirer to measure the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at their fair values on the acquisition date, with goodwill being the excess value over the net identifiable assets acquired. SFAS No. 160 clarifies that a noncontrolling interest in a subsidiary should be reported as equity in the consolidated financial statements. The calculation of earnings per share will continue to be based on income amounts attributable to the parent. SFAS No. 141 (R) and SFAS No. 160 are effective for financial statements issued for fiscal years beginning after December 15, 2008. Early adoption is prohibited. The Company has not yet determined the effect on our consolidated financial statements, if any, upon adoption of SFAS No. 141 (R) or SFAS No. 160.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements - an Amendment of ARB No. 51* (SFAS 160), which establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS No. 160 also requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. It also requires disclosure, on the face of the consolidated statement of income, of the amounts of consolidated net income attributable to the parent and to the noncontrolling interest. SFAS No. 160 also provides guidance when a subsidiary is deconsolidated and requires expanded disclosures in the consolidated financial statements that clearly identify and distinguish between the interests of the parent's owners and the interests of the noncontrolling owners of a subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The Company is currently evaluating the impact this statement will have on its financial position and results of operations.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* (SFAS 161), which amends and expands the disclosure requirements of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments; (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations; and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments and disclosures about credit-risk-related contingent features in derivative instruments. This statement applies to all entities and all derivative instruments. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company has not yet determined the effect on our consolidated financial statements, if any, upon adoption of SFAS No. 161.

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**GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
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MARCH 31, 2008**

Reclassifications

Certain prior period amounts have been reclassified to conform with the current period presentation.

2. PEOPLEMED.COM, INC.

During 1999, Global Med formed a subsidiary, PeopleMed.com, Inc. (PeopleMed), a Colorado corporation, which is approximately 83% owned by the Company, to develop a software application designed to give HMO providers and other third party payers access to clinical information for chronic disease patients. This application allows doctors and other medical employees access to a patient's history. Late in 2007, PeopleMed began offering Validation Services. Validation Services include documenting and testing systems to enable the customer to conform their use of the software system to conform with regulations and requirements. The remaining 17% of PeopleMed is owned by third parties and certain officers and directors of Global Med. There is no minority interest reflected in the March 31, 2008 or December 31, 2007 balance sheets because PeopleMed had a stockholders' deficit as of those dates.

3. COMMITMENTS AND CONTINGENCIES

Legal Proceedings

In September 2002, Global Med filed a lawsuit against Donnie L. Jackson, Jr., Global Med's former Vice President of Sales and Marketing. Global Med alleges, among other things, that prior to his resignation in July 2002 Mr. Jackson misappropriated certain trade secrets of Global Med. After leaving Global Med, Mr. Jackson became a management employee of one of Global Med's competitors. On March 30, 2005, the Superior Court of the State of California in and for the County of El Dorado granted the motion for summary judgment for Donnie L. Jackson, Jr. On September 1, 2005, the Company deposited \$1.004 million with the Superior Court in the State of California in the County of El Dorado. This deposit represented potential fees and attorneys' costs the Company could be required to pay in the event the Company did not prevail on appeal. The \$1.004 million is classified as a Deposit in escrow on the Company's balance sheet as of December 31, 2006. Based on external evidence and the advice of legal counsel, the Company determined that it was more likely than not that the Company would be required to pay the \$1.004 million. As a result, the Company expensed the amount of the Deposit in escrow and set up a liability for \$1.004 million during 2005. In December 2006, the summary judgment was reversed by the California Court of Appeals and the matter was remanded to the trial court. In May 2007, the \$1.004 million Deposit in escrow was returned to the Company along with \$80 thousand in accrued interest. As of March 31, 2008, the Company reclassified the Deposit in escrow as a long-term liability based on the prevailing circumstances of the case. As of March 31, 2008, the Company has determined that the return of the deposit and other circumstances surrounding the case prohibit the Company from reversing the accrual of the \$1.004 million under SFAS 5, Accounting for Contingencies. The Company intends to continually re-evaluate the facts and circumstances surrounding the case and the related accounting.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
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4. STOCK-BASED COMPENSATION

The Company adopted SFAS No. 123R, Share Based Payment (SFAS 123R), on January 1, 2006. SFAS 123R requires all share-based payments, including grants of stock options, to be recognized in the income statement as an operating expense, based on their fair values.

Prior to adoption of SFAS 123R, Global Med accounted for stock-based employee compensation under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB). The Company has applied the modified prospective method in adopting SFAS 123R, and as a result, periods prior to the adoption of SFAS 123R have not been restated.

The following summarizes the activity of the Company's stock options for the three months ended March 31, 2008:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Number of shares under option:				
Outstanding at January 1, 2008	10,823,602	\$ 0.82		
Granted	---	---		
Exercised	(28,000)	0.69		
Canceled or expired	---	---		
Outstanding at March 31, 2008	10,795,602	\$ 0.81	3.9	\$ 8,798,082
Exercisable at March 31, 2008	9,783,824	\$ 0.79	3.7	\$ 7,827,3587

There were 28 thousand options exercised during the three months ended March 31, 2008. The total intrinsic value of options exercised during the three-months ended March 31, 2008 was approximately \$20 thousand.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2008

The following summarizes the activity of the Company's stock options that have not vested for the three months ended March 31, 2008.

	Shares	Weighted Average Fair Value
	1,117,703	\$ 0.93
Nonvested at January 1, 2008		
Granted	---	---
Canceled or expired	---	---
Vested	105,925	0.96
Nonvested at March 31, 2008	1,011,778	\$ 0.91

As of March 31, 2008, there was \$919 thousand of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under existing stock option plans. This cost is expected to be recognized over a weighted-average period of 4 years. The total measurement fair value of shares vested during the three months ended March 31, 2008 and 2007 was \$106 thousand and \$51 thousand, respectively.

The Black-Scholes option pricing model is used by the Company to determine the weighted average fair value of options. The fair value of options at date of grant and the assumptions utilized to determine such values are indicated in the following table:

	Three Months Ended March 31,	
	2008	2007
Weighted average fair value at date of grant for options granted during the period	\$ ---	\$ 158,000
Risk-free interest rates	---	4.56%
Expected stock price volatility	---	3.29%
Expected dividend yield	---	0

No options were granted during the three months ended March 31, 2008.

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GLOBAL MED TECHNOLOGIES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
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Under SFAS 123R forfeitures are estimated at the time of valuation and reduce expense ratably over the vesting period. This estimate is adjusted periodically based on the extent to which actual forfeitures differ, or are expected to differ, from the previous estimate. Under SFAS 123 and APB 25, the Company elected to account for forfeitures when awards were actually forfeited, at which time all previous pro forma expense was reversed to reduce pro forma expense for that period. As of March 31, 2008, the Company anticipates all outstanding options will vest.

6. NET INCOME PER SHARE

Basic earnings per share is computed by dividing the net income by the weighted average number of common shares outstanding for the period. Diluted shares outstanding is calculated factoring in stock options, and warrants outstanding, and their equivalents are included in diluted computations through the treasury stock method unless they are antidilutive. Convertible securities are included in diluted computations through the if converted method unless they are antidilutive.

The following tables set forth the computation of basic and diluted earnings per share for the three months ended March 31, 2008 and 2007, respectively, (in thousands):

Three Months Ended March 31,	2008	2007
Weighted average number of shares used in the basic		
Earnings per share computation	26,935	23,212
Effect of dilutive securities:		
Common stock options	2,965	838
Common stock warrants	4,414	657
Preferred stock convertible securities	10,601	13,854
Dilutive securities	17,980	15,349
Adjusted weighted average number of shares used in		
diluted earnings per share computation	44,915	38,561

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ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward Looking Statements

Certain statements in this Quarterly Report on Form 10-QSB are forward-looking in nature. These statements can be identified by the use of forward-looking terminology such as believes, expects, may, will, should, anticipates, or negative comparable terminology or by discussion of strategy.

The risks and uncertainties are discussed in greater detail in the Company's other filings with the Securities and Exchange Commission, including, most recently, its Annual Report on Form 10-KSB. There may be additional risks of which the Company is not presently aware or that it currently believes are immaterial which could have an adverse impact its business. The Company makes no commitment to revise or update any forward-looking statement in order to reflect events or circumstances that may change.

Overview/Outlook

The Company posted record revenues for the three months ended March 31, 2008 of 4.593 million. In addition for the three months ended March 31, 2008, the Company posted operating income of \$625 thousand and operating cash flows of \$867 thousand.

Global Med designs, develops, markets and supports information management software products for blood banks, hospitals, centralized transfusion centers and other health care related facilities. Revenues are derived from the licensing of software, maintenance, the provision of consulting and other value added support services, and the resale of software obtained from vendors.

Global Med sells various core products and their related components through its Wyndgate division: SafeTrace®, SafeTrace Tx®, and its EIDorado product suite. SafeTrace is used to assist community blood centers, hospitals, plasma centers and outpatient clinics in the U.S. in complying with the quality and safety standards of the U.S. Food and Drug Administration (the FDA) for the collection and management of blood and blood products. SafeTrace Tx is a transfusion management information system that is designed to be used by hospitals and centralized transfusion centers to help insure the quality of blood transfused into patient-recipients. SafeTrace Tx provides electronic cross-matching capabilities to help insure blood compatibility with patient-recipients and tracks, inventories, bills and documents all activities with blood products from the time blood products are received in inventory to the time the blood products are used or returned to blood centers. SafeTrace Tx complements SafeTrace, because the combined SafeTrace Tx and SafeTrace software system is now able to integrate hospitals with blood centers and provide a vein-to-vein tracking of the blood supply.

The Company plans to continue to commit significant research and development (R&D) resources to the development of its EIDorado suite of products. In May of 2007, the Company's first module of EIDorado, Donor Doc, received 510(k) clearance from the FDA. Donor Doc is an electronic history questionnaire that assists in the blood donor screening process. On February 14, 2008, the Company received 510(k) clearance from the FDA for EIDorado Donor. EIDorado Donor is intended as a comprehensive blood management software application designed to provide for the information system needs of blood banks and donor centers. The software is designed to manage, automate, and control activities associated with donors, donor collections, testing, manufacturing, inventory, and distribution. EIDorado Donor was developed with scalability in mind and is designed to manage the system needs of diverse facilities, from small hospital blood banks to community blood centers, to regional and national centers, both domestically and internationally. The blood management software has been designed with guidance from the Company's technology workgroup, comprised of leading industry representatives from around the world. Throughout the EIDorado Donor development process, the work group's contributions assisted the Company in delivering a feature-rich and user-friendly solution.

SafeTrace, SafeTrace Tx, and EIDorado Donor and Donor Doc have been cleared by the FDA for sale in the United States. The Company's development efforts are focused on developing new software products as well as continuously improving its existing products. The Company plans to continue to commit significant development resources to the development of its EIDorado product suite. Some of these additional products are considered medical devices by the FDA. The Company will be required to obtain FDA 510(k) clearance for these medical devices prior to their sale or introduction into the U.S. market.

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In 1999, Global Med introduced PeopleMed. PeopleMed supports chronic disease management as an ASP. PeopleMed's system uses the Internet to coordinate sources of information and users of a patient's clinical information, including laboratory, pharmacy, primary and specialty care providers, claims, and medical records. PeopleMed began offering validation services to the blood bank industry late in 2007. Validation services include documenting and testing systems to enable the user of these systems to conform to specific requirements and regulations. In fall of 2007, PeopleMed's services were expanded to include validation activities and offering of quality-certified resources to help clients and non-clients perform FDA-required user validation testing on blood bank software systems prior to Go-Live. In addition to Go-Live activities, PeopleMed also offers independent services for system revalidation for clients who are upgrading to newer versions and for clients modifying the setup of the software application to meet the May 2008 deadline to start using a new required label format for blood products called ISBT 128.

The decision to purchase a new blood bank system is driven in large part by one or all of the following: replacing antiquated technology, upgrading the laboratory information system (LIS) of the hospital, which typically includes the purchase of a blood bank system, and replacing existing products that have been sunsetted. The Company believes that because the purchase of an LIS by a hospital is a significant driver in the decision to purchase a blood bank system, the Company is heavily reliant on its relationships with its channel partners that sell their LIS systems in combination with the Company's blood bank products.

Entities that plan to purchase blood bank products primarily have two choices:

- Upgrade their current system with their existing vendor, or
- Select a replacement system from an alternative vendor.

Overall, Global Med's revenues for the three months ended March 31, 2008 increased \$874 thousand or 23.5% to \$4.593 million from \$3.719 million from the prior comparable period in 2007. Cost of revenues increased \$419 thousand or 36.8% for the three months ended March 31, 2008 to \$1.558 million from \$1.139 million for the prior comparable period in 2007. For the three months ended March 31, 2008 and 2007, operating expenses were \$2.410 million and \$2.284 million, and net income was \$360 thousand and \$287 thousand, respectively. The increase in net income was primarily attributable to the increase in revenues and partially offset by a substantial increase in the Company's provision for income taxes.

For the three months ended March 31, 2008 operations provided \$867 thousand in cash. For the comparable period in 2007, Global Med's operations provided \$504 thousand in cash. The Company believes that its cash flows from the sale of SafeTrace, SafeTrace Tx, and new products to customers and the current backlog of existing business will continue to be strong on an annual basis through the remainder of fiscal year 2008 and possibly thereafter. The Company believes its revenues and operating income will continue to grow in 2008 and possibly beyond.

The Company believes that its current customer base and projected backlog of business, as well as sales to new customers, will be sufficient to fund operations which include its planned software development activities, and likely will generate positive cash flows from operations and negative cash flows from investing activities through 2008, and possibly thereafter. The Company believes that based on its recurring revenues, current backlog, and its projected pipeline of business, it will be profitable during 2008 and possibly thereafter.

Management of the Company is focused on increasing its revenues and cash flows through direct sales efforts, increasing its marketing footprint through adding additional channel partners and strategic alliances, and developing new products and enhanced functionality to its existing product mix to attract potential customers. The Company is currently reviewing opportunistic business acquisitions.

On March 26, 2008, the Company signed a Stock Purchase Agreement (the Purchase Agreement) to acquire Inlog, SA, a French company, and its subsidiaries (Inlog) for a maximum of \$11.5 million in a combination of cash, stock and earnout payments. Inlog, based in Lyon, France, is a leading European provider of donor center and transfusion information management systems as well as laboratory information systems and other ancillary medical software systems. Prior to closing, the Purchase Agreement requires that the buyer, Global Med, be able to obtain financing acceptable to the buyer, the seller, Inlog, deliver U.S. GAAP financials to the buyer, and the Company's Board of Directors finalize the acquisition, at their sole discretion. None of these conditions precedent to closing have occurred. There can be no assurance that the Company will be able to obtain the financing necessary for this acquisition on terms acceptable to it or at all. The Company plans to finance this transaction through a combination of existing cash, new debt, and the issuance of additional equity to the owners of Inlog.

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Inlog's product line consists of five (5) primary products: EdgeBlood (for the donor center marketplace), EdgeTrace (for the hospital transfusion marketplace), EdgeLab (a LIS), EdgeCell (cellular therapy for tissue banks, stem cell centers and cord blood centers) and SAPA (supports regulatory compliance and document management). Inlog is ISO 9001:2000 certified and its products have received the NF/ISO 25051/12119 certification guaranteeing the highest level of quality regarding the design, testing and validation of its software, its documentation quality and the quality of its product support and maintenance.

Inlog has been developing, implementing, and supporting its blood bank information management solutions since 1992 and supplies over 700 sites in fifteen (15) countries with its products. Inlog recently completed the national installation of its EdgeBlood product in France. All 2.5 million French blood donations flow through Inlog's products in France including blood collections, infectious disease testing, component manufacturing and distribution. In addition to France, Inlog provides its software applications in Germany, Austria, Belgium and Switzerland, as well as installations in Greece and Monaco.

In the event that the Company and Inlog finalize the aforementioned transaction, the Company's software applications will have a presence in twenty (20) countries (including the United States, Canada, Caribbean, European Union, Africa, French Polynesia, and New Caledonia). The Company believes that the acquisition of Inlog is strategically important as Inlog's existing international marketplace may provide a platform for the Company's continued growth.

The Company has been engaged in a legal action involving a former officer and employee. Refer to the Legal Proceedings section for further discussion.

As of March 31, 2008, the annual recurring maintenance revenues that will be generated once all of the Company's current customers have implemented the software will be approximately \$9.4 million. Significant future revenue growth for the Company is contingent upon continued new system sales and successful implementation of the Company's software at existing and future sites. The Company believes it may continue to grow its revenue at double-digit rates for the remainder of the current year, and on an annual basis possibly thereafter.

The Company plans to continue to develop and submit additional EIDorado modules to the FDA.

Balance Sheet Changes

As of March 31, 2008 compared with December 31, 2007, certain balance sheet accounts changed substantially. Cash increased by \$637 thousand from \$6.748 million as of December 31, 2007 to \$7.385 million as of March 31, 2008, primarily as a result of the increase in cash flows from operations. Net accounts receivable decreased \$697 thousand, primarily as a result of the collection of certain accounts receivable balances that related to certain customers' annual maintenance contracts that were billed during the fourth quarter of 2007 and collected during the three months ended March 31, 2008. Prepaid expenses and other current assets increased \$213 thousand primarily as a result of capitalization of \$255 thousand in pre-acquisition costs. Refer to note 1 "Pre-Acquisition Costs" for further discussion.

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2008 COMPARED TO THREE MONTHS ENDED MARCH 31, 2007

Revenues. Revenues are comprised primarily of license fees, maintenance and usage fees, and implementation and consulting services revenues.

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Revenues for the three months ended March 31, 2008 increased by \$874 thousand or 23.5% to \$4.593 million from \$3.719 million for the comparable period in 2007. The primary reasons for the increase were a \$589 thousand in software license fees and a \$309 thousand increase in maintenance fees.

The table below shows the percentage of our total reported revenues for the period. The maintenance, consulting services, and software license fees relate primarily to the Company's SafeTrace and SafeTrace Tx software.

	2008	2007
Maintenance	41.6%	43.1%
Consulting services	18.7%	25.4%
Software license fees	35.9%	28.5%
PeopleMed	3.8%	3.0%
Total Revenue	100%	100%

Cost of revenue. Cost of revenue as a percentage of total revenues was 33.9% and 30.6% for the three months ended March 31, 2008 and 2007, respectively. Cost of revenues increased \$419 thousand or 36.8% to \$1.558 million for the three months ended March 31, 2008 from \$1.139 million for the comparable period in 2007. This increase was due primarily to a \$292 thousand increase in labor-related costs and a \$68 thousand increase in third party software costs which resulted in additional revenues to the Company.

Gross profit. Gross profit as a percentage of total revenue was 66.1% and 69.4% for the three months ended March 31, 2008 and 2007, respectively. Gross profit increased \$455 thousand or 17.6% to \$3.035 million for the three months ended March 31, 2008 from \$2.580 million for the comparable period in 2007. The increase in gross profit was primarily associated with the \$874 thousand increase in revenues. The increase in gross profit resulted primarily from the increase in software license and maintenance revenues but was partially offset by higher labor costs associated with maintenance and implementation revenues.

General and administrative. General and administrative expenses increased \$113 thousand or 14% to \$919 thousand for the three months ended March 31, 2008 compared to \$806 thousand for the comparable period in 2007. The primary reasons for the increase was a \$104 thousand increase in employee-related labor charges, which were made up primarily of accrued bonuses and direct labor costs to be paid in the event the Company achieves certain minimum levels of pre-tax income for the year. The Company's compensation committee is in the process of determining the criteria upon which the year-end bonus payouts will be based. Members of the management of the Company have estimated the current bonus payout in these financials based on the bonus payouts incorporated into the Company's current budget for 2008 which has been approved by the Company's Board of Directors of which three of its independent members are also on the Company's Compensation Committee.

Sales and marketing. For the three months ended March 31, 2008, sales and marketing expenses increased \$188 thousand or 36.4% to \$704 thousand for the three months ended March 31, 2008 compared to \$516 thousand for the comparable period in 2007. The increase in sales and marketing expenses is primarily associated with a combined \$34 thousand increase in payroll expenses, a \$129 thousand increase in commission expenses, primarily associated with higher sales activity for the quarter.

Research and development. Research and development expenses decreased \$183 thousand or 19.8% to \$741 thousand for the three months ended March 31, 2008 compared to \$924 thousand for the comparable period in 2007. This decrease was primarily due to a \$151 thousand decrease in payroll-related expenses, a \$59 thousand increase in capitalized software development costs. These decreases were partially offset by a \$59 thousand increase in travel expenses.

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Depreciation and Software Amortization. Depreciation and software amortization costs for the three months ended March 31, 2008 and 2007 were \$46 thousand and \$38 thousand, respectively.

Income from operations before other income (expense). The Company's income from operations during the three months ended March 31, 2008 and 2007 was \$625 thousand and \$296 thousand, respectively.

Interest income. Interest income for the three months ended March 31, 2008 and 2007 was \$34 thousand and \$16, respectively. The Company's higher cash balances during the quarter resulted in the additional interest income.

Interest expense. Interest expense was \$4 thousand and \$3 thousand for the three months ended March 31, 2008 and 2007 respectively.

Income taxes. For the three months ended March 31, 2008 and 2007, the Company's income tax expense was \$295 thousand and \$22 thousand, respectively. The substantial increase in the Company's income tax expense was the result primarily of two factors: a significant increase in the Company's taxable income as well as an increase in the Company's effective tax rate. The effective tax rate for the first quarter of 2008 when compared with the comparable period in 2007, increased significantly as a result of the reversal of a portion of the Company's valuation allowance associated with the Company's net operating loss carryforwards (NOLs) during the fourth quarter of 2007. In the event the Company continues to be profitable, the Company believes it may be able to continue to shield a significant portion of its taxable income from the payment of income taxes because of these NOLs. Because the Company is required to recognize its tax expense in accordance with US GAAP, this could result in a significant difference between the recognized tax expense and taxes the Company is required to pay.

Net income. The Company's net income for the three months ended March 31, 2008 was \$360 thousand and \$287 thousand for the same period in 2007.

LIQUIDITY AND CAPITAL RESOURCES

The Company had cash and cash equivalents of \$7.385 million as of March 31, 2008 compared to \$6.748 million at December 31, 2007, none of which was restricted.

The Company had net working capital of \$3.817 million as of March 31, 2008 and \$3.445 million at December 31, 2007. The increase in working capital was primarily the result of the \$839 thousand decrease in the accrued expenses and other current liabilities.

The Company had shareholders' equity of \$3.416 million and virtually no debt as of March 31, 2008. The Company believes that it will generate positive cash flows from operations through 2008, and possibly thereafter.

While the Company's plans may change, the Company currently intends to spend between \$600 thousand to \$650 thousand during 2008 on capital equipment which may result in negative cash flows for investing activities. The Company's cash flows from operations should be sufficient to meet its current cash requirements exclusive of acquisitions. The Company believes that based on its current backlog as well as projected pipeline of business, it will be able to achieve profitability for the year ended December 31, 2008 and possibly thereafter.

The acquisition of Inlog would require significant external financing in the form of additional debt or equity. There can be no assurance that the Company will obtain financing on terms favorable to the Company in the near term or at all.

The Company has not ever paid and has no intention of paying dividends to the common shareholders in the foreseeable future.

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Cash flows from operations provided \$867 thousand in cash for the three months ended March 31, 2008. The cash provided during the three months ended March 31, 2008 consisted primarily of the net income of \$360 thousand net of non-cash changes which provided \$170 thousand, and changes in operating assets and liabilities which provided \$337 thousand. The primary source of the Company's operating cash inflows is its billings to customers for the sale of software, services, and maintenance and support. For the three months ended March 31, 2008 and 2007, the Company's accounts receivable billings were approximately \$4.4 million and \$3.2 million, respectively. For the three months ended March 31, 2008 and 2007, the Company collected approximately \$5.1 million and \$4.2 million, respectively from accounts receivable. As a result of the cash collections from accounts receivable being significantly more than the billings, the Company's gross accounts receivable balance decreased by approximately \$679 thousand, while the cash balance increased by approximately \$637 thousand. The Company's cash outflows from operations were approximately \$4.4 million and consisted primarily of three components, payroll, vendor-related expenses, and payment of \$745 thousand in income taxes. Payroll related expenses typically range from 50%-60% of the Company's cash outflows from operations with vendor payments typically making up the majority of the remaining amount. The Company believes that the cash flows from its recurring customer base, accounts receivable, backlog, and new system sales will provide for positive cash flows from operations on an annual basis in 2008 and possibly thereafter. Interest and non-operating cash flows are typically not material.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not required for a Smaller Reporting Company.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation Of Disclosure Controls And Procedures

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's Principal Executive Officer and the Vice President of Finance, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. The Company's disclosure controls and procedures are designed to provide a reasonable level of assurance of achieving the Company's disclosure control objectives. The Company's Principal Executive Officer and Vice President of Finance have concluded that the Company's disclosure controls and procedures are, in fact, effective at this reasonable assurance level as of the period covered.

Internal Controls Over Financial Reporting

As of the end of the period covered by this report, the Company carried out an evaluation under the supervision and with the participation of the Company's Principal Executive Officer and the Vice President of Finance, of the effectiveness of the Company's internal control over financial reporting. The Company's Principal Executive Officer and Vice President of Finance have concluded that the Company's controls over financial reporting are in fact, effective at this reasonable assurance level as of the period covered. For the year ended December 31, 2008, the Company's independent registered public accounting firm, Ehrhardt Keefe Steiner & Hottman PC, will be required to attest to and report on management's assessment. This quarterly report does not include an attestation report of the Company's registered public accounting firm regarding internal controls over financial reporting.

Changes In Internal Controls Over Financial Reporting

In connection with the evaluation of the Company's internal controls over financial reporting for the fourth quarter and year ended December 31, 2007, the Company's Principal Executive Officer and Vice President of Finance determined that there was one significant change to the Company's internal controls over financial reporting that has materially affected, or is reasonably likely to materially effect, the Company's internal controls over financial reporting. This change related to a single control deficiency that was identified during the fourth quarter of 2007 related to the Company's preparation of its income tax provision. Management believes that the additional controls it implemented during the three months ended March 31, 2008 related to the preparation of its income tax provision have removed the control deficiency, and its controls over financial reporting are now effective.

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PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In September 2002, Global Med filed a lawsuit against Donnie L. Jackson, Jr., Global Med's former Vice President of Sales and Marketing. Global Med alleges, among other things, that prior to his resignation in July 2002 Mr. Jackson misappropriated certain trade secrets of Global Med. After leaving Global Med, Mr. Jackson became a management employee of one of Global Med's competitors. On March 30, 2005, the Superior Court of the State of California in and for the County of El Dorado granted the motion for summary judgment for Donnie L. Jackson, Jr. On September 1, 2005, the Company deposited \$1.004 million with the Superior Court in the State of California in the County of El Dorado. This deposit represents potential fees and attorneys' costs the Company could be required to pay in the event the Company did not prevail on appeal. The \$1.004 million is classified as a Deposit in escrow on the Company's balance sheets as of December 31, 2006 and March 31, 2007. Based on external evidence and the advice of legal counsel, the Company determined that it was more likely than not that the Company would be required to pay the \$1.004 million. As a result, the Company expensed the amount of the Deposit in escrow and set up a liability for \$1.004 million. On December 2006, the summary judgment was reversed by the California Court of Appeals and the matter was remanded to the trial court.

ITEM 1A. RISK FACTORS

For the years ended December 31, 2007 and 2006, the Company's operations generated positive cash flows from operating activities in the amount of \$4.421 million and \$1.224 million, respectively. The Company believes that its current customer base and projected backlog of business, as well as sales to new customers, will be sufficient to fund operations which include its planned software development activities, and likely will generate positive cash flows from operations and negative cash flows from investing activities through 2008, and possibly thereafter. The Company believes that based on its recurring revenues, current backlog, and its projected pipeline of business, it will be profitable during 2008 and possibly thereafter; but the Company's projections may not occur as planned. In the event the Company's projections do not occur as anticipated, the Company may not generate sufficient revenues to operate profitably in the future or generate sufficient operating cash flows to continue to expand its business or operate its business at current levels.

There is substantial competition in all aspects of the blood bank and hospital information management industry. Numerous companies are developing technologies and marketing products and services in the healthcare information management area. Many competitors in the blood bank industry have received FDA clearance for their products. Many of these competitors have been in business longer and have substantially greater personnel and financial resources than Global Med. Global Med believes it is able to compete based on the current technological capabilities of SafeTrace, SafeTrace Tx, and ElDorado Donor and Donor Doc.

Our success will also depend in part on our ability to develop commercially viable products without infringing the proprietary rights of others. We have not conducted freedom of use patent searches and patents may exist or could be filed which would have an adverse effect on our ability to market our products or maintain our competitive position with respect to our products.

Our future success will depend to a significant extent on the ability of our current and future management personnel to operate effectively, both independently and as a group. In order to compete successfully against current and future competitors, to timely complete research and development projects and to develop future products, we must continue to expand our operations, particularly in the areas of research and development, sales and marketing and training. If we experience significant growth in the future, such growth would likely place significant strain upon our management, operating and financial systems and other resources. In addition, the Company is currently reviewing opportunistic business acquisitions. Management of the Company is focused on increasing its revenues and cash flows through direct sales efforts, increasing its marketing footprint through adding additional channel partners and strategic alliances, and developing new products and enhanced functionality to its existing product mix to attract potential customers. In addition, acquisitions may present an opportunity to increase revenues. To accommodate such growth and compete effectively, we must continue to implement and improve our information systems, procedures and controls, and to expand, train, motivate and manage our work force. Any failure to implement and improve our operational, financial and management systems or to expand, train, motivate or manage our work force could materially and adversely affect our business, financial condition and results of operations, which could force us to reduce our planned expenditures which could negatively impact our business operations.

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On March 26, 2008, the Company entered into an agreement to acquire Inlog, a private European medical software firm for a maximum of \$11.5 million in a combination of cash, stock and earnout. Prior to closing, the Purchase Agreement requires that the buyer, Global Med, be able to obtain financing acceptable to the buyer, the seller, Inlog, deliver U.S. GAAP financials to the buyer, and the Company's Board of Directors finalize the acquisition, at their sole discretion. None of these conditions precedent to closing have occurred. There can be no assurance that the Company will be able to obtain the financing necessary for this acquisition on terms acceptable to it or at all. In the event the acquisition occurs, the Company plans to finance this transaction through a combination of existing cash, new debt, and the issuance of additional equity to the owners of Inlog.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

There were no matters submitted to a vote of the security holders during the first quarter ended March 31, 2008.

ITEM 5. OTHER INFORMATION

A Current Report on Form 8-K was filed on March 28, 2008 announcing the signing of a stock purchase agreement with Inlog SA, a French software medical company, for the purchase of all outstanding common stock for a total consideration not to exceed \$11.5 million.

A Current Report on Form 8-K was filed on March 14, 2008 announcing the Company's results for the three and twelve months ended December 31, 2007.

ITEM 6. EXHIBITS

Exhibit 31.1 Certification of the Chairman and Chief Executive Officer, Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 31.2 Certification of the Vice President of Finance Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.1 Certification of Chairman and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.2 Certification of Vice President of Finance pursuant to 18 U.S.C. Smily:Times New Roman; font-size:10pt">

2016

3,362

2017

2,911

2018

2,950

2019 and thereafter

1,099

\$15,634

Guarantor Arrangements

The Company has agreements whereby it indemnifies its officers and directors for certain events or occurrences while the officer or director is, or was, serving at the Company's request in such capacity. The term of the indemnification period is for the officer or director's lifetime. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has a director and officer insurance policy that limits its exposure and enables the Company to recover a portion of any future amounts under certain circumstances and subject to deductibles and exclusions. As a result of its insurance policy coverage, the Company believes the estimated fair value of these indemnification agreements is not material. Accordingly, the Company had no liabilities recorded for these agreements as of December 31, 2013 and June 30, 2013.

In the ordinary course of its business, the Company from time to time enters into standard indemnification provisions in its agreements with its clients. Pursuant to these provisions, the Company may be obligated to indemnify its clients for certain losses suffered or incurred, including losses arising from violations of applicable law by the Company or by its third-party website publishers, losses arising from actions or omissions of the Company or its third-party publishers, and for third-party claims that a Company product infringed upon any United States patent, copyright or other intellectual property rights. Where applicable, the Company generally limits its liabilities under such indemnities. With respect to its DSS products, the Company also generally reserves the right to resolve intellectual property infringement claims by providing a non-infringing alternative or by obtaining a license on reasonable terms, and failing that, by terminating its relationship with the client and thus terminating the infringing activity. Subject to these limitations, the term of such indemnity provisions is generally coterminous with the corresponding agreements but in some cases survives for a period of time after termination of the agreement.

The potential amount of future payments to defend lawsuits or settle indemnified claims under these indemnification provisions is generally limited and the Company believes the estimated fair value of these indemnity provisions is not material, and accordingly, the Company had no liabilities recorded for these agreements as of December 31, 2013 and June 30, 2013.

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QUINSTREET, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Litigation

In December 2012, Internet Patents Corporation (IPC) filed a patent infringement lawsuit against the Company in the United States District Court for the Northern District of California, seeking a judgment that the Company has infringed a patent held by IPC. The Company received the related summons and complaint from IPC in March 2013. In September 2013, the court dismissed a related case because it found that the patent is invalid, and on the same date, the court issued IPC an Order to Show Cause that the lawsuit against the Company should not be dismissed. In October 2013, IPC filed a response to the order and the court subsequently dismissed the case against the Company. In November 2013, IPC filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit. While the Company denies IPC's claims and believes that the probability of any loss is remote, there can be no assurance that the Company will prevail in this matter and any adverse ruling or settlement may have a significant impact on its business and operating results. In addition, regardless of the outcome of the matter, the Company may incur significant legal fees defending the action until it is resolved.

10. Stock Benefit Plans

Stock Incentive Plans

The Company may grant incentive stock options (ISOs), nonstatutory stock options (NQSOs), restricted stock, restricted stock units, stock appreciation rights, performance-based stock awards, and other forms of equity compensation, as well as performance cash awards, under its 2010 Equity Incentive Plan (the 2010 Incentive Plan) as well as NQSOs and restricted stock units to non-employee directors under the 2010 Non-Employee Directors' Stock Award Plan (the Directors' Plan). To date, the Company has issued only ISOs, NQSOs and restricted stock units under the plans.

As of December 31, 2013, 9,210,527 shares were reserved and 6,099,068 shares were available for issuance under the 2010 Incentive Plan; 1,593,162 shares were reserved and 1,187,035 shares were available for issuance under the Directors' Plan.

Stock-Based Compensation

The Company estimates the fair value of stock options at the date of grant using the Black-Scholes option-pricing model. Options are granted with an exercise price equal to the fair value of the common stock at the date of grant. The weighted average Black-Scholes model assumptions and the weighted average grant date fair value of employee stock options for the three and six months ended December 31, 2013 and 2012 were as follows:

Three Months Ended	Six Months Ended
December 31,	December 31,

	2013	2012	2013	2012
Expected term (in years)	4.6	4.6	4.6	4.6
Expected volatility	47%	54%	48%	55%
Expected dividend yield	0.0%	0.0%	0.0%	0.0%
Risk-free interest rate	1.3%	0.8%	1.4%	0.7%
Grant date fair value	\$ 3.71	\$ 3.07	\$ 3.90	\$ 3.97

The fair value of restricted stock units is determined based on the closing price of the Company's common stock on the grant date. Compensation expense is amortized net of estimated forfeitures on a straight-line basis over the requisite service period of the stock-based compensation awards.

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QUINSTREET, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

11. Segment Information

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is its chief executive officer. The Company's chief executive officer reviews financial information presented on a consolidated basis, accompanied by information about operating segments, including net sales and operating (loss) income before depreciation, amortization and stock-based compensation expense.

The Company determined its reportable operating segments to be DMS, which derives revenue from fees earned through the delivery of qualified leads, clicks, calls, customers and, to a lesser extent, impressions, and DSS, which derives revenue from the sale of direct selling services through a hosted solution. The accounting policies of the two reportable operating segments are the same as those described in Note 2, Summary of Significant Accounting Policies.

The Company evaluates the performance of its operating segments based on operating income before depreciation, amortization and stock-based compensation expense.

The Company does not allocate most of its assets, nor its depreciation and amortization expense, stock-based compensation expense, interest income, interest expense or income tax expense by segment. Accordingly, the Company does not report such information.

Table of Contents**QUINSTREET, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)**

Summarized information by segment was as follows (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2013	2012	2013	2012
Net revenue by segment:				
DMS	\$ 65,841	\$ 71,514	\$ 142,537	\$ 149,848
DSS	304	237	569	529
Total net revenue	66,145	71,751	143,106	150,377
Segment operating income before depreciation, amortization, and stock-based compensation expense:				
DMS	6,268	11,085	15,729	22,909
DSS	209	143	379	294
Total segment operating income before depreciation, amortization, and stock-based compensation expense	6,477	11,228	16,108	23,203
Depreciation and amortization	(6,668)	(10,179)	(13,344)	(18,458)
Stock-based compensation expense	(2,626)	(3,029)	(5,661)	(5,799)
Impairment of goodwill		(92,350)		(92,350)
Total operating loss	\$ (2,817)	\$ (94,330)	\$ (2,897)	\$ (93,404)

The following tables set forth net revenue and long-lived assets by geographic area (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2013	2012	2013	2012
Net revenue:				
United States	\$ 65,523	\$ 71,180	\$ 141,940	\$ 149,089
International	622	571	1,166	1,288
Total net revenue	\$ 66,145	\$ 71,751	\$ 143,106	\$ 150,377

	December 31, 2013	June 30, 2013
Property and equipment, net:		
United States	\$ 10,607	\$ 9,502
International	259	205
Total property and equipment, net:	\$ 10,866	\$ 9,707

Table of Contents**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the fiscal year ended June 30, 2013, filed with the Securities and Exchange Commission (SEC).

This Quarterly Report on Form 10-Q contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they do not materialize or if they prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are 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. Forward-looking statements are often identified by the use of words such as, but not limited to, anticipate, believe, can, continue, could, estimate, expect, intend, may, will, plan, project, seek, should, target, will, would, and similar expressions or variations intended to identify forward-looking statements. These statements reflect the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified in Part II Item 1A. Risk Factors below, and those discussed in the sections titled Special Note Regarding Forward-Looking Statements and Risk Factors included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013, filed with the SEC. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Management Overview

QuinStreet is a leader in performance marketing online. We have built a strong set of capabilities to engage Internet visitors with targeted media and to connect our marketing clients with their potential customers online. We focus on serving clients in large, information-intensive industry verticals where relevant, targeted media and offerings help visitors make informed choices, find the products that match their needs, and thus become qualified customer prospects for our clients.

We deliver cost-effective marketing results to our clients most typically in the form of a qualified lead or inquiry, in the form of a qualified click, or in the form of a call. Leads, clicks or calls can then convert into a customer or sale for clients at a rate that results in an acceptable marketing cost to them. We are typically paid by clients when we deliver qualified leads, clicks, calls or customers as defined by our agreements with them. References to the delivery of customers means the sale of completed customer transactions (e.g. bound insurance policies or customer appointments with clients). Because we bear the costs of media, our programs must deliver value to our clients and provide for a media yield, or generation of an acceptable margin on our media costs, that provides a sound financial outcome for us. To deliver leads, clicks, calls, and customers to our clients, generally we:

own or access targeted media;

run advertisements or other forms of marketing messages and programs in that media to create visitor responses in the form most typically of leads (visitor generated contact information and requests), clicks (to further qualification or matching steps, or to online client applications or offerings) or calls (to our owned and operated call centers or that of our clients or their agents);

match these leads, clicks, calls or customers to client offerings or brands that we believe can meet visitor interests or needs, converting visitors into qualified leads, clicks, calls or customers for our clients; and

optimize client matches and media yield such that we achieve desired results for clients and a sound financial outcome for us.

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Our primary financial objective has been and remains creating revenue growth from sustainable sources, at target levels of profitability. Our primary financial objective is not to maximize profits, but rather to achieve target levels of profitability while investing in various growth initiatives, as we continue to believe we are in the early stages of a large, long-term market.

Our Direct Marketing Services (DMS) business accounted for substantially all of our net revenue in the three and six months ended December 31, 2013 and 2012. Our DMS business derives net revenue from fees earned through the delivery of qualified leads, clicks, calls or customers and, to a lesser extent, display advertisements, or impressions. Through a vertical focus, targeted media presence and our technology platform, we are able to deliver targeted, measurable marketing results to our clients.

Our two largest client verticals within our DMS business are education and financial services. Our education client vertical represented 45% and 44% of net revenue in the three and six months ended December 31, 2013 and 46% and 45% of net revenue for the three and six months ended December 31, 2012. Our financial services client vertical represented 37% and 39% of net revenue in the three and six months ended December 31, 2013 and 37% and 38% of net revenue for the three and six months ended December 31, 2012. Other DMS client verticals, consisting primarily of business-to-business technology, home services and medical, represented 18% and 17% of net revenue in the three and six months ended December 31, 2013 and 17% of net revenue in both the three and six months ended December 31, 2012.

In addition, we derived less than 1% of our net revenue in both the three and six months ended December 31, 2013, and for the same period last fiscal year, from the provision of a hosted solution and related services for clients in the direct selling industry, also referred to as our Direct Selling Services (DSS) business.

We generated substantially all of our revenue from sales to clients in the United States.

No client accounted for 10% or more of our net revenue in the three and six months ended December 31, 2013 or 2012.

Trends Affecting our Business

Client Verticals

To date, we have generated the majority of our revenue from clients in our education and financial services client verticals. We expect that a majority of our revenue for the remainder of fiscal year 2014 will continue to be generated from clients in these two client verticals.

Our education client vertical has been significantly affected by the adoption of regulations affecting for-profit educational institutions over the past several years. The regulations have affected, and are expected to continue to affect, our clients' businesses and marketing practices, including an overall decrease in our clients' external marketing expenditures. The effect of these regulations or any future regulations may continue to result in fluctuations in the volume and mix of our business with these clients. We are working to offset declines and volatility by diversifying our products, media and markets, including expansion into non-profit and international education markets.

Our financial services client vertical continued to be negatively affected due to reduced availability of high quality media at acceptable margins caused by changes in search engine algorithms, acquisition of media sources by competitors and increased competition for quality media. These effects may continue to impact our business in the near future. We are working to offset declines by diversifying our product base with additions of leads, calls and

bound policies.

Acquisitions

Acquisitions in Fiscal Year 2014

During the six months ended December 31, 2013 we acquired the operations of an online publishing business.

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Acquisitions in Fiscal Year 2013

We did not complete any acquisitions in the six months ended December 31, 2012.

Development and Acquisition of Targeted Media

One of the primary challenges of our business is finding or creating media that is high quality and targeted enough to attract prospects for our clients at costs that work for our business model. In order to grow our business, we must be able to find, develop or retain quality targeted media on a cost-effective basis. Consolidation of media sources, changes in search engine algorithms and increased competition for available media has, during some periods, limited and may continue to limit our ability to generate revenue at acceptable margins.

Seasonality

Our results are subject to significant fluctuation as a result of seasonality. In particular, our quarters ending December 31 (our second fiscal quarter) are typically characterized by seasonal weakness. In our second fiscal quarters, there is lower availability of lead supply from some forms of media during the holiday period on a cost effective basis and some of our clients have lower budgets. In our quarters ending March 31 (our third fiscal quarter), this trend generally reverses with better lead availability and often new budgets at the beginning of the year for our clients with fiscal years ending December 31.

Regulations

Our revenue has fluctuated as a result of newly-adopted or amended regulations and the increased enforcement of existing regulations. Our business is affected directly because we operate websites and conduct telemarketing and email marketing, and indirectly as our clients adjust their operations as a result of regulatory changes that affect their industries.

One example of a recent regulatory change that may affect our business is the Telephone Consumer Protection Act (the TCPA), which the Federal Communications Commission recently amended to, among other things, impose heightened consent and opt-out requirements that companies conducting telemarketing must follow. Certain provisions of the regulations became effective in July 2012, and additional regulations requiring prior express written consent for telemarketing calls to wireless numbers became effective in October 2013. Our efforts to comply with the TCPA has had a relatively small negative effect on traffic conversion rates. Our clients may make business decisions based on their own experiences with the TCPA regardless of our products, and the changes we implemented to comply with the new regulations. Those decisions may negatively affect our revenue or profitability.

In addition, our education client vertical has been significantly affected by the adoption of regulations affecting for-profit educational institutions over the past several years, and a higher level of legislative scrutiny is expected to continue. Clients in our financial services vertical have increasingly been affected by laws and regulations as a result of the adoption of new regulations under The Dodd Frank Wall Street Reform and Consumer Protection Act and the increased enforcement of new and pre-existing laws and regulations. The effect of these regulations, or any future regulations, may continue to result in fluctuations in the volume and mix of our business with these clients.

Basis of Presentation

General

Our business is composed of two operating segments: DMS and DSS. For further discussion and financial information about our operating segments, see Note 11, Segment Information, to our condensed consolidated financial statements.

Net Revenue

DMS. Our DMS business generates revenue from fees earned through the delivery of qualified leads, clicks, calls, customers and, to a lesser extent, display advertisements, or impressions. We deliver targeted and measurable results through a vertical focus that we classify into the following client verticals: education, financial services and other (which includes business-to-business technology, home services and medical).

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DSS. Our DSS business generated less than 1% of net revenue in each of the three and six months ended December 31, 2013 and 2012. We expect DSS to continue to represent an immaterial portion of our business.

Cost of Revenue

Cost of revenue consists primarily of media costs, personnel costs, amortization of intangible assets, depreciation expense, and amortization of internal software development costs relating to revenue-producing technologies. Media costs consist primarily of fees paid to website publishers that are directly related to a revenue-generating event and pay-per-click, or PPC, ad purchases from Internet search companies. We pay these website publishers and Internet search companies on a revenue-share, a cost-per-lead, or CPL, cost-per-click, or CPC, and cost-per-thousand-impressions, or CPM, basis. Personnel costs include salaries, stock-based compensation expense, bonuses, and employee benefit costs. Personnel costs are primarily related to individuals associated with maintaining our servers and websites, our editorial staff, client management, creative team, content, compliance group, and media purchasing analysts. Costs associated with software incurred in the development phase or obtained for internal use are capitalized and amortized in cost of revenue over the software's estimated useful life.

Operating Expenses

We classify our operating expenses into three categories: product development, sales and marketing and general and administrative. Our operating expenses consist primarily of personnel costs and, to a lesser extent, professional services fees, rent and other costs. Personnel costs for each category of operating expenses generally include salaries, stock-based compensation expense, bonuses, commissions, and employee benefit costs.

Product Development. Product development expenses consist primarily of personnel costs and professional services fees associated with the development and maintenance of our technology platforms, development and launching of our websites, product-based quality assurance, and testing. In the current period of business challenges, we are constraining expenses generally to the extent practicable. However, we expect product development expenses to continue to increase in absolute dollars for the remainder of fiscal year 2014 as we believe that continued investment in technology is critical to attaining our strategic objectives.

Sales and Marketing. Sales and marketing expenses consist primarily of personnel costs and, to a lesser extent, professional services fees, travel costs and advertising. In the current period of business challenges, we are constraining expenses generally to the extent practicable. However, we expect sales and marketing expenses to continue to increase in absolute dollars for the remainder of fiscal year 2014 as we hire additional personnel in sales and marketing to support our offerings.

General and Administrative. General and administrative expenses consist primarily of personnel costs of our executive, finance, legal, employee benefits and compliance, technical support, and other administrative personnel, as well as accounting and legal professional services fees, and insurance. In the current period of business challenges, we are constraining expenses generally to the extent practicable. However, we expect general and administrative expenses, including increased legal and accounting costs to increase in absolute dollars for the remainder of fiscal year 2014 as we continue to invest in corporate infrastructure and expand our business internationally.

Interest and Other Income (Expense), Net

Interest and other income (expense), net, consists primarily of interest expense, other income and expense, net and interest income. Interest expense is related to our credit facility, including the related interest rate swap and promissory notes issued in connection with our acquisitions, and includes imputed interest on non-interest bearing

notes. Borrowings under our credit facility, the aggregate principal amount of outstanding promissory notes and related interest expense could increase if, among other things, we make additional acquisitions through debt financing. Interest income represents interest earned on our cash, cash equivalents and marketable securities, which may increase or decrease depending on market interest rates and the amounts invested.

Other income (expense), net, includes foreign currency exchange gains and losses and other non-operating items.

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Income Tax (Provision for) Benefit from

We are subject to tax in the United States as well as other tax jurisdictions or countries in which we conduct business. Earnings from our limited non-U.S. activities are subject to local country income tax and may be subject to U.S. income tax.

Critical Accounting Policies, Estimates and Judgments

In presenting our consolidated financial statements in conformity with U.S. generally accepted accounting principles, or GAAP, we are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures.

Some of the estimates and assumptions we are required to make relate to matters that are inherently uncertain as they pertain to future events. We base these estimates and assumptions on historical experience or on various other factors that we believe to be reasonable and appropriate under the circumstances. On an ongoing basis, we reconsider and evaluate our estimates and assumptions. Actual results may differ significantly from these estimates.

We believe that the critical accounting policies listed below involve our more significant judgments, assumptions and estimates and, therefore, could have the greatest potential impact on our consolidated financial statements.

Revenue recognition;

Valuation of goodwill and intangible assets;

Stock-based compensation;

Income taxes; and

Valuation of long-lived assets.

There have been no material changes to our critical accounting policies, estimates and judgments disclosed in our Annual Report on Form 10-K subsequent to June 30, 2013. For further information on our critical and other significant accounting policies and estimates, see Part II, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations of our Annual Report on Form 10-K for the year ended June 30, 2013, filed with the SEC.

Recently Issued Accounting Standards

See Note 2, Summary of Significant Accounting Policies, to our condensed consolidated financial statements.

Table of Contents**Results of Operations**

The following table sets forth our consolidated statement of operations for the periods indicated:

	Three Months Ended December 31,				Six Months Ended December 31,			
	2013		2012		2013		2012	
	(In thousands)				(In thousands)			
Net revenue	\$ 66,145	100.0%	\$ 71,751	100.0%	\$ 143,106	100.0%	\$ 150,377	100.0%
Cost of revenue ⁽¹⁾	56,116	84.8	61,712	86.0	119,708	83.6	126,902	84.4
Gross profit	10,029	15.2	10,039	14.0	23,398	16.4	23,475	15.6
Operating expenses: ⁽¹⁾								
Product development	4,776	7.2	4,504	6.3	9,935	6.9	9,397	6.2
Sales and marketing	3,659	5.5	3,496	4.9	7,815	5.5	7,187	4.8
General and administrative	4,411	6.7	4,019	5.6	8,545	6.0	7,945	5.3
Impairment of goodwill		0.0	92,350	128.7		0.0	92,350	61.4
Operating loss	(2,817)	(4.2)	(94,330)	(131.5)	(2,897)	(2.0)	(93,404)	(62.1)
Interest income	27	0.0	28	0.0	54	0.0	56	0.0
Interest expense	(976)	(1.5)	(1,354)	(1.9)	(2,002)	(1.4)	(2,366)	(1.6)
Other (expense) income, net	(29)	(0.0)	(4)	0.0	(48)	(0.0)	42	0.0
Loss before income taxes	(3,795)	(5.7)	(95,660)	(133.3)	(4,893)	(3.4)	(95,672)	(63.6)
(Provision for) benefit from taxes	(40,234)	(60.8)	32,169	44.8	(40,075)	(28.0)	32,044	21.3
Net loss	\$ (44,029)	(66.5)%	\$ (63,491)	(88.5)%	\$ (44,968)	(31.4)%	\$ (63,628)	(42.3)%

⁽¹⁾ Cost of revenue and operating expenses include stock-based compensation expense as follows:

Cost of revenue	\$ 721	1.1%	\$963	1.3%	\$1,595	1.1%	\$1,886	1.3%
Product development	610	0.9	698	1.0	1,342	0.9	1,391	0.9
Sales and marketing	598	0.9	858	1.2	1,368	1.0	1,623	1.1
General and administrative	697	1.1	510	0.7	1,356	0.9	899	0.6
Net Revenue								

	Three Months Ended December 31,		Six Months Ended December 31,		Three	Six
	2013	2012	2013	2012	Months % Change	Months % Change
	(in thousands)					
Net revenue	\$ 66,145	\$ 71,751	\$ 143,106	\$ 150,377	(8%)	(5%)
Cost of revenue	56,116	61,712	119,708	126,902	(9%)	(6%)
Gross profit	\$ 10,029	\$ 10,039	\$ 23,398	\$ 23,475	(0%)	(0%)

Net revenue decreased \$5.6 million, or 8%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012. Our education client vertical revenue decreased \$2.8 million, or 9%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012, as a result of our education clients' lower budgets, largely due to uncertainty surrounding regulations affecting for-profit educational institutions and their operational adjustment to those regulatory changes. Our financial services client vertical revenue decreased \$2.2 million, or 8%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012, primarily due to our inability to cost effectively access sufficient high quality media given our current product offerings. Our other client verticals revenue decreased \$0.6 million, or 4%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012, primarily due to volatility in client demand in our medical, home services and business-to-business technology client verticals.

Net revenue decreased \$7.3 million, or 5%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012. Our education client vertical revenue decreased \$4.4 million, or 7%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012, as a result of our education clients' lower budgets, largely due to

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uncertainty surrounding regulations affecting for-profit educational institutions and their operational adjustment to those regulatory changes. Our financial services client vertical revenue decreased \$0.7 million, or 1%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012, primarily due to our inability to cost effectively access sufficient high quality media given our current product offerings. Our other client verticals revenue decreased \$2.2 million, or 8%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012, primarily due to volatility in client demand in our business-to-business technology, medical and home services client verticals.

Cost of Revenue

Cost of revenue decreased \$5.6 million, or 9%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012, driven by decreased amortization of intangible assets of \$3.8 million, decreased media costs of \$2.5 million and decreased stock-based compensation of \$0.2 million, offset by increased personnel costs of \$0.4 million, other expenses of \$0.3 million and increased depreciation of \$0.2 million. The decreased amortization of intangible assets was attributable to an amortization charge associated with certain licensed patents in the three months ended December 31, 2012, assets from historical acquisitions becoming fully amortized and a reduced number of acquisitions in recent periods. The decreased media costs were attributable to lower revenue levels. The increased personnel costs were attributable to an increase in average headcount. Gross margin, which is the difference between net revenue and cost of revenue as a percentage of net revenue, was 15% for the three months ended December 31, 2013 and 14% for the three months ended December 31, 2012.

Cost of revenue decreased \$7.2 million, or 6%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012, driven by decreased amortization of intangible assets of \$5.5 million, decreased media costs of \$2.0 million and decreased stock-based compensation of \$0.3 million offset by increased other expenses of \$0.3 million and depreciation of \$0.3 million. The decreased amortization of intangible assets was attributable to an amortization charge associated with certain licensed patents in the three months ended December 31, 2012, assets from historical acquisitions becoming fully amortized and a reduced number of acquisitions in recent periods. The decreased media costs were primarily attributable to lower revenue levels offset by a lower mix of traffic from owned and operated media. Gross margin, which is the difference between net revenue and cost of revenue as a percentage of net revenue, was 16% for the six months ended December 31, 2013 and 2012.

Operating Expenses

	Three Months Ended December 31,		Six Months Ended December 31,		Three Months	Six Months
	2013	2012	2013	2012	% Change	% Change
	(in thousands)					
Product development	\$ 4,776	\$ 4,504	\$ 9,935	\$ 9,397	6%	6%
Sales and marketing	3,659	3,496	7,815	7,187	5%	9%
General and administrative	4,411	4,019	8,545	7,945	10%	8%
Impairment of goodwill		92,350		92,350	(100%)	(100%)
Operating expenses	\$ 12,846	\$ 104,369	\$ 26,295	\$ 116,879	(88%)	(78%)

Product Development Expenses

Product development expenses increased \$0.3 million, or 6%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012. This was primarily due to increased personnel costs of \$0.3 million due to an increase in average headcount.

Product development expenses increased \$0.5 million, or 6%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012. This was primarily due to increased personnel costs of \$0.5 million due to an increase in average headcount.

Table of Contents*Sales and Marketing Expenses*

Sales and marketing expenses increased \$0.2 million, or 5%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012. This was primarily due to increased personnel costs of \$0.3 million due to an increase in average headcount and various miscellaneous increases in sales and marketing expenses of \$0.2 million offset by decreased stock-based compensation of \$0.3 million.

Sales and marketing expenses increased \$0.6 million, or 9%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012. This was primarily due to increased personnel costs of \$0.6 million due to an increase in average headcount and various miscellaneous increases in sales and marketing expenses of \$0.3 million offset by decreased stock-based compensation of \$0.3 million.

General and Administrative Expenses

General and administrative expenses increased \$0.4 million, or 10%, for the three months ended December 31, 2013, compared to the three months ended December 31, 2012. This was primarily due to increased tax expense related to an additional business tax assessment of \$0.5 million and increased stock-based compensation expense of \$0.2 million offset by a decrease in personnel costs of \$0.3 million.

General and administrative expenses increased \$0.6 million, or 8%, for the six months ended December 31, 2013, compared to the six months ended December 31, 2012. This was primarily due to increased stock-based compensation of \$0.5 million due to incremental stock grants and an increase in the fair value of our common stock and an additional business tax assessment of \$0.5 million offset by a decrease in personnel costs of \$0.3 million and various miscellaneous decreases in general and administration expenses of \$0.1 million.

Interest and Other Income (Expense), Net

	Three Months Ended		Six Months		Three	Six
	December 31,		Ended		Months	Months
	2013	2012	2013	2012	% Change	% Change
	(in thousands)					
Interest income	\$ 27	\$ 28	\$ 54	\$ 56	(4%)	(4%)
Interest expense	(976)	(1,354)	(2,002)	(2,366)	(28%)	(15%)
Other income (expense), net	(29)	(4)	(48)	42	625%	(214%)
Interest and other income (expense), net	\$ (978)	\$ (1,330)	\$ (1,996)	\$ (2,268)	(26%)	(12%)

Interest and other income (expense), net decreased \$0.4 million, or 26% for the three months ended December 31, 2013, compared to the three months ended December 31, 2012 due to decreased debt obligations.

Interest and other income (expense), net decreased \$0.3 million, or 12% for the six months ended December 31, 2013, compared to the six months ended December 31, 2012 due to decreased debt obligations.

Provision for Taxes

	Three Months Ended December 31, 2013		Six Months Ended December 31, 2013		Three Months % Change	Six Months % Change
	2012		2012			
	(in thousands)					
(Provision for) Benefit from taxes	\$ (40,234)	\$ 32,169	\$ (40,075)	\$ 32,044	(225%)	(225%)

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We recorded a provision for income taxes of \$40.2 million and \$40.1 million for the three and six months ended December 31, 2013. We estimate our annual effective tax rate to be negative 4%. This differs from the annual statutory rate of 35% primarily due to a one-time, non-cash charge in the amount of \$40.2 million to establish a valuation allowance for a significant portion of our deferred tax assets.

We regularly assess the need for a valuation allowance against our deferred tax assets. Significant judgment is required to determine whether a valuation allowance is necessary and the amount of such valuation allowance, if appropriate. We consider all available evidence, both positive and negative to determine, based on the weight of available evidence, whether it is more likely than not that some or all of the deferred tax assets will not be realized. In evaluating the need for a valuation allowance, we consider, among other things, the nature, frequency and severity of current and cumulative losses, forecasts of future profitability, and the duration of statutory carryforward periods. We determined that the significant negative evidence associated with the cumulative losses in recent periods and the current results outweighed the positive evidence as of December 31, 2013. As a result, in the second quarter of fiscal 2014, we determined a valuation allowance was required as near-term realization of these assets was deemed unlikely and recorded a one-time, non-cash charge of \$40.2 million. This accounting treatment has no effect on our actual ability to utilize deferred tax assets such as loss carryforwards and tax credits to reduce future cash tax payments. We will continue to assess the likelihood that the deferred tax assets will be realizable at each reporting period and the valuation allowance will be adjusted accordingly.

Liquidity and Capital Resources

As of December 31, 2013, our principal sources of liquidity consisted of cash and cash equivalents of \$83.2 million, short-term marketable securities of \$39.2 million, cash we expect to generate from operations, and our \$100.0 million revolving credit line, which is committed until November 2016, a portion of which is available to be drawn subject to compliance with applicable covenants. Our cash and cash equivalents are maintained in highly liquid investments with remaining maturities of 90 days or less at the time of purchase. We believe our cash equivalents are liquid and accessible.

Our short-term and long-term liquidity requirements primarily arise from our working capital requirements, debt service on our \$85 million term loan balance at December 31, 2013, and acquisitions from time to time. Our primary operating cash requirements include the payment of media costs, personnel costs, costs of information technology systems, and office facilities. Our ability to fund these requirements will depend on our future cash flows, which are determined, in part, by future operating performance and are, therefore, subject to prevailing global macroeconomic conditions and financial, business and other factors, some of which are beyond our control, and also our ability to access our credit facility. Even though we may not need additional funds, we may still elect to obtain additional debt or equity financing or draw down on or increase our borrowing capacity under our current credit facility for other reasons.

We believe that our existing cash, cash equivalents, short-term marketable securities, cash generated from operations, and our available borrowings under the credit facility will be sufficient to satisfy our currently anticipated cash requirements through at least the next 12 months.

The following table summarizes our cash flows for the periods indicated:

**Six Months Ended
December 31,**

	2013	2012
	(in thousands)	
Cash flows provided by operating activities	\$ 10,341	\$ 21,639
Cash flows used in investing activities	(10,841)	(7,901)
Cash flows used in financing activities	(6,329)	(13,958)

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Operating Activities

Cash flows provided by operating activities are primarily the result of our net loss adjusted for non-cash expenses such as depreciation and amortization, stock-based compensation expense, impairment of goodwill, and changes in working capital components.

Cash flows provided by operating activities were \$10.3 million for the six months ended December 31, 2013, compared to \$21.6 million for the six months ended December 31, 2012.

Cash flows provided by operating activities for the six months ended December 31, 2013 consisted of changes in working capital of \$36.3 million and non-cash charges of \$19.0 million, partially offset by a net loss of \$45 million. The changes in working capital accounts was primarily due to a decrease in net deferred taxes of \$40.4 million and a decrease in accounts receivable of \$3.6 million offset by a net decrease in accounts payable and accrued liabilities of \$6.1 million and a net decrease in deferred revenue and other noncurrent liabilities of \$1.0 million. The decrease in deferred taxes is due to a one-time charge to establish a valuation allowance. The decrease in accounts receivable was primarily due to lower revenue levels and the net decrease in accounts payable and accrued liabilities is primarily due to timing of payments. The non-cash charges primarily consisted of depreciation and amortization of \$13.3 million and stock-based compensation expense net of tax benefits of \$5.4 million.

Cash flows provided by operating activities for the six months ended December 31, 2012 consisted of non-cash charges of \$116.7 million, partially offset by net loss of \$63.6 million and changes in working capital of \$31.4 million. The non-cash charges primarily consisted of impairment of goodwill of \$92.4 million, depreciation and amortization of \$18.5 million and stock-based compensation expense net of tax benefits of \$5.7 million. The contribution to working capital accounts was primarily due to increase deferred taxes of \$28.9 million, net decrease in accounts payable and accrued liabilities of \$9.9 million and increase in prepaid expenses and other assets of \$4.6 million, partially offset by decrease in accounts receivable of \$12.2 million. The decrease in accounts receivable, as well as the net decrease in accounts payable and accrued liabilities, are primarily due to timing of payments.

Investing Activities

Cash flows from investing activities include capital expenditures, capitalized internal development costs and net investments in marketable securities.

Cash flows used in investing activities was \$10.8 million for the six months ended December 31, 2013, compared to cash flows used in investing activities of \$7.9 million for the six months ended December 31, 2012.

Cash used in investing activities in the six months ended December 31, 2013 was primarily due to capital expenditures and internal software development costs of \$5.4 million, licenses to intangible assets of \$2.7 million and acquisition costs of \$0.9 million. Net investments in marketable securities totaled \$1.9 million in the six months ended December 31, 2013.

Cash used in investing activities in the six months ended December 31, 2012 was primarily due to net investments in marketable securities of \$3.3 million and licenses of intangible assets of \$2.5 million. Capital expenditures and internal software development costs totaled \$2.1 million in the six months ended December 31, 2012.

Financing Activities

Cash flows from financing activities include proceeds from exercise of stock options, withholding taxes related to restricted stock net of share settlement, excess tax benefits from stock-based compensation, and principle payments on bank debt and acquisition-related notes payable.

Cash flows used in financing activities was \$6.3 million for the six months ended December 31, 2013, compared to cash flows used in financing activities of \$14.0 million for the six months ended December 31, 2012.

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Cash used in financing activities in the six months ended December 31, 2013 was primarily due to principal payments on acquisition-related notes payable and our term loan of \$7.2 million and withholding taxes related to restricted stock net share settlement of \$1.3 million, partially offset by exercises of stock options of \$1.9 million and excess tax benefits from exercises of stock options of \$0.3 million.

Cash used in financing activities in the six months ended December 31, 2012 was primarily due to repurchases of our common stock of \$6.2 million and principal payments on acquisition-related notes payable and our term loan and related fees of \$8.0 million, partially offset by proceeds received from exercises of stock options of \$0.3 million.

Off-Balance Sheet Arrangements

During the periods presented, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Contractual Obligations

Our contractual obligations relate to borrowings under our credit facility, acquisition-related notes payable and operating leases. There have been no significant changes to our contractual obligations from those disclosed in our Annual Report on Form 10-K for the year ended June 30, 2013.

The following table summarizes our contractual obligations for the periods indicated (in thousands):

Year Ending June 30,	Promissory Notes	Credit Facility	Operating Leases	Total
2014 (remaining six months)	\$ 928	\$ 7,500	\$ 1,836	\$ 10,264
2015	560	17,500	3,476	21,536
2016	50	20,000	3,362	23,412
2017		40,000	2,911	42,911
2018			2,950	2,950
2019 and thereafter			1,099	1,099
Total	\$ 1,538	\$ 85,000	\$ 15,634	\$ 102,172

Credit Facility

In November 2011, we entered into the Second Amended and Restated Revolving Credit and Term Loan Agreement (the Second Loan Agreement) with Comerica Bank (the Bank), the administrative agent and lead arranger. The Second Loan Agreement consists of a \$100 million five-year term loan, with annual principal amortization of 5%, 10%, 15%, 20%, and 50%, and a \$200 million five-year revolving credit line. On February 15, 2013, we entered into the First Amendment to Credit Agreement and Amendment to Guaranty (First Amendment to the Second Loan Agreement) with the Bank to, among other things: (1) amend the definition of adjusted EBITDA, effective as of December 31, 2012, to exclude extraordinary or non-recurring non-cash expenses of losses including, without limitation, goodwill impairments, and any extraordinary or non-recurring cash expenses in an aggregate amount not to exceed \$5 million for the life of the Second Loan Agreement; and (2) reduce the \$200 million five-year revolving credit line portion of the facility to \$100 million, effective as of February 15, 2013.

Borrowings under the Second Loan Agreement are secured by substantially all of our assets. Interest is payable at a rate computed using either Base rate or a Eurodollar rate plus an applicable margin, at our option. Base rate is defined as the applicable margin plus the greatest of (a) the Prime Rate for such day, (b) the Federal Funds Effective Rate in effect on such day, plus 1% and (c) the Daily Adjusting LIBOR Rate plus 1%. Base rate borrowings bear interest at a Base rate plus an applicable margin which varies

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from (1) 0.625% to 1.375% for revolving loans and (2) 1.00% to 1.75% for term loans, depending on our funded debt to adjusted EBITDA ratio. Eurodollar rate borrowings bear interest at the Eurodollar rate plus an applicable margin which varies from (1) 1.625% to 2.375% for revolving loans and (2) 2.00% to 2.75% for term loans, depending on our funded debt to adjusted EBITDA ratio. Adjusted EBITDA is defined as net (loss) income less (provision for) benefit from taxes, depreciation expense, amortization expense, stock-based compensation expense, interest and other income (expense), acquisition costs for business combinations, extraordinary or non-recurring non-cash expenses of losses including, without limitation, goodwill impairments, and any extraordinary or non-recurring cash expenses in an aggregate amount not to exceed \$5 million for the life of this Second Loan Agreement. The revolving credit line requires an annual facility fee of 0.375% of the revolving credit line capacity. The Second Loan Agreement expires in November 2016. The Second Loan Agreement restricts our ability to raise additional debt financing and pay dividends, and also requires us to comply with other nonfinancial covenants. In addition, we are required to maintain financial ratios computed as follows:

1. A minimum fixed charge coverage ratio of 1.15:1, calculated as the ratio of (i) trailing twelve months of adjusted EBITDA to (ii) the sum of capital expenditures, net cash interest expense, cash taxes, cash dividends, and trailing twelve months payments of indebtedness. Payment of unsecured indebtedness is excluded to the degree that sufficient unused revolving credit line capacity exists such that the relevant debt payment could be made from the credit facility.
2. A maximum funded debt to adjusted EBITDA ratio of 3:1, calculated as the ratio of (i) the sum of all obligations owed to lending institutions, the face amount of any letters of credit, indebtedness owed in connection with acquisition-related notes and indebtedness owed in connection with capital lease obligations to (ii) trailing twelve months of adjusted EBITDA.

We were in compliance with the covenants of our loan agreements as of December 31, 2013 and June 30, 2013.

Interest Rate Swap

In February 2012, we entered into an interest rate swap to reduce our exposure to the financial impact of changing interest rates under our term loan. We do not speculate using derivative instruments. The swap encompasses the principal balances scheduled to be outstanding as of January 1, 2014 and thereafter, such principal and notional amount totaling \$85 million in January 2014 and amortizing to \$35 million in November 2016. The effective date of the swap was April 9, 2012 with a maturity date of November 4, 2016. At December 31, 2013, we had approximately \$85 million of notional amount outstanding in the swap agreement that exchanges a variable interest rate base (Eurodollar rate) for a fixed interest rate of 0.97% over the term of the agreement. This interest rate swap is designated as a cash flow hedge of the interest rate risk attributable to forecasted variable interest payments. The effective portion of the fair value gains or losses on this swap are included as a component of accumulated other comprehensive loss.

At December 31, 2013, our interest rate swap qualified as a cash flow hedge. For this qualifying hedge, the effective portion of the change in fair value will be recognized through earnings when the underlying transaction being hedged affects earnings, thereby allowing the swap's gains and losses to offset interest expense from the term loan on the statement of operations. Any hedge ineffectiveness is recognized in earnings in the current period.

Headquarter Lease

We entered into a lease agreement in February 2010 for approximately 63,998 square feet of office space located at 950 Tower Lane, Foster City, California. The term of the lease began on November 1, 2010 and expires on October 31, 2018. The monthly base rent was abated for the first 12 calendar months under the lease, and was \$0.1 million through the 24th calendar month of the term of the lease. Monthly base rent increased to \$0.2 million for the

subsequent 12 months and now increases approximately 3% after each 12-month anniversary during the remaining term, including any extensions under our options to extend. We have two options to extend the term of the lease for one additional year for each option following the expiration date of the lease or renewal term, as applicable.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risks in the ordinary course of our business. These risks include primarily interest rate and foreign currency exchange risks.

Interest Rate Risk

We invest our cash equivalents and short-term investments primarily in liquid, highly-rated U.S. government or municipal fixed income securities, certificates of deposit with financial institutions and money market funds. Unrestricted cash, cash equivalents and short-term investments are held for working capital purposes and acquisition financing. We do not enter into investments for trading or speculative purposes. We believe that we do not have material exposure to changes in the fair value of these investments as a result of changes in interest rates due to the short-term nature of our investments. Declines in interest rates may reduce future investment income. However, a hypothetical decline of 1% in the interest rate on our investments would not have a material effect on our consolidated financial statements.

As of December 31, 2013, our credit facility consisted of an \$85 million outstanding term loan and a \$100 million revolving line of credit with no amount outstanding. Interest on borrowings under the credit facility is payable quarterly at specified margins above either the Eurodollar rate or the Prime Rate. Our exposure to interest rate risk under the credit facility will depend on the extent to which we utilize the facility. To reduce our exposure to rising interest rates under the term loan, in February 2012, we entered into an interest rate swap encompassing the principal balances scheduled to be outstanding as of January 1, 2014 and thereafter, such scheduled principal amount totaling \$85 million on January 1, 2014 and amortizing to \$35 million on November 4, 2016. The interest rate swap effectively fixes the Eurodollar rate at a fixed rate of 0.97%. As such, a hypothetical change of 1% from prevailing interest rates as of December 31, 2013 would not have an effect on our interest expense.

Foreign Currency Exchange Risk

To date, our international client agreements have been predominately denominated in U.S. dollars, and, accordingly, we have limited exposure to foreign currency exchange rate fluctuations related to client agreements, and do not currently engage in foreign currency hedging transactions. As the local accounts for some of our foreign operations are maintained in the local currency of the respective country, we are subject to foreign currency exchange rate fluctuations associated with the remeasurement to U.S. dollars. A hypothetical change of 10% in foreign currency exchange rates would not have a material effect on our consolidated financial condition or results of operations.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our principal executive and principal financial officers, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2013. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions

regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of December 31, 2013, our principal executive and principal financial officers concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

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Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Securities Exchange Act that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In December 2012, Internet Patents Corporation (IPC) filed a patent infringement lawsuit against us in the United States District Court for the Northern District of California, seeking a judgment that we had infringed a patent held by IPC. We received the related summons and complaint from IPC in March 2013. In September 2013, the court dismissed a related case because it found that the patent is invalid, and on the same date, the court issued IPC an Order to Show Cause that the lawsuit against us should not be dismissed. In October 2013, IPC filed a response to the order and the court subsequently dismissed the case against us. In November 2013, IPC filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit. While we deny IPC's claims and believe that the probability of any loss is remote, there can be no assurance that we will prevail in this matter and any adverse ruling or settlement may have a significant impact on our business and operating results. In addition, regardless of the outcome of the matter, we may incur significant legal fees defending the action until it is resolved.

From time to time, we may become involved in other legal proceedings and claims arising in the ordinary course of our business.

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ITEM 1A. RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the risks described below and the other information in this periodic report. If any of such risks actually occur, our business, operating results or financial condition could be adversely affected. In those cases, the trading price of our common stock could decline and you may lose all or part of your investment.

Risks Related to Our Business and Industry

We operate in an emerging industry and have a relatively new business model, which makes it difficult to evaluate our business and prospects.

We derive nearly all of our revenue from the sale of online marketing and media services, which is an emerging industry that has undergone rapid and dramatic changes in its relatively short history and which is characterized by rapidly-changing Internet media, evolving industry standards, regulatory uncertainty, and changing user and client demands. As a result, we face risks and uncertainties such as but not limited to:

our emerging industry and relatively new business model;

changes in the economic condition, market dynamics, regulatory or legislative environment affecting our business or our clients' businesses;

our dependence on Internet search companies to attract Internet visitors;

our ability to accurately forecast our operating results and appropriately plan our expenses;

our ability to compete in our industry;

our ability to develop our websites to allow Internet visitors to access our websites through mobile devices;

our ability to develop new services and enhancements and features to meet new demands from our clients;
and

our ability to successfully challenge regulatory audit, investigations or alleged noncompliance with laws. If we are unable to address these risks, our business, results of operations and prospects could suffer.

We depend on two market verticals for a majority of our revenue. Negative changes in the economic condition, market dynamics or regulatory environment in these verticals have caused, and may continue to cause, our revenue to decline and our business and growth to suffer.

To date, we have generated a large majority of our revenue from clients in our education and financial services client verticals. We expect that a majority of our revenue, at least in the near term, will continue to be generated from clients in our education and financial services client verticals. Changes in the market conditions or the regulatory environment in these two highly-regulated client verticals have negatively impacted, and may continue to negatively impact, our clients' businesses, marketing practices and budgets and, therefore, our financial results.

Our and our clients' businesses are subject to many regulatory requirements. Current or future regulations could have a material adverse effect on our business, results of operations and financial condition.

Our business is subject to many laws and regulatory requirements, including Federal, state, and local laws and regulations regarding unsolicited commercial email, telemarketing, user privacy, search engines, Internet tracking technologies, direct marketing, data security, data privacy, pricing, sweepstakes, promotions, intellectual property ownership and infringement, trade secrets, export of encryption technology, acceptable content and quality of goods, and taxation, among others. Each of our education, financial services and other client verticals is also subject to various laws and regulations, and our marketing activities on behalf of our clients are regulated. Many of these laws are frequently changing, and keeping our business in compliance with or bringing our business into compliance with new laws may be costly, affect our revenue and harm our financial results. Violations or alleged violations of laws by

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us or our third party publishers could result in liability for damages, fines, criminal prosecution, unfavorable publicity, and restrictions on our ability to operate any of which could have a material adverse effect on our business, results of operations and financial condition. In addition, new laws or regulations or changes in enforcement of existing laws or regulations applicable to our clients could affect the activities or strategies of our clients and, therefore, lead to reductions in their level of business with us.

For example, the Federal Communications Commission recently amended the Telephone Consumer Protection Act that affects telemarketing calls. Certain provisions of the regulations became effective in July 2012, and additional regulations requiring prior express written consent for certain types of telephonic communications became effective in October 2013. Our efforts to comply with the TCPA has had a relatively small negative effect on traffic conversion rates. However, depending on future traffic and product mix, it could potentially have a material effect on our revenue and profitability. Additionally, we generate leads from which consumers provide a wireless number, and in turn a significant amount of revenue comes from calls made by our internal call centers as well as by third-party call centers. We also purchase a portion of our lead data from third-party publishers and cannot guarantee that these third parties will comply with the regulations. Any failure by us or the third-party publishers on which we rely on for telemarketing, email marketing and other lead generation activities to adhere to or successfully implement appropriate processes and procedures in response to existing regulations and changing regulatory requirements could result in legal liability or damage our reputation in the marketplace, either of which could have a material adverse effect on our business, results of operations and financial condition. Furthermore, our clients may make business decisions based on their own experiences with the TCPA regardless of our products, and the changes we implemented to comply with the new regulations. These decisions may negatively affect our revenue or profitability.

From time to time, we are subject to audits, inquiries, investigations, claims of non-compliance and lawsuits by Federal and state governmental agencies, regulatory agencies, attorneys general, and other governmental or regulatory bodies, any of whom may allege violations of legal requirements. For example, in June 2012, we entered into an Assurance of Voluntary Compliance agreement following a civil investigation into certain of our marketing practices related to our education client vertical that was conducted by the attorneys general of a number of states. If the results of any future investigations, audits, inquiries, claims or litigation are unfavorable to us, we may be required to pay monetary fines or penalties or have restrictions placed on our business, which could materially adversely affect our business, financial condition, results of operations, and cash flows.

We depend on third-party website publishers for a significant portion of our visitors. Any decline in the supply of media available through these websites or increase in the price of this media could cause our revenue to decline or our cost to reach visitors to increase.

A significant portion of our revenue is attributable to visitor traffic originating from third-party publishers. In many instances, website publishers can change the media inventory they make available to us at any time and, therefore, impact our results of operations. In addition, website publishers may place significant restrictions on our offerings. These restrictions may prohibit advertisements from specific clients or specific industries, or restrict the use of certain creative content or formats. If a website publisher decides not to make media inventory available to us, or decides to demand a higher revenue share or places significant restrictions on the use of such inventory, we may not be able to find media inventory from other websites that satisfy our requirements in a timely and cost-effective manner. In addition, the number of competing online marketing service providers and advertisers that acquire inventory from websites continues to increase. Consolidation of Internet advertising networks and website publishers could eventually lead to a concentration of desirable inventory on websites or networks owned by a small number of individuals or entities, which could limit the supply or impact the pricing of inventory available to us. For example, since 2012, our revenue has declined in our financial services client vertical primarily due to volume declines caused by losses of available media from third-party publishers acquired by competitors, changes in search engine algorithms which

reduced or eliminated traffic from some third-party publishers and increased competition for quality media. We cannot assure you that we will be able to acquire media inventory that meets our clients' performance, price and quality requirements, in which case our revenue could decline or our operating costs could increase.

Our operating results have fluctuated in the past and may do so in the future, which makes our results of operations difficult to predict and could cause our operating results to fall short of analysts' and investors' expectations.

Historically, quarterly and annual operating results have fluctuated due to changes in our business, our industry and the general economic climate. We expect our future operating results to vary significantly from quarter to quarter due to a variety of factors, many of which are beyond our control. Our fluctuating operating results could cause our performance and outlook to be below the expectations of securities analysts and investors, causing the price of our common stock to fall. Our business is changing and evolving, and, as a result, our historical operating results may not be useful to you in predicting our future operating results. Factors that may increase the volatility of our operating results include the following:

changes in client volume;

loss of or reduced demand by existing clients;

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the availability and price of quality media;

consolidation of media sources;

changes in search engine algorithms that affect our and our publishers' websites; and

regulatory and legislative changes.

We depend upon Internet search providers to direct a significant portion of the visitors to our and our third-party publishers' websites. Changes in search engine algorithms have in the past and may in the future harm the websites' placements in both paid and organic search result listings, which may cause the number of visitors to our websites, our third-party publishers' websites and our revenue to decline.

Our success depends on our ability to attract online visitors to our and our third-party publishers' websites and convert them into prospects for our clients in a cost-effective manner. We depend on Internet search providers to direct a substantial share of visitors to our websites. Search providers offer two types of search results: organic and paid listings. Organic listings are displayed based solely on formulas designed by the search companies. Paid listings are displayed based on a combination of the advertiser's bid price for particular keywords and the search engines' assessment of the website's relevance and quality.

Our ability to maintain or grow the number of visitors to our websites from search providers is not entirely within our control. Search providers frequently revise their algorithms and changes in their algorithms could cause our websites to receive less favorable placements. We have experienced fluctuations in organic rankings for a number of our websites and some of our paid listing campaigns have also been harmed by search engine algorithmic changes. Search providers could determine that our or our third-party publishers' websites content is either not relevant or is of poor quality. In addition, we may fail to optimally manage our paid listings, or our proprietary bid management technologies may fail. In any of these cases, our websites may receive less favorable placement in organic or paid listings, which would reduce the number of visitors to our sites and have a detrimental effect on our ability to generate revenue. If visits to our websites decrease, we may need to use more costly sources to replace lost visitors, and such increased expense could adversely affect our business and profitability.

If we fail to compete effectively against other online marketing and media companies and other competitors, we could lose clients and our revenue may decline.

The market for online marketing is intensely competitive, and we expect this competition to continue to increase in the future both from existing competitors and, given the relatively low barriers to entry into the market, from new competitors. We compete both for clients and for limited high-quality media. We compete for clients on the basis of a number of factors, including return on investment of client's marketing spending, price and client service.

We compete with Internet and traditional media companies for a share of clients' overall marketing budgets, including:

online marketing or media services providers such as Education Dynamics in the education client vertical and BankRate in the financial services client vertical;

offline and online advertising agencies;

major Internet portals and search engine companies with advertising networks;

other online marketing service providers, including online affiliate advertising networks and industry-specific portals or lead generation companies;

website publishers with their own sales forces that sell their online marketing services directly to clients;

in-house marketing groups and activities at current or potential clients;

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offline direct marketing agencies;

mobile and social media; and

television, radio and print companies.

Competition for web traffic among websites and search engines, as well as competition with traditional media companies, has resulted and may continue to result in significant increases in media pricing, declining margins, reductions in revenue, and loss of market share. In addition, if we expand the scope of our services, we may compete with a greater number of websites, clients and traditional media companies across an increasing range of different services, including in vertical markets where competitors may have advantages in expertise, brand recognition and other areas. Internet search companies with brand recognition, such as Google, Yahoo! and Microsoft, have significant numbers of direct sales personnel and substantial proprietary advertising inventory and web traffic that provide a significant competitive advantage and have a significant impact on pricing for Internet advertising and web traffic. Some of these companies may offer or develop more vertically targeted products that match consumers with products and services and, thus, compete with us more directly. The trend toward consolidation in online marketing may also affect pricing and availability of media inventory and web traffic. Many of our current and potential competitors also enjoy other competitive advantages over us, such as longer operating histories, greater brand recognition, larger client bases, greater access to advertising inventory on high-traffic websites, and significantly greater financial, technical and marketing resources. As a result, we may not be able to compete successfully. Competition from other marketing service providers' online and offline offerings has affected and may continue to affect both volume and price, and, thus, revenue, profit margins and profitability. If we fail to deliver results that are superior to those that other online marketing service providers deliver to clients, we could lose clients, and our revenue may decline.

Federal and state regulations governing clients in our education vertical have negatively affected, and may continue to negatively affect, our clients' businesses, marketing practices and budgets, any or all of which could have a material adverse effect on our financial results.

Historically, we have generated nearly half of our revenue from our education client vertical, and nearly all of that revenue was generated from post-secondary educational institutions. Post-secondary educational institutions are subject to extensive Federal and state regulations, including the Higher Education Act, Department of Education regulations and individual state higher education regulations. The regulations govern many aspects of these clients' operations, including marketing and recruiting activities, as well as the schools' eligibility to participate in Title IV Federal student financial aid programs, which is the principal source of funding for many of our education clients. There have been significant changes to these regulations in the recent past, and a high level of regulatory activity and heightened legislative scrutiny is expected to continue in the post-secondary education sector. Changes in, or new interpretations of, applicable laws, regulations, standards or policies applicable to these clients could have a material adverse effect on their accreditation, authorization to operate in various states, or receipt of funds under Title IV programs, any of which, in turn, may harm our ability to generate revenue from these clients and our financial results.

More people are using mobile devices to access the internet. If we fail to develop our websites to keep pace with this shift in user devices, we may not remain competitive and could lose clients or advertising inventory.

The number of people who access the Internet through mobile devices such as smart phones and tablets has increased dramatically in the past few years, and the trend is expected to continue. Our online marketing services and content were originally designed for desktop or laptop computers. The shift from desktop or laptop computers to mobile devices could potentially deteriorate the user experience for visitors to our websites and may make it more difficult for

visitors to respond to our offerings. It may also require us to develop new offerings specifically designed for mobile devices. Additionally, the monetization of our online marketing services and contents on these mobile devices might not be as lucrative for us compared to those on desktop and laptop computers. If we fail to develop our websites cost effectively and improve our monetization capabilities of our mobile marketing services, we may not remain competitive and may negatively affect our business and operating results.

A substantial portion of our revenue is generated from a limited number of clients and, if we lose a major client, our revenue will decrease and our business and prospects would be harmed.

A substantial portion of our revenue is generated from a limited number of clients. None are 10% or more, however we have a few customers that account for a large portion of our net revenue for the quarter ended December 31, 2013. Our clients can generally terminate their contracts with us at any time, with limited prior notice or penalty as these contracts do not contain penalty provisions for cancellations before the end of the contract term. Our clients may also reduce their level of business with us, leading to lower revenue.

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In addition, reductions in business by one or more significant clients may trigger price reductions for our other clients for products whose prices are determined in whole or in part by client bidding or competition. Any such price reduction could result in lower revenue. We expect that a limited number of clients will continue to account for a significant percentage of our revenue, and the loss of any one of these clients, or material reduction in their marketing spending with us, could decrease our revenue and harm our business.

We rely on our management team and other key employees, and the loss of one or more key employees could harm our business.

Our success and future growth depend upon the continued services of our management team, including Douglas Valenti, Chief Executive Officer, and other key employees in all areas of our organization. From time to time, there may be changes in our key employees resulting from the hiring or departure of executives and employees, which could disrupt our business. We have experienced declines in our business and a depressed stock price, making our equity and cash incentive compensation programs less attractive to current and potential key employees. If we lose the services of key employees or if we are unable to attract and retain additional qualified employees, our business and growth could suffer.

Third-party publishers or vendors may engage in unauthorized or unlawful acts that could subject us to significant liability or cause us to lose clients.

We generate a significant portion of our web visitors from online media that we purchase from third-party website publishers. We also rely on third-party call centers and email marketers. Some of these third-parties are authorized to use our clients' brands, subject to contractual restrictions. Any activity by third-party publishers or vendors that clients view as potentially damaging to their brands can harm our relationship with the client and cause the client to terminate its relationship with us, resulting in a loss of revenue. In addition, we may also face liability for any failure of our third-party publishers or vendors to comply with regulatory requirements, as further described in the risk factor beginning, "Our business is subject to many regulatory requirements, and current or future regulation could have a material adverse effect on our business, results of operations and financial condition."

The law is unsettled on the extent of liability that an advertiser in our position has for the activities of third-party publishers or vendors. Recent Department of Education regulations impose strict liability on our education clients for misrepresentations made by their marketing service providers. In addition, certain of our contracts impose liability on us for the acts of our third-party publishers or vendors. We could be subject to costly litigation and, if we are unsuccessful in defending ourselves, damages for the unauthorized or unlawful acts of third-party publishers or vendors.

We gather, transmit and store consumer personally identifiable information and unauthorized access to or accidental disclosure of this information may cause us to incur significant expenses and may negatively affect our reputation and business.

We gather, transmit and store consumer personally identifiable information. This information may include social security numbers, credit scores, credit card information, and financial and health information, some of which is held and managed by our third-party vendors. As a result, we are subject to certain contractual terms, as well as Federal, state and foreign laws and regulations designed to protect personally identifiable information. Despite our implementation of security measures and controls, our computer systems may be susceptible to electronic or physical computer break-ins, viruses and other disruptions and security breaches. In the past, we have experienced security incidents involving access to our user databases. Although, to our knowledge, no sensitive financial or personal information has been compromised in the past, any future security incidents could result in the compromise of such

data and subject us to liability. In addition, the increased use of mobile devices by our employees increases the risk of unintentional disclosure of personally identifiable information. Any perceived or actual unauthorized disclosure of personally identifiable information, whether through breach of our network by an unauthorized party, employee theft, misuse, or error could harm our reputation, impair our ability to attract website visitors and to attract and retain our clients, or subject us to claims or litigation arising from damages suffered by consumers, and thereby harm our business and operating results. In addition, we could incur significant costs in complying with the multitude of state, Federal and foreign laws regarding personally identifiable information.

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If we fail to continually enhance and adapt our products and services to keep pace with rapidly changing technologies and industry standards, we may not remain competitive and could lose clients or advertising inventory.

The online media and marketing industry is characterized by rapidly changing standards, changing technologies, frequent new product and service introductions, and changing user and client demands. The introduction of new technologies and services embodying new technologies and the emergence of new industry standards and practices could render our existing technologies and services obsolete and unmarketable or require unanticipated investments in technology. We continually make enhancements and other modifications to our proprietary technologies, and these changes may contain design or performance defects that are not readily apparent. If our proprietary technologies fail to achieve their intended purpose or are less effective than technologies used by our competitors, our business could be harmed.

Our future success will depend in part on our ability to successfully adapt to these rapidly changing online media formats and other technologies. If we fail to adapt successfully, we could lose clients or advertising inventory.

Acquisitions and investments could complicate operations, or could result in dilution and other harmful consequences that may adversely impact our business and results of operations.

Acquisitions have historically been an important element of our overall corporate strategy and use of capital. Any possible future acquisitions could be material to our financial condition and results of operations. We may evaluate and enter into discussions regarding a wide array of potential strategic transactions. The process of integrating an acquired company, business or technology has created, and will continue to create, unforeseen operating difficulties and expenditures. The areas where we face risks include:

diversion of management time and focus from operating our business to acquisition integration challenges;

failure to successfully further develop the acquired business or technology;

implementation or remediation of controls, procedures and policies at the acquired company;

integration of the acquired company's accounting, human resource, and other administrative systems, and coordination of product, engineering and sales and marketing functions;

transition of operations, users and customers onto our existing platforms;

failure to obtain required approvals on a timely basis, if at all, from governmental authorities, or conditions placed upon approval, under competition and antitrust laws which could, among other things, delay or prevent us from completing a transaction, or otherwise restrict our ability to realize the expected financial or strategic goals of an acquisition;

in the case of foreign acquisitions, the need to integrate operations across different cultures and languages and to address the particular economic, currency, political and regulatory risks associated with specific countries;

cultural challenges associated with integrating employees from the acquired company into our organization, and retention of employees from the businesses we acquire;

liability for activities of the acquired company before the acquisition, including patent and trademark infringement claims, violations of laws, commercial disputes, tax liabilities and other known and unknown liabilities; and

litigation or other claims in connection with the acquired company, including claims from terminated employees, customers, former stockholders or other third-parties.

Our failure to address these risks or other problems encountered in connection with our past or future acquisitions and investments could cause us to fail to realize the anticipated benefits of such acquisitions or investments, incur unanticipated liabilities and harm our business generally.

Future acquisitions could also result in dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities, amortization expenses, impairment of goodwill or restructuring charges, any of which could harm our financial condition or results. Also, the anticipated benefit of many of our acquisitions may not materialize.

We rely on certain advertising agencies for the purchase of various advertising and marketing services on behalf of their clients. Such agencies may have or develop high-risk credit profiles, which may result in credit risk to us.

A portion of our client business is sourced through advertising agencies and, in many cases, we contract with these agencies and not directly with the underlying client. Contracting with these agencies subjects us to greater credit risk than where we contract with

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clients directly. In many cases, agencies are not required to pay us unless and until they are paid by the underlying client. In addition, many agencies are thinly capitalized and have or may develop high-risk credit profiles. This credit risk may vary depending on the nature of an agency's aggregated client base. If an agency became insolvent, or if an underlying client did not pay the agency, we may be required to write off account receivables as bad debt. Any such write-offs could have a materially negative effect on our results of operations for the periods in which the write-offs occur.

We have a significant amount of debt, which may limit our ability to fund general corporate requirements and obtain additional financing, limit our flexibility in responding to business opportunities and competitive developments and increase our vulnerability to adverse economic and industry conditions.

As of December 31, 2013, we had debt with a principal balance of \$85 million. As a result of obligations associated with our debt, we may not have sufficient liquidity:

to respond to business opportunities, competitive developments and adverse economic conditions;

to fund all of our costs if our revenue declines or costs increase; and

to repay the principal balance of our debt when due.

Our debt obligations may also impair our ability to obtain additional financing, if needed. Our indebtedness is secured by substantially all of our assets, leaving us with limited collateral for additional financing. Moreover, the terms of our indebtedness restrict our ability to take certain actions, including the incurrence of additional indebtedness, certain mergers and acquisitions, investments, asset sales, dividends, and stock repurchases. In addition, even if we are able to raise needed equity financing, we are required to use a portion of the net proceeds of certain types of equity financings to repay the outstanding balance of our term loan. A failure to pay interest or indebtedness when due could result in a variety of adverse consequences, including the acceleration of our indebtedness. In such a situation, it is unlikely that we would be able to fulfill our obligations under our credit facility or repay the accelerated indebtedness or otherwise cover our costs.

Damage to our reputation could harm our business, financial condition and results of operations.

Our business is dependent on attracting a large number of visitors to our and our third-party publishers' websites and providing leads, clicks, calls, and customers to our clients, which depends in part on our reputation within the industry and with our clients. There are companies within our industry that regularly engage in activities that others may view as unlawful or inappropriate. These activities by third-parties, such as spyware or deceptive promotions, may be seen as characteristic of participants in our industry and, therefore, may harm the reputation of all participants in our industry, including us.

Our ability to attract potential consumers and, thereby, clients also depends in part on consumers receiving competitive levels of customer service, responsiveness and prices from our lead purchasers. If lead purchasers do not provide competitive levels of service to consumers, our reputation and our ability to attract clients and consumers could be harmed.

In addition, from time to time, we may be subject to investigations, inquiries or litigation by various regulators, which may harm our reputation regardless of the outcome of any such action. For example, in 2012, we responded to a civil investigation conducted by the attorneys general of a number of states into certain of our marketing and business practices resulting in us entering into an Assurance of Voluntary Compliance agreement. Negative perceptions of our business may result in additional regulation, enforcement actions by the government and increased litigation, any of which may affect our business and result in lower revenue.

Any damage to our reputation, including from publicity from legal proceedings against us or companies that work within our industry, governmental proceedings, consumer class action litigation, or the disclosure of information security breaches or private information misuse, could adversely affect our business, financial condition and results of operations.

If we do not effectively manage any future growth, our operating performance will suffer and we may lose clients.

We have historically experienced growth in our operations and operating locations. This growth placed, and any future growth will continue to place, significant demands on our management and our operational and financial infrastructure. Growth, if any, may make it more difficult for us to accomplish the following:

successfully scale our technology to accommodate a larger business and integrate acquisitions;

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maintain our standing with key vendors, including Internet search companies and third-party website publishers;

maintain our client service standards; and

develop and improve our operational, financial and management controls and maintain adequate reporting systems and procedures.

Our future success depends in part on the efficient performance of our software and technology infrastructure. As the numbers of websites and Internet users increase, our technology infrastructure may not be able to meet the increased demand. Unexpected constraints on our technology infrastructure could lead to slower website response times or system failures and adversely affect the availability of websites and the level of user responses received, which could result in the loss of clients or revenue or harm to our business and results of operations.

In addition, our personnel, systems, procedures, and controls may be inadequate to support our future operations if we return to growth. The improvements required to manage growth may require us to make significant expenditures, expand, train and manage our employee base, and reallocate valuable management resources. If we fail to effectively manage future growth, our operating performance will suffer, and we may lose clients, key vendors and key personnel.

Interruption or failure of our information technology and communications systems could impair our ability to effectively deliver our services, which could cause us to lose clients and harm our operating results.

Our delivery of marketing and media services depends on the continuing operation of our technology infrastructure and systems. Any damage to or failure of our systems could result in interruptions in our ability to deliver offerings quickly and accurately or process visitors' responses emanating from our various web presences. Interruptions in our service could reduce our revenue and profits, and our reputation could be damaged if people believe our systems are unreliable. Our systems and operations are vulnerable to damage or interruption from earthquakes, terrorist attacks, floods, fires, power loss, break-ins, hardware or software failures, telecommunications failures, computer viruses or other attempts to harm our systems, and similar events. If we or third-party data centers that we utilize were to experience a major power outage, we would have to rely on back-up generators. These back-up generators may not operate properly through a major power outage and their fuel supply could also be inadequate during a major power outage or disruptive event. Furthermore, we do not currently have backup generators at our Foster City, California headquarters. Information systems such as ours may be disrupted by even brief power outages, or by the fluctuations in power resulting from switches to and from back-up generators. This could give rise to obligations to certain of our clients which could have an adverse effect on our results for the period of time in which any disruption of utility services to us occurs.

Our primary data center is at a third-party co-location center in San Francisco, California. All of the critical components of the system are redundant and we have a backup data center in Las Vegas, Nevada. We have implemented these backup systems and redundancies to minimize the risk associated with earthquakes, fire, power loss, telecommunications failure, and other events beyond our control; however, these backup systems may fail or not be adequate to prevent losses.

Any unscheduled interruption in our service would result in an immediate loss of revenue. If we experience frequent or persistent system failures, the attractiveness of our technologies and services to clients and website publishers could be permanently harmed. The steps we have taken to increase the reliability and redundancy of our systems are

expensive, reduce our operating margin and may not be successful in reducing the frequency or duration of unscheduled interruptions.

We rely on call centers, Internet and data center providers, and other third-parties for key aspects of the process of providing services to our clients, and any failure or interruption in the services and products provided by these third-parties could harm our business.

We rely on internal and third-party call centers as well as third-party vendors, including data center and Internet providers. Notwithstanding disaster recovery and business continuity plans and precautions instituted to protect our clients and us from events that could interrupt delivery of services, there is no guarantee that such interruptions would not result in a prolonged interruption in our ability to provide services to our clients. Any temporary or permanent interruption in the services provided by our call centers or third-party providers could significantly harm our business.

In addition, any financial or other difficulties our third-party providers face may have negative effects on our business, the nature and extent of which we cannot predict. We exercise little control over our third-party vendors, which increases our vulnerability to

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problems with the services they provide. We license technology and related databases from third-parties to facilitate analysis and storage of data and delivery of offerings. We have experienced interruptions and delays in service and availability for data centers, bandwidth and other technologies in the past. Any errors, failures, interruptions or delays experienced in connection with these third-party technologies and services could adversely affect our business and could expose us to liabilities to third-parties.

We may need additional capital in the future to meet our financial obligations and to pursue our business objectives. Additional capital may not be available or may not be available on favorable terms and our business and financial condition could therefore be adversely affected.

While we anticipate that our existing cash and cash equivalents, together with availability under our credit facility and cash from operations, will be sufficient to fund our operations for at least the next 12 months, we may need to raise additional capital to fund operations in the future or to finance acquisitions. If we seek to raise additional capital in order to meet various objectives, including developing future technologies and services, increasing working capital, acquiring businesses, and responding to competitive pressures, capital may not be available on favorable terms or may not be available at all. In addition, pursuant to the terms of our credit facility, we are required to use a portion of the net proceeds of certain equity financings to repay the outstanding balance of our term loan. Lack of sufficient capital resources could significantly limit our ability to take advantage of business and strategic opportunities. Any additional capital raised through the sale of equity or debt securities with an equity component would dilute our stock ownership. If adequate additional funds are not available, we may be required to delay, reduce the scope of, or eliminate material parts of our business strategy, including potential additional acquisitions or development of new technologies.

Our quarterly revenue and operating results may fluctuate significantly from quarter to quarter due to seasonal fluctuations in advertising spending.

In addition to other factors that cause our operating results to fluctuate, results are also subject to significant seasonal fluctuation. In particular, our quarters ending December 31 (our second fiscal quarter) are typically characterized by seasonal weakness. In our second fiscal quarters, there is generally lower availability of lead supply from some forms of media during the holiday period on a cost effective basis and some of our clients have lower budgets. In our quarters ending March 31 (our third fiscal quarter), this trend generally reverses with better lead availability and often new budgets at the beginning of the year for our clients with fiscal years ending December 31.

If the market for online marketing services fails to continue to develop, our success may be limited, and our revenue may decrease.

The online marketing services market is relatively new and rapidly evolving, and it uses different measurements than traditional media to gauge its effectiveness. Some of our current or potential clients have little or no experience using the Internet for advertising and marketing purposes and have allocated only limited portions of their advertising and marketing budgets to the Internet. The adoption of online marketing, particularly by those entities that have historically relied upon traditional media for advertising, requires the acceptance of a new way of conducting business, exchanging information and evaluating new advertising and marketing technologies and services. In particular, we are dependent on our clients' adoption of new metrics to measure the success of online marketing campaigns. We may also experience resistance from traditional advertising agencies who may be advising our clients. We cannot assure you that the market for online marketing services will continue to grow. If the market for online marketing services fails to continue to develop or develops more slowly than we anticipate, the success of our business may be limited, and our revenue may decrease.

If we do not adequately protect our intellectual property rights, our competitive position and business may suffer.

Our ability to compete effectively depends upon our proprietary systems and technology. We rely on patent, trade secret, trademark and copyright law, confidentiality agreements, and technical measures to protect our proprietary rights. We enter into confidentiality agreements with our employees, consultants, independent contractors, advisors, client vendors, and publishers. These agreements may not effectively prevent unauthorized disclosure of confidential information or unauthorized parties from copying aspects of our services or obtaining and using our proprietary information. Further, these agreements may not provide an adequate remedy in the event of unauthorized disclosures or uses, and we cannot assure you that our rights under such agreements will be enforceable. Effective patent, trade secret, copyright, and trademark protection may not be available in all countries where we currently operate or in which we may operate in the future. Some of our systems and technologies are not covered by any copyright, patent or patent application. We cannot guarantee that: (i) our intellectual property rights will provide competitive advantages to us; (ii) our ability to assert our intellectual property rights against potential competitors or to settle current or future disputes will be

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effective; (iii) our intellectual property rights will be enforced in jurisdictions where competition may be intense or where legal protection may be weak; (iv) any of the patent, trademark, copyright, trade secret or other intellectual property rights that we presently employ in our business will not lapse or be invalidated, circumvented, challenged, or abandoned; (v) competitors will not design around our protected systems and technology; or (vi) that we will not lose the ability to assert our intellectual property rights against others.

We have from time to time become aware of third-parties who we believe may have infringed our intellectual property rights. Such infringement or infringement of which we are not yet aware could reduce our competitive advantages and cause us to lose clients, third-party website publishers or could otherwise harm our business. Policing unauthorized use of our proprietary rights can be difficult and costly. Litigation, while it may be necessary to enforce or protect our intellectual property rights, could result in substantial costs and diversion of resources and management attention and could adversely affect our business, even if we are successful on the merits. In addition, others may independently discover trade secrets and proprietary information, and in such cases we could not assert any trade secret rights against such parties.

Third-parties may sue us for intellectual property infringement, which, even if unsuccessful, could require us to expend significant costs to defend or settle.

We cannot be certain that our internally developed or acquired systems and technologies do not and will not infringe the intellectual property rights of others. In addition, we license content, software and other intellectual property rights from third-parties and may be subject to claims of infringement if such parties do not possess the necessary intellectual property rights to the products they license to us.

In addition, we have in the past, and may in the future, be subject to legal proceedings and claims that we have infringed the patents or other intellectual property rights of third-parties. These claims sometimes involve patent holding companies or other adverse patent owners who have no relevant product revenue and against whom our own intellectual property rights, if any, may therefore provide little or no deterrence. For example, in December 2012, Internet Patents Corporation (IPC) filed a patent infringement lawsuit against us in the Northern District of California alleging that some of our websites infringe a patent held by IPC. IPC is a non-practicing entity that relies on asserting its patents as its primary source of revenue. In addition, third-parties have asserted and may in the future assert intellectual property infringement claims against our clients, and we have agreed in certain circumstances to indemnify and defend against such claims. Any intellectual property-related infringement claims, whether or not meritorious and regardless of the outcome of the litigation, could result in costly litigation and could divert management resources and attention. Should we be found liable for infringement, we may be required to enter into licensing agreements, if available on acceptable terms or at all, pay substantial damages, or limit or curtail our systems and technologies. Moreover, we may need to redesign some of our systems and technologies to avoid future infringement liability. Any of the foregoing could prevent us from competing effectively and increase our costs.

Additionally, the laws relating to use of trademarks on the Internet are unsettled, particularly as they apply to search engine functionality. For example, other Internet marketing and search companies have been sued for trademark infringement and other intellectual property-related claims for displaying ads or search results in response to user queries that include trademarked terms. The outcomes of these lawsuits have differed from jurisdiction to jurisdiction. We may be subject to trademark infringement, unfair competition, misappropriation or other intellectual property-related claims which could be costly to defend and result in substantial damages or otherwise limit or curtail our activities, and therefore adversely affect our business or prospects.

Limitations on our ability to collect and use data derived from user activities could significantly diminish the value of our services and have an adverse effect on our ability to generate revenue.

When a user visits our websites, we use technologies, including cookies, to collect information such as the user's IP address and the user's past responses to our offerings. We access and analyze this information in order to determine the effectiveness of a marketing campaign and to determine how to modify the campaign. The use of cookies is the subject of litigation, regulatory scrutiny and industry self-regulatory activities, including the discussion of do-not-track technologies and guidelines.

Additionally, users are able to block or delete cookies from their browser. Periodically, certain of our clients and publishers seek to prohibit or limit our collection or use of this data. Interruptions, failures or defects in our data collection systems, as well as privacy concerns regarding the collection of user data, could also limit our ability to analyze data from our clients' marketing campaigns. This risk is heightened when we deliver marketing services to clients in the financial services client vertical. If our access to data is limited in the future, we may be unable to provide effective technologies and services to clients and we may lose clients and revenue.

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If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements on a timely basis could be impaired, which would adversely affect our ability to operate our business.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. We may in the future discover areas of our internal financial and accounting controls and procedures that need improvement. Our internal control over financial reporting will not prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. All control systems have inherent limitations, and, accordingly, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud will be detected. If we are unable to maintain proper and effective internal controls, we may not be able to produce accurate financial statements on a timely basis, which could adversely affect our ability to operate our business and could result in regulatory action.

As a creator and a distributor of Internet content, we face potential liability and expenses for legal claims based on the nature and content of the materials that we create or distribute. If we are required to pay damages or expenses in connection with these legal claims, our operating results and business may be harmed.

We display original content and third-party content on our websites and in our marketing messages. As a result, we face potential liability based on a variety of theories, including defamation, negligence, deceptive advertising (including Department of Education regulations regarding misrepresentation in education marketing), copyright or trademark infringement. We are also exposed to risk that content provided by third-parties is inaccurate or misleading, and for material posted to our websites by users and other third-parties. These claims, whether brought in the United States or abroad, could divert management time and attention away from our business and result in significant costs to investigate and defend, regardless of the merit of these claims. In addition, if we become subject to these types of claims and are not successful in our defense, we may be forced to pay substantial damages.

We face additional risks in conducting business in international markets.

We have entered into certain international markets and may enter into additional international markets in the future. We have limited experience in marketing, selling and supporting our services outside of the United States, and we may not be successful in introducing or marketing our services abroad. There are risks and challenges inherent in conducting business in international markets, such as:

adapting our technologies and services to foreign clients' preferences and customs;

successfully navigating foreign laws and regulations, including marketing, privacy regulations, employment and labor regulations;

changes in foreign political and economic conditions;

tariffs and other trade barriers, fluctuations in currency exchange rates and potentially adverse tax consequences;

language barriers or cultural differences;

reduced or limited protection for intellectual property rights in foreign jurisdictions;

difficulties and costs in staffing, managing or overseeing foreign operations;

education of potential clients who may not be familiar with online marketing;

challenges in collecting accounts receivables; and

successfully interpreting and complying with the U.S. Foreign Corrupt Practices Act and similar worldwide anti-bribery laws, particularly when operating in countries with varying degrees of governmental corruption.

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If we are unable to successfully expand and market our services abroad, our business and future growth may be harmed, and we may incur costs that may not lead to future revenue.

We recognized an impairment in the carrying value of goodwill. Additional such charges in the future could negatively affect our operating results and financial condition.

We continue to have a substantial amount of goodwill and purchased intangible assets on our balance sheet as a result of historical acquisitions. The carrying value of goodwill represents the fair value of an acquired business in excess of identifiable assets and liabilities as of the acquisition date. The carrying value of intangible assets with identifiable useful lives represents the fair value of relationships, content, domain names, acquired technology, among others, as of the acquisition date, and are amortized based on their economic lives. Goodwill expected to contribute indefinitely to our cash flows is not amortized, but must be evaluated for impairment at least annually. If the carrying value exceeds current fair value as determined based on the discounted future cash flows of the related business, the goodwill or intangible asset is considered impaired and is reduced to fair value via a non-cash charge to earnings. Events and conditions that could result in impairment include adverse changes in the regulatory environment, a reduced market capitalization or other factors leading to reduction in expected long-term growth or profitability.

Goodwill impairment analysis and measurement is a process that requires significant judgment. Our stock price and any estimated control premium are factors affecting the assessment of the fair value of our underlying reporting units for purposes of performing any goodwill impairment assessment. For example, our public market capitalization sustained a decline after December 31, 2012 to a value below the net book carrying value of our equity, triggering the need for a goodwill impairment analysis. As a result of our goodwill impairment analysis, we recorded a goodwill impairment charge of \$92.4 million in the second quarter of fiscal year 2013.

It is possible that another material change could occur in the future. We will continue to conduct impairment analyses of our goodwill on an annual basis, unless indicators of possible impairment arise that would cause a triggering event, and we would be required to take additional impairment charges in the future if any recoverability assessments reflect estimated fair values that are less than our recorded values. Further impairment charges with respect to our goodwill could have a material adverse effect on our results of operations and financial condition.

We could lose clients if we fail to detect click-through or other fraud on advertisements in a manner that is acceptable to our clients.

We are exposed to the risk of fraudulent clicks or actions on our websites or our third-party publishers' websites, which could lead the clients to become dissatisfied with our campaigns, and in turn, lead to loss of clients and related revenue. Click-through fraud occurs when an individual clicks on an ad displayed on a website or an automated system is used to create such clicks with the intent of generating the revenue share payment to the publisher rather than to view the underlying content. Action fraud occurs when online forms are completed with false or fictitious information in an effort to increase a publisher's compensable actions. From time to time, we have experienced fraudulent clicks or actions. We do not charge our clients for fraudulent clicks or actions when they are detected, and such fraudulent activities could negatively affect our profitability or harm our reputation. If fraudulent clicks or actions are not detected, the affected clients may experience a reduced return on their investment in our marketing programs, which could lead the clients to become dissatisfied with our campaigns, and in turn, lead to loss of clients and the related revenue. Additionally, we have, from time to time, had to, and in the future may have to, terminate relationships with publishers who we believed to have engaged in fraud. Termination of such relationships entails a loss of revenue associated with the legitimate actions or clicks generated by such publishers.

Risks Related to the Ownership of Our Common Stock

Our stock price has been volatile, and you may not be able to resell shares of our common stock at or above the price you paid.

The trading price of our common stock has been volatile since our initial public offering and may continue to be subject to wide fluctuations in response to various factors, some of which are beyond our control. These factors include those discussed in this Risk Factors section of this periodic report and others such as:

our ability to return to growth and to manage any such growth effectively;

changes in earnings estimates or recommendations by securities analysts;

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announcements about our revenue, earnings or other financial results that are not in line with analyst expectations;

our ability to find, develop or retain high quality targeted media on a cost effective basis;

relatively low trading volume in our stock creates inherent volatility regardless of factors related to our business performance or prospects;

the sale of, or indication of the intent to sell, substantial amounts of our common stock by our directors, officers or substantial shareholders;

announcements by us or our competitors of new services, significant contracts, commercial relationships, acquisitions or capital commitments;

our commencement of, or involvement in, litigation; and

negative publicity about us, our industry, our clients or our clients' industries.

In recent years, the stock market in general, and the market for technology and Internet-based companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may seriously affect the market price of our common stock, regardless of our actual operating performance. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company's securities, securities class action litigation has often been instituted against these companies. Such litigation, if instituted against us, could result in substantial costs and a diversion of our management's attention and resources.

If securities or industry analysts do not publish research or reports about our business, or if they issue an adverse opinion regarding our stock, our stock price and trading volume could decline.

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about us, our business or the industries or businesses of our clients. If any of the analysts issue an adverse opinion regarding our stock or if our actual results do not meet analyst estimates, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

Our directors and executive officers and their respective affiliates have substantial influence over us and could delay or prevent a change in corporate control.

As of December 31, 2013, our directors and executive officers, together with their affiliates, beneficially owned approximately 25% of our outstanding common stock. As a result, these stockholders, acting together, have substantial influence over the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, consolidation or sale of all or substantially all of our assets. In addition, these stockholders, acting together, have significant influence over the management and affairs of our company. Accordingly, this

concentration of ownership may have the effect of:

delaying, deferring or preventing a change in corporate control;

impeding a merger, consolidation, takeover or other business combination involving us; or

discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of us.

Provisions in our charter documents under Delaware law and in contractual obligations could discourage a takeover that stockholders may consider favorable and may lead to entrenchment of management.

Our amended and restated certificate of incorporation and bylaws contain provisions that could have the effect of delaying or preventing changes in control or changes in our management without the consent of our board of directors. These provisions include:

a classified board of directors with three-year staggered terms, which may delay the ability of stockholders to change the membership of a majority of our board of directors;

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no cumulative voting in the election of directors, which limits the ability of minority stockholders to elect director candidates;

the exclusive right of our board of directors to elect a director to fill a vacancy created by the expansion of the board of directors or the resignation, death or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;

the ability of our board of directors to determine to issue shares of preferred stock and to determine the price and other terms of those shares, including preferences and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;

a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;

the requirement that a special meeting of stockholders may be called only by the chairman of the board of directors, the chief executive officer or the board of directors, which may delay the ability of our stockholders to force consideration of a proposal or to take action, including the removal of directors; and

advance notice procedures that stockholders must comply with in order to nominate candidates to our board of directors or to propose matters to be acted upon at a stockholders' meeting, which may discourage or deter a potential acquiror from conducting a solicitation of proxies to elect the acquiror's own slate of directors or otherwise attempting to obtain control of us.

We are also subject to certain anti-takeover provisions under Delaware law. Under Delaware law, a corporation may not, in general, engage in a business combination with any holder of 15% or more of its capital stock unless the holder has held the stock for three years or, among other things, the board of directors has approved the transaction.

We do not currently intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.

We currently have not and do not intend to declare and pay dividends on our common stock for in the near term. We currently intend to invest our future earnings, if any, to fund our growth. Additionally, the terms of our credit facility restrict our ability to pay dividends. Therefore, you are not likely to receive any dividends on your common stock in the near term.

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

Unregistered Sales of Equity Securities

None.

Purchases of Equity Securities by QuinStreet

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

None.

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ITEM 6. EXHIBITS

Exhibit

Number	Description of Document
10.1 ⁽¹⁾	Amendment to Consulting Services Agreement dated October 30, 2013 to the Transition Agreement dated September 18, 2013 between the Company and Bronwyn Syiek.
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

⁽¹⁾ Incorporated by reference in exhibit 10.3 to QuinStreet, Inc. s Quarterly Report on Form 10-Q (SEC File No.001-34628) filed November 6, 2013.

* Filed herewith.
Furnished herewith.

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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.

QUINSTREET, INC.

/s/ Gregory Wong

Gregory Wong

Chief Financial Officer and Senior Vice

President

(Principal Financial and Accounting Officer
and duly authorized signatory)

Date: February 7, 2014

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INDEX TO EXHIBITS

Exhibit	
Number	Description of Document
10.1 ⁽¹⁾	Amendment to Consulting Services Agreement dated October 30, 2013 to the Transition Agreement dated September 18, 2013 between the Company and Bronwyn Syiek.
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