Net Element, Inc.
Form S-3/A
February 14, 2018

As filed with the Securities and Exchange Commission on February 14, 2018

File No. 333-222466

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

AMENDMENT NO. 2

TO

FORM S-3

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

NET ELEMENT, INC.

(Exact name of registrant as specified in its charter)

Delaware	**90-1025599**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3363 NE 163rd St., Suite 705
North Miami Beach, Florida 33160
(305) 507-8808

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Jonathan New

Chief Financial Officer

Net Element, Inc.
3363 NE 163rd St., Suite 705
North Miami Beach, Florida 33160
(305) 507-8808

(Name, address, including zip code, and telephone number,
including area code, of agent for service)

with a copy to:

Serge Pavluk, Esq.

Snell & Wilmer L.L.P.

350 South Grand Avenue, 31st Floor

Los Angeles, California 90071-3406

Telephone: (213) 929-2500

Approximate date of commencement of proposed sale to the public: From time to time after this Registration Statement becomes effective.

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. ¨

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. x

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box. ¨

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box. ¨

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

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

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	**Amount to be Registered**[4]	**Proposed Maximum Offering Price Per Security**[1]	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee	
Common Stock, par value $0.0001 per share	350,553	$ 6.68	$ 2,341,694.04	$ 291.54	
Common Stock underlying Purchase Warrants[2]	404,676	$ 6.68	$ 2,703,235.68	$ 336.55	
Common Stock underlying Pre-Funded Warrants[3]	323,907	$ 6.68	$ 2,163,698.76	$ 269.38	
Total	1,079,136		$ 7,208,628.48	$ 897.47	(5)

(1) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(c) under the Securities Act, based upon the average of the high and low prices of the common stock on the NASDAQ Capital Market on February 13, 2018.

(2) Represents shares of Common Stock, par value $0.0001 per share, issuable upon the exercise of five-year warrants at an exercise price of $11.12 per share (the "Purchase Warrants").

(3) Represents shares of Common Stock, par value $0.0001 per share, issuable upon the exercise of five-year pre-paid warrants at an exercise price of $0.01 per share (the "Pre-Funded Warrants").

(4) Pursuant to Rule 416 under the Securities Act of 1933, as amended (the "Securities Act"), this registration statement also covers any indeterminate number of additional shares of common stock issuable upon stock splits, stock dividends, dividends or other distributions, recapitalizations or similar events with respect to the shares of common stock being registered pursuant to this registration statement.

(5) $1,801.67 of the filing fee was previously paid by the Registrant on January 8, 2018 in connection with the filing of Registrant's registration statement on Form S-3 (File No. 333-222466), which is amended hereby.

The Registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act or until this registration statement shall become effective on such date as the Securities and Exchange Commission (the "Commission"), acting pursuant to said Section 8(a), may determine.

The information in this prospectus is not complete and may be changed. The selling stockholder may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities, and the selling stockholder is not soliciting offers to buy these securities, in any state where the offer or sale of these securities is not permitted.

SUBJECT TO COMPLETION, DATED FEBRUARY 14, 2018

PRELIMINARY PROSPECTUS

NET ELEMENT, INC.

1,079,136 Shares

Common Stock

This prospectus relates to the sale of up to 1,079,136 shares of common stock of Net Element, Inc., a Delaware corporation ("us", "we", "our", "Net Element", or the "Company"), by Esousa Holdings LLC, a New York limited liability company. Esousa Holdings LLC is also referred to in this prospectus as the selling stockholder.

Such shares include (i) 350,553 shares of common stock of the Company issued on December 29, 2017 (the "Purchase Shares"), (ii) 404,676 shares of common stock of the Company issuable upon the valid exercise of five-year warrants at an exercise price of $11.12 per share (the "Purchase Warrant Shares"), and (iii) 323,907 shares of common stock of the Company issuable on the valid exercise of five-year pre-paid warrants at an exercise price of $0.01 per share (the "Pre-Funded Warrant Shares"). The Purchase Shares, Purchase Warrant Shares and the Pre-Funded Warrant Shares are referred to collectively as the "Shares."

The prices at which the selling stockholder may sell the Shares will be determined by the prevailing market price for the Shares or in negotiated transactions or through other means described in the section entitled "Plan of Distribution" or a supplement to this prospectus. The selling stockholder may also sell the shares under Rule 144 under the Securities Act of 1933, as amended, if available, rather than under this prospectus. We will not receive proceeds from the sale of the Shares by the selling stockholder. However, we may receive proceeds from the exercise of the five-year warrants at an exercise price of $11.12 per share (the “Purchase Warrants”) and the five-year pre-paid warrants at an exercise price of $0.01 per share (the “Pre-Funded Warrants;” together with the Purchase Warrants, the “Warrants”) held by the selling stockholder when exercised, which, if exercised in cash at the current applicable exercise price with respect to all of the Warrants, would result in gross proceeds to the Company of $4,503,236.19. We will pay the expenses of registering the Shares, but all selling and other expenses incurred by the selling stockholder will be paid by the selling stockholder.

We are registering the offer and sale of the Shares pursuant to certain registration rights granted to the selling stockholder for the continuous resale at market by the selling stockholder. The registration of the Shares does not necessarily mean that any of the Shares will be offered or sold by the selling stockholder. The timing and amount of any sale is within the sole discretion of the selling stockholder.

Our common stock is listed on the Nasdaq Capital Market under the ticker symbol “NETE.” On February 13, 2018, the last reported sale price per share of our common stock was $6.56 per share.

You should read this prospectus and any prospectus supplement, together with additional information described under the headings “Incorporation of Certain Documents by Reference” and “Where You Can Find More Information,” carefully before you invest in any of our securities.

Investing in our securities involves a high degree of risk. See “Risk Factors” on page 6 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 14, 2018

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ABOUT THIS PROSPECTUS

You should rely only on the information contained or incorporated by reference in this prospectus and any prospectus supplement or issuer free writing prospectus relating to the offering of our common stock by the selling stockholder. No one has been authorized to provide you with information that is different from that contained or incorporated by reference in this prospectus, any accompanying prospectus supplement and any related issuer free writing prospectus in connection with the offering described herein and therein, and, if given or made, such information or representations must not be relied upon as having been authorized by us. Neither this prospectus nor any prospectus supplement nor any related issuer free writing prospectus shall constitute an offer to sell or a solicitation of an offer to buy offered securities in any jurisdiction in which it is unlawful for such person to make such an offering or solicitation.

You should read the entire prospectus and any prospectus supplement and any related issuer free writing prospectus, as well as the documents incorporated by reference into this prospectus or any prospectus supplement or any related issuer free writing prospectus, before making an investment decision. Neither the delivery of this prospectus or any prospectus supplement or any issuer free writing prospectus nor any sale made hereunder shall under any circumstances imply that the information contained or incorporated by reference herein or in any prospectus supplement or issuer free writing prospectus is correct as of any date subsequent to the date hereof or of such prospectus supplement or issuer free writing prospectus, as applicable. You should assume that the information appearing in this prospectus, any prospectus supplement or any document incorporated by reference is accurate only as of the date of the applicable documents, regardless of the time of delivery of this prospectus or any sale of securities. Our business, financial condition, results of operations and prospects may have changed since that date.

PROSPECTUS SUMMARY

This summary highlights certain information about us, this offering and selected information contained in the prospectus. This summary is not complete and does not contain all of the information that you should consider before deciding whether to invest in our common stock. For a more complete understanding of our company and this offering, we encourage you to read and consider the more detailed information in the prospectus, including "Risk Factors" and the financial statements and related notes. Unless we specify otherwise, all references in this prospectus to "Net Element," "we," "our," "us" and "our company" refer to NET ELEMENT, INC.

Unless otherwise indicated all historical and pro forma common stock and per share data in this prospectus have been retroactively restated to the earliest period presented to account for the 1-for-10 reverse stock split that became effective on October 5, 2017.

Information About the Company

Background and Business

Company Overview

Net Element is a global financial technology and value-added solutions group that supports companies in accepting electronic payments in an omni-channel environment that spans across point-of-sale ("POS"), e-commerce and mobile devices. The Company operates in three segments as a provider of North America Transaction Solutions, Mobile Payment Solutions and Online Payment Solutions.

We enable merchants of all sizes to accept and process over 100 different payment options in more than 40 currencies, including credit, debit and prepaid payments. We also provide merchants with value-added services and technologies including integrated payment technologies, POS solutions, security solutions, fraud management, information solutions and analytical tools.

We provide a range of solutions to our clients across the value chain of commerce-enabling services and technologies. We create our value-added solutions from a suite of proprietary technology products which includes cloud-based applications, processing services, security offerings, and customer support programs that we configure to meet our clients' individual needs.

We provide additional services including:

- POS solutions and other adjacent business services throughout the United States provided by TOT Payments doing business as ***Unified Payments***;
- Proprietary cloud-based POS platform for the hospitality industry and small to medium sized businesses ("SMB") merchants through ***Aptito*** and ***Restoactive***;
- Proprietary integrated, global e-commerce and mobile payments processing platform and fraud management system through ***PayOnline***;
- Integrated payment processing solutions to the travel industry, which includes integrations with various Global Distribution Systems ("GDS") such as Amadeus®, Galileo®, Sabre®, additional geo filters and passenger name record (PNR) through Pay-Travel service offered by ***PayOnline***;
- PayNet Solutions – universal payment platform provided by ***PayOnline*** (software-as-a-service ("SaaS") and White Label models). Providing an opportunity for top clients of ***PayOnline*** to develop their own independent business solutions.
- Direct-carrier, mobile operator solutions for small ticket content providers and merchants throughout selected international markets provided by ***Digital Provider***.

We have operations and offices located within the United States ("U.S.") (domestic) and outside of the U.S. (international) where sales, customer service and/or administrative personnel are based. Through U.S. based subsidiaries, we generate revenues from transactional services, valued-added payment services and technologies for SMBs. Through wholly owned subsidiaries, we operate internationally with a focus on transactional services, mobile payment transactions, online payment transactions, value-added payment services and technologies in selected international markets.

Our business is characterized by transaction related fees, multi-year contracts, and a diverse client base which allows us to grow alongside our clients. Our multi-year contracts allow us to achieve a high level of recurring revenues. While the contracts typically do not specify fixed revenues to be realized thereunder, they do provide a framework for revenues to be generated based on volume of services provided during the contract's term.

In August 2017, we substantially reorganized the business of Digital Provider and consolidated its operations into PayOnline and TOT Group Russia. We currently are not generating revenues from new content, and we continue to explore partnership opportunities that can monetize our relationships and contracts with mobile operators.

Our Corporate Organization

Our Company was formed in 2010 and incorporated as a Cayman Islands exempted company with limited liability under the name Cazador Acquisition Corporation Ltd. ("Cazador"). Cazador was a blank check company incorporated for the purpose of effecting a merger; share capital exchange; asset acquisition; share purchase; reorganization or similar business combination with one or more operating businesses or assets. In 2012, Cazador completed a merger (the "Merger") with Net Element, Inc., a Delaware corporation ("Pre-Merger Net Element"), which was a company with businesses in the online media and mobile commerce payment processing markets. Immediately prior to the effectiveness of the Merger, the Company (then known as Cazador) changed its jurisdiction of incorporation by discontinuing as an exempted company in the Cayman Islands and continuing and domesticating as a corporation incorporated under the laws of the State of Delaware. Effective upon consummation of the Merger, (i) Pre-Merger Net Element was merged with and into the Company, resulting in Pre-Merger Net Element ceasing to exist and the Company continuing as the surviving company in the Merger, and (ii) the Company changed its name to Net Element International, Inc. In 2013, the Company divested its non-core entertainment assets. In December 2013, the Company changed its name to Net Element, Inc. We entered the mobile payments business through the launch of Tot Money (renamed Digital Provider in 2015) in Russia in 2012. We entered the financial technology and value-added transactional service business through the acquisitions of Unified Payments in April 2013 and Aptito in June 2013. We entered the online payment business with our acquisition of PayOnline in May 2015.

Additional Information

Our principal office is located at 3363 NE 163rd Street, Suite 705, North Miami Beach, Florida 33160, and our main telephone number is (305) 507-8808. Our website address is www.netelement.com. The information on our website is not a part of, and should not be construed as being incorporated by reference into, this prospectus.

The Offering

Common stock being offered by the selling stockholder	Up to 1,079,136 Shares, including 350,553 Purchase Shares, 404,676 Purchase Warrant Shares, and 323,907 Pre-Funded Warrant Shares.
Common stock outstanding	3,862,352 (as of February 14, 2018)
Use of proceeds	The selling stockholder will receive all of the proceeds from the sale of the shares offered for sale by it under this prospectus. We will not receive proceeds from the sale of the shares by the selling stockholder. We will, however, receive the exercise price of the Purchase Warrants (with the exercise price of $11.12 per share) and the Pre-Funded Warrants (with the exercise price of $0.01 per share) held by the selling stockholder if and when exercised by the selling stockholder exercised in cash, which, if exercised in cash at the current applicable exercise price with respect to all of the Warrants, would result in gross proceeds to the Company of $4,503,236.19.
Nasdaq Capital Market Symbol	NETE
Risk Factors	Investing in our securities involves a high degree of risk. You should carefully review and consider the “Risk Factors” section of this prospectus for a discussion of factors to consider before deciding to invest in shares of our common stock.

Recent Events

Development of the Company's anticipated blockchain technology solutions

We believe that one of the key roles of the blockchain ecosystem in the commerce environment is to facilitate transactions and serve as a frictionless and secure payment platform with an ability to encourage innovation through value-added services introduced on the platform and cater to both merchants and their customers.

We are developing a decentralized crypto-based ecosystem to act as a framework for a number of value-added services that can connect merchants and consumers directly utilizing blockchain technology while increasing the economic efficiency of all transactions being made within the ecosystem. Specifically, we launched a platform called Netevia that delivers end-to-end payment processing through easy-to-use APIs and complements the Company's ability to perform in a multi-channel environment, including point-of-sale (POS), e-commerce, mobile devices and will enable the Company to perform in decentralized blockchain technology solutions. The Company is working to implement additional features on the platform, which will include default value-added modules, such as payments platform technology solution, peer-to-peer interface solution and blockchain rewards system solution. We expect that the users of our blockchain based payments solution, when such solution is fully implemented, will be able to make payments by using payments options of their preference: fiat money, mainstream and alternative cryptocurrencies. The main function of the blockchain based payments solution is to provide the "one-click" payment technology solution with minimum transaction costs and maximum comfort for the users. We expect that such function will be complementary to our current platform which supports multiple payment methods internationally. We also expect that the peer-to-peer module will allow participants to transact directly using blockchain technology and support conversion and transmittal of multiple payment methods including traditional payment methods, mainstream and alternative cryptocurrencies, and the rewards system that will reward users for active use of the ecosystem and contributions into its development.

In providing such blockchain technology solutions, we will not be holding any deposits, nor trade in, digital assets. We are committed to comply with the government regulations applicable to our blockchain technology solutions.

In December of 2017, we partnered with Bunker Capital to develop and deploy such blockchain technology-based solutions. The terms of such relationships with Bunker Capital is for Bunker Capital to assist the Company with its development of the blockchain technology, connection and the development of smart contracts, suitable models, and implementation of an initial coin offering. As of the date of filing of this registration statement, the Company has been focused on the development of the blockchain technology solutions and has not made any commitment related to any digital securities offering and/or an initial coin offering should the Company decide to pursue such an offering. As of the date of filing of this registration statement, Bunker Capital has not performed for the Company any services related to any digital securities offering and/or an initial coin offering. The Company and Bunker Capital continue to work on the business plan for such blockchain technology-based solutions, and the Company has assembled a team of software engineers to continue working on its blockchain technology platform.

When such blockchain technology solutions are fully implemented, we expect that our core business, a technology and value-added solutions that support electronic payments acceptance in an multi-channel environment including point-of-sale (POS), e-commerce and mobile devices will be complimented by such blockchain ecosystem.

In addition to the blockchain based ecosystem, we are working to identify and invest into unique projects which decentralize and disrupt the transaction processing industry by combining blockchain technology and real world applications and, accordingly, we may determine in the future to pursue or develop such other projects. Specifically, our framework includes identifying and investing in companies that will be able to add value in the ecosystem that we serve, particular address the following criteria:

- Differentiation point
- Distribution / Market penetration
- Value-added technology or service

Even though, we do not look to invest into start-ups or projects that do not have a defined market penetration strategy, we will consider investing into technologies that fit into our ecosystem. The Company does not intend to make any minority investments, but rather we intent to hold majority positions and full operational control over any investments we make. The Company does not have plans to hold or trade digital assets or cryptocurrencies at this time.

On February 7, 2018, Net Element launched future-ready multi-channel payments platform, Netevia. Connecting and simplifying payments across sales channels through a single integration point, Netevia delivers end-to-end payment processing though easy-to-use APIs. This model complements Net Element’s ability to perform in a multi-channel environment, including point-of-sale (POS), e-commerce, mobile devices and will when such blockchain technology solutions are fully implemented enable the Company to perform in blockchain technology solutions.

Netevia will form part of the recently announced decentralized blockchain technology solutions that enable an unlimited number of value-added services to connect merchants and consumers via blockchain technology, while increasing economic efficiency of all transactions made within the ecosystem. The first implementation of the ecosystem will be deployed on the public Ethereum or similar blockchain and adhere to the ERC20 protocol.

Retailers and services providers are struggling with inefficient and costly payment mechanisms, which have not kept pace with global commerce and remain to be flat. Netevia’s blockchain solution code named “VIA Protocol” under development, is intended to solve this problem by utilizing smart contract architecture and a value transfer protocol, which enable new billing methodologies over the blockchain as well as create dynamic services offerings such as rewards, loyalty and one-click payments. In addition, VIA Protocol will enable use of cryptocurrency as a payment method in a multi-channel commerce and significantly increase the total volume of payments transacted utilizing blockchain technology.

VIA Protocol will be a comprehensive solution which offers robust payment mechanism far more credible, efficient, flexible, cost-effective, and scalable than current implementations. Unlike today's payment methods, which include main stream and alternative payment methods, VIA Protocol is being designed utilizing best standards of existing blockchain protocols such as BIP-70, as well as extending their functionality with standards of fiat payment methods such as Level 3 transactional data, specifically to overcome existing multi-channel payment problems and offer a set of tools developed to facilitate onboarding processes for both merchants and customers. In addition, VIA Protocol will increase economic efficiency, reduce friction, and minimize risks by removing intermediaries such as credit card companies, charging excessive fees such as interchange.

To make instant payment acceptance available to our merchants at the point of sale from variety of blockchain wallets we are required to offer real-time exchange of cryptocurrency into fiat. To facilitate this process, Netevia will be integrated into cryptocurrency facilitator such as blockpay.ch, shapeshift.io or others that are able to offer reliable solution. VIA Protocol will provide technological solutions to support payment acceptance in mainstream cryptocurrencies, which include Bitcoin, Ethereum and Litecoin, as well as alternative cryptocurrencies such as Dash and Ripple.

VIA Protocol will be built around smart contracts that govern transaction behavior. It can be set as a simple single transaction, a complex transaction that includes, among others, recurring payments, pay-per-use payments, split payments, exchange rate corrections or a combination of the above. Businesses may use VIA Protocol's payment mechanism as is or modify and/or create new ones to fit their needs using Netevia's user-friendly developer center.

The solutions offered by VIA Protocol will create business opportunities for external third party companies that can build additional value-added services on top of the VIA Protocol and contribute to the Netevia ecosystem. These companies include, but are not limited to, credit network companies, mobile network operators, rewards networks, content providers, billing companies, merchant cash advance providers, supply-chain managers, social media, and others.

VIA Protocol will be promoted through partnerships with merchants and independent sales groups, by encouraging them to adopt Netevia ecosystem from the onset. Through system integrators and developers, VIA Protocol will plug into industries throughout numerous markets. With new features to be implemented on the platform, Netevia plans to disrupt everyday commerce.

First value-added application will be based on multi-channel loyalty / rewards system and will reward customers for making purchases using cryptocurrencies or other payment methods at the point of sale. Netevia will introduce a point reward system available for both merchants and its customers.

Our core principals are to provide transparency for payments management, financial management, code management and business practices for merchants, we will strive to maintain high standard for honesty, ethical business conduct and compliance with applicable laws, rules, and regulations for the users.

We estimate that the initial phase costs of the project will be approximately $500,000. The Company began its development and has already launched first part of the Netevia project as noted in the press release dated February 7,

2018. Scope of the initial phase:

- Use of Ethereum or any other platform to develop reliable blockchain ecosystem
- Preparation of standard API for payment flow. Authorization/Capture/Hold/Void/Refund/Add tips (integration with the cryptocurrency facilitator such as blockpay.ch or others that are able to offer reliable solution)
- Use of smart contract technology as part of the API available to developers
- Addition of conversion tool for initial payment acceptance (economic model to charge discount rate to merchants)
- Evaluate mechanism to issue refunds/holds
- Settlement mechanism and process
- Wallet apps for users
- Integrations into POS systems
- Introduction of VIA Protocol

While the Company expects that funding of the project will be from current funds held by the Company, which is sufficiently funded to absorb such costs, the Company has yet to approximate its capital needs and might require additional capital to fully utilize its business plan on a go forward basis as the Company develops and deploys the ecosystem, cost of development of the ecosystem, value-added solutions as well as deployment and distribution costs.

Our core principals are to provide transparency for payments management, financial management, code management and business practices for merchants, we will strive to maintain high standard for honesty, ethical business conduct and compliance with applicable laws, rules, and regulations for the users.

Private Placement of Common Stock and Warrants

On December 29, 2017, we entered into, and consummated the transactions contemplated by, a Unit Purchase Agreement (the "Purchase Agreement") with Esousa Holdings LLC ("Esousa"). Pursuant to the Purchase Agreement, on December 29, 2017 (the "Closing Date"), the Company sold to Esousa (the "Private Placement") (i) an aggregate of 350,553 shares of Company common stock, par value $0.0001, at a purchase price of $11.12 per share (i.e., a price equal to the Company's consolidated closing bid price per share as reported by the Nasdaq Capital Market); (ii) an aggregate of 404,676 five-year warrants to purchase shares of Company common stock (the "Purchase Warrants") at a purchase price of $0.125 per share and exercise price of $11.12 per share; and (iii) an aggregate of 323,907 five-year pre-paid warrants to purchase shares of Company common stock (the "Pre-Funded Warrants") with exercise price of $0.01 per share (collectively, the "Securities"). The aggregate purchase price for the Securities was $7,550,585.

The Company will not issue any shares of our common stock under the Purchase Agreement, nor shall the Purchase Warrant and/or the Pre-Funded Warrant be exercisable, if such shares proposed to be issued and sold (including the shares issuable upon exercise of the Purchase Warrants and/or the Pre-Funded Warrants), when aggregated with all other shares of the Company common stock then owned beneficially (as calculated pursuant to Section 13(d) of the Exchange Act of 1934, as amended, and Rule 13d-3 promulgated thereunder) by Esousa and its affiliates would result in the beneficial ownership by Esousa and its affiliates of more than 9.99% of the then issued and outstanding shares of the Company common stock. Subject to certain exclusions, the Purchase Agreement contains certain restrictions on future equity fundings, including issuances without Esousa's consent of any securities convertible into the Company's common until 30 days after the resale registration statement for the Securities purchased by Esousa has been declared effective by the Securities and Exchange Commission (the "SEC") and any floating conversion rate or variable priced securities convertible into the Company's common stock until six months after such registration statement has been declared effective by the SEC.

Esousa represented to the Company in the Purchase Agreement that neither it nor any of its agents, representatives and affiliates engaged prior to the Closing Date in any direct or indirect short-selling or hedging of the Company's common stock.

As contemplated by the Purchase Agreement, on the Closing Date, the Company entered into a registration rights agreement with Esousa (the "Registration Rights Agreement"). The Registration Rights Agreement (i) required the

Company to file within 21 days of the Closing Date (the "Filing Deadline") a registration statement for the Securities purchased by Esousa in the Private Placement and (ii) granted certain piggyback rights thereunder. The Registration Rights Agreement requires the Company to and to use its commercially reasonable efforts to cause the Registration Statement to become effective as promptly thereafter as practicable but in any event not later than 90 days after the Closing Date (the "Effectiveness Deadline"). If the Company fails to meet the Filing Deadline or the Effectiveness Deadline, subject to certain terms provided for in the Registration Rights Agreement, the Company will be required to pay liquidated damages to Esousa. The Registration Rights Agreement provides for customary indemnification and contribution provisions. In the event Esousa no longer holds "Registrable Securities," as defined in the Registration Rights Agreements or when the Registrable Securities may be resold by Esousa pursuant to Rule 144 promulgated under the 1933 Act, the Company may not be obligated to cause the declaration of effectiveness of the Registration Statement by the SEC.

Pursuant to the Purchase Agreement and the Registration Rights Agreement, we are registering 1,079,136 shares of our common stock under the Securities Act, which includes the shares of common stock issuable upon exercise of the Purchase Warrants and the Pre-Funded Warrants. All 1,079,136 shares of common stock are being offered pursuant to this prospectus.

RISK FACTORS

You should carefully consider the following information about risks, as well as those risk factors set forth in our most recent Annual Report on Form 10-K on file with the Commission, which are incorporated by reference in this prospectus, together with the other information contained in this prospectus, before making an investment in our common stock. If any of the circumstances or events described below actually arises or occurs, our business, results of operations, cash flows and financial condition could be harmed. In any such case, the market price of our common stock could decline, and you may lose all or part of your investment.

Additional Risks Relating to the Private Placement

We may be obligated to pay liquidated damages if we fail to obtain and maintain effectiveness of a registration statement under the Registration Rights Agreement.

We have granted the selling stockholder resale registration rights pursuant to the terms of the Registration Rights Agreement. If a registration statement is not filed before the Filing Deadline or declared effective by the SEC before the Effectiveness Deadline, or if the registration statement thereafter becomes ineffective or the selling shareholder is unable to register the Shares thereunder for a certain period of time, the Company will be obligated to pay to the selling shareholder, as liquidated damages, an amount in cash or shares of our common stock equal to one percent (1%) of the selling shareholder’s total paid purchase price for the Securities pursuant to the Purchase Agreement.

The sale of a substantial amount of our common stock, including resale of the shares of common stock issuable upon the exercise of Warrants acquired in the Private Placement, in the public market after this offering could adversely affect the prevailing market price of our common stock and cause stockholders to experience dilution.

We have outstanding an aggregate of 3,862,352 shares of our common stock as of February 14, 2018. The Warrants are exercisable for an aggregate of 728,583 shares of common stock, subject to adjustment as provided in the Warrants, in addition to 350,553 shares of common stock being offered pursuant to this prospectus. The Warrants are exercisable at any time. Pursuant to the registration rights granted in the Private Placement, we agreed to register the resale by the selling stockholder named herein of the 350,553 shares of common stock being offered pursuant to this prospectus and the 728,583 shares of our common stock issuable upon exercise of the Warrants. Upon such registration, these registered shares will become generally available for immediate resale. Sales of substantial amounts of shares of our common stock in the public market, or the perception that such sales might occur, could adversely affect the market price of our common stock, and the market value of our other securities, and could result in dilution to shareholders who hold our common stock. In addition, we may issue additional shares of common stock or other equity or debt securities convertible into our common stock in connection with a future financing, acquisition, employee arrangements or otherwise. Any such issuance could result in substantial dilution to our stockholders and could cause our stock price to decline. A substantial number of shares of common stock are being offered by this prospectus, and we cannot predict if and when the selling stockholder may sell such shares in the public markets. We have also registered the offer and sale of all shares of common stock that we may issue under our equity compensation plan. Any such issuance could result in substantial dilution to our existing stockholders and could cause our stock price to decline.

Additional Risks Relating to Blockchain Technology

Risks of unfavorable regulatory action in one or more jurisdictions.

Blockchain technologies and cryptocurrencies have been the subject of scrutiny by various regulatory bodies around the world. The Company could be impacted by one or more regulatory inquiries or actions, including but not limited to restrictions on the use of blockchain technology, which could impede or limit the development of our anticipated blockchain technology solutions.

Competitive risks and alternative platforms.

Blockchain industry is highly competitive, and should intensify in the future. There are many platforms that enable the use of blockchain technologies in the payments ecosystem. Additional competitors are likely to enter the industry in the future. There is also competition from the traditional payment networks, all of which could potentially negatively impact the Company.

We may not be able to develop new products or enhance the capabilities related to blockchain technology that is being developed by the Company to keep pace with our industry's rapidly changing technology and customer requirements.

The industry for blockchain technology is characterized by rapid technological changes, new product introductions, enhancements, and evolving industry standards. Our business prospects depend on our ability to develop new products and applications for our technology in new markets that develop as a result of technological and scientific advances, while improving performance and cost-effectiveness. New technologies, techniques or products could emerge that might offer better combinations of price and performance than the blockchain technology solutions that are being developed by the Company. It is important that we anticipate changes in technology and market demand. If we do not successfully innovate and introduce new technology into our anticipated technology solutions or effectively manage the transitions of our technology to new product offerings, our business, financial condition and results of operations could be harmed.

Risks associated with unauthorized access.

Third parties that gains access to a user's login credentials or private keys may be able to transfer the user's value. To minimize this risk, the users should guard against unauthorized access to their electronic devices.

Risks that our anticipated blockchain technology solutions, as developed, will not meet the expectations of its target audience.

Our anticipated blockchain technology solutions are presently under development and may undergo significant changes before beta and/or final release. Any expectations regarding the form and functionality of our anticipated blockchain technology solutions may not be met upon release, for any number of reasons including change in the design and implementation plans and execution.

Risks of theft and hacking.

Hackers or other groups or organizations may attempt to interfere with the blockchain technology or the availability of our anticipated blockchain technology solutions in any number of ways, including without limitation denial of service attacks, Sybil attacks, spoofing, smurfing, malware attacks, or consensus based attacks. The Company expects to spend significant resources to consistently penetrate test and monitor its technology to prevent any such threats.

Risk of security weaknesses in the core infrastructure and software.

Some parts of the core software may be based on open-source software. There is a risk that the development team, or other third parties may intentionally or unintentionally introduce weaknesses or bugs into the core infrastructure elements of our anticipated blockchain technology solutions interfering with the use of or causing the loss to the Company.

Risk of weaknesses or exploitable breakthroughs in the field of cryptography.

Advances in cryptography, or technical advances such as the development of quantum computers, could present risks to cryptocurrencies and network, which could result tin the theft or loss.

We may require additional capital to fully utilize its business plan on a going forward basis as the Company develops and deploys its anticipated blockchain technology solutions and related ecosystem.

While the Company expects that funding of the project will be from current funds held by the Company, which is sufficiently funded to absorb such costs, the Company has yet to approximate its capital needs and might require additional capital to fully utilize its business plan on a go forward basis as the Company develops and deploys the ecosystem, cost of development of the ecosystem, value-added solutions as well as deployment and distribution costs. There is no assurance that the Company will be able to obtain any such additional capital in sufficient amounts or on acceptable terms when needed.

INFORMATION CONCERNING FORWARD-LOOKING STATEMENTS

This prospectus, including the documents incorporated by reference herein, contains statements that do not directly or exclusively relate to historical facts. Such statements are "forward-looking statements." You can typically identify forward-looking statements by the use of forward-looking words, such as "may," "will," "could," "project," "believe," "anticip "expect," "estimate," "continue," "potential," "plan," "forecast" and other similar words. These include, but are not limited to, statements relating to our future financial and operating results, plans, objectives, expectations and intentions and other statements that are not historical facts. These statements represent our intentions, plans, expectations, assumptions and beliefs about future events and are subject to risks, uncertainties and other factors. Many of these factors are outside of our control and could cause actual results to differ materially from the results expressed or implied by these forward-looking statements. In addition to the risk factors described under "Risk Factors" beginning on page 4 of this prospectus, these factors include:

- the impact of any new or changed laws, regulations, card network rules or other industry standards affecting our business, including the U.S. government decision to impose sanctions or other legal restrictions that may restrict our ability to do business in Russia;
- the impact of any significant chargeback liability and liability for merchant or customer fraud, which we may not be able to accurately anticipate and/or collect;
- our ability to secure or successfully migrate merchant portfolios to new bank sponsors if current sponsorships are terminated;
- whether blockchain technology solutions that are being developed by the Company will be adopted by the Company's merchants and consumers, whether such blockchain technology solutions will be successful, whether the Company will be successful in its endeavors to identify and invest into relevant projects and whether investment into blockchain ecosystem will positively impact the Company;

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- our and our bank sponsors' ability to adhere to the standards of the Visa® and MasterCard® payment card associations;
- our reliance on third-party processors and service providers;
- our dependence on independent sales groups ("ISGs") that do not serve us exclusively to introduce us to new merchant accounts;
- our ability to pass along increases in interchange costs and other costs to our merchants;
- our ability to protect against unauthorized disclosure of merchant and cardholder data, whether through breach of our computer systems or otherwise;
- the effect of the loss of key personnel on our relationships with ISGs, card associations, bank sponsors and our other service providers;
- the effects of increased competition, which could adversely impact our financial performance;
- the impact of any increase in attrition due to an increase in closed merchant accounts and/or a decrease in merchant charge volume that we cannot anticipate or offset with new accounts;
- the effect of adverse business conditions on our merchants;
- our ability to adopt technology to meet changing industry and customer needs or trends;

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- the impact of any decline in the use of credit cards as a payment mechanism for consumers or adverse developments with respect to the credit card industry in general;
- the impact of any adverse conditions in industries in which we obtain a substantial amount of our bankcard processing volume;
- the impact of seasonality on our operating results;
- the impact of any failure in our systems due to factors beyond our control;
- the impact of any material breaches in the security of third-party processing systems we use;
- the impact of any new and potential governmental regulations designed to protect or limit access to consumer information;
- the impact on our profitability if we are required to pay federal, state or local taxes on transaction processing;
- the impact on our growth and profitability if the markets for the services that we offer fail to expand or if such markets contract;
- our ability (or inability) to continue as a going concern;
- the willingness of the Company's majority stockholders, and/or other affiliates of the Company, to continue investing in the Company's business to fund working capital requirements;
- the Company's ability (or inability) to obtain additional financing in sufficient amounts or on acceptable terms when needed;
- the impact on our operating results or liquidity in the event of an unfavorable outcome on legal proceedings and claims which arise in the ordinary course;
- the impact on our operating results as a result of impairment of our goodwill and intangible assets;
- our material weaknesses in internal control over financial reporting and our ability to maintain effective controls over financial reporting in the future; and
- the other factors identified in the "Risk Factors" section of this prospectus.

Forward-looking statements are based on our current expectations about future events. Although we believe that the expectations reflected in the forward-looking statements are reasonable, these expectations may not be achieved. We are under no duty to update any of the forward-looking statements after the date of this prospectus to conform those statements to actual results. In evaluating these statements, you should consider various factors, including the risks outlined in the section entitled "Risk Factors" beginning on page 6 of this prospectus.

PRIVATE PLACEMENT OF COMMON STOCK AND WARRANTS

Overview

On December 29, 2017, we entered into, and consummated the transactions contemplated by, a Unit Purchase Agreement (the “Purchase Agreement”) with Esousa Holdings LLC (“Investor” or “Esousa”). Pursuant to the Purchase Agreement, on December 29, 2017 (the “Closing Date”), the Company sold to Investor (the “Private Placement”) (i) an aggregate of 350,553 shares of Company common stock, par value $0.0001, at a purchase price of $11.12 per share (the “Purchase Shares”); (ii) an aggregate of 404,676 five-year warrants to purchase shares of Company common stock (the “Purchase Warrants”) at a purchase price of $0.125 per share and exercise price of $11.12 per share; and (iii) an aggregate of 323,907 five-year pre-paid warrants to purchase shares of Company common stock (the “Pre-Funded Warrants”) with exercise price of $0.01 per share (collectively, the “Securities”). The aggregate purchase price for the Securities was $7,550,585.

As contemplated by the Purchase Agreement, on the Closing Date, the Company entered into a registration rights agreement with Esousa (the “Registration Rights Agreement”). The Registration Rights Agreement (i) required the Company to file within 21 days of the Closing Date (the “Filing Deadline”) a registration statement for the Securities purchased by Esousa in the Private Placement and (ii) granted certain piggyback rights thereunder. The Registration Rights Agreement requires the Company to use its commercially reasonable efforts to cause the Registration Statement to become effective as promptly thereafter as practicable but in any event not later than 90 days after the Closing Date (the “Effectiveness Deadline”). If the Company fails to meet the Filing Deadline or the Effectiveness Deadline, subject to certain terms provided for in the Registration Rights Agreement, the Company will be required to pay liquidated damages to Esousa described below under the caption “Effectiveness of Registration Statement Condition.” The Registration Rights Agreement provides for customary indemnification and contribution provisions. In the event Esousa no longer holds “Registrable Securities,” as defined in the Registration Rights Agreements or when the Registrable Securities may be resold by Esousa pursuant to Rule 144 promulgated under the 1933 Act, the Company may not be obligated to cause the declaration of effectiveness of the Registration Statement by the SEC

Pursuant to the Purchase Agreement and the Registration Rights Agreement, we are registering 1,079,136 shares of our common stock under the Securities Act, which includes the shares of common stock of the Company issuable upon exercise of the Purchase Warrants (the “Purchase Warrant Shares”) and the Pre-Funded Warrants (the “Pre-Funded Warrant Shares”). All 1,079,136 shares of common stock are being offered pursuant to this prospectus.

Purchase of Units

Pursuant to the Purchase Agreement, the Company sold to Investor certain units (the “Units”), with each Unit consisting of one Purchase Share and three-fifths (3/5) of a Purchase Warrant, where each whole Purchase Warrant entitles the holder to purchase one share of common stock of the Company.

Purchase Price

The total purchase price for the Units was $7,550,585, which consisted of (i) $0.125 per Purchase Warrant, and (ii) $11.12 per Purchase Share. The purchase price for the Purchase Shares was calculated using the consolidated closing bid price for the Company’s common stock, as reported by the Nasdaq Capital Market on the Closing Date.

Maximum Percentage

The Purchase Agreement provides that the Company shall not issue any shares of common stock thereunder if such issuance, when aggregated with all other shares of common stock of the Company beneficially owned by Investor and its affiliates, would result in a beneficial ownership (as calculated pursuant to Section 13(d) of the Exchange Act of 1934, as amended (the “Exchange Act”) and Rule 13d-3 promulgated thereunder) by Investor and its affiliates of more than 9.99% of the then issued and outstanding shares of common stock of the Company (the “Maximum Percentage”).

To the extent that an issuance would cause Investor’s beneficial ownership to exceed the Maximum Percentage, the Purchase Agreement provides that the Company shall, in lieu of issuing such shares, issue warrants to Investor to purchase, at a purchase price of $0.01 per share, the number of shares of common stock that would have caused Investor’s beneficial ownership to exceed the Maximum Percentage (the “Pre-Funded Warrants”).

Pursuant to these terms and the purchase price as described above, the Company sold to Investor an aggregate of (i) 350,553 Purchase Shares; (ii) 404,676 Purchase Warrants; and (iii) 323,907 Pre-Funded Warrants.

Terms of the Warrants

Purchase Warrants

On December 29, 2017 the Company issued to Investor an aggregate of 404,676 Purchase Warrants at a purchase price of $0.125 per share and an exercise price of $11.12 per share. The Purchase Warrants may be exercised at any time through 5:30 P.M., prevailing New York time on December 29, 2022 (the “Expiration Date”). Any portion of the Purchase Warrants not exercised prior to the Expiration Date will be terminated.

The Investor may exercise the Purchase Warrants by delivering to the Company (i) an exercise notice, appropriately completed and duly signed, and (ii) payment of the exercise price in immediately available funds (which may take the form of a “cashless exercise” if so indicated in the exercise notice). The Investor may not exercise or exchange the Purchase Warrants to the extent (but only to the extent) the Investor or any of its affiliates would beneficially own (as determined in accordance with Section 13(d) of the Exchange Act) a number of shares of the Company’s common stock which would exceed 9.99% of the total number of shares issued and outstanding.

Pre-funded Warrants

On December 29, 2017 the Company issued to Investor an aggregate of 323,907 Pre-funded Warrants at an exercise price of $0.01 per share. The Pre-funded Warrants may be exercised at any time through the Expiration Date. Any portion of the Pre-funded Warrants not exercised prior to the Expiration Date will be terminated.

The Investor may exercise the Pre-funded Warrants by delivering to the Company (i) an exercise notice, appropriately completed and duly signed, and (ii) payment of the exercise price in immediately available funds (which may take the form of a "cashless exercise" if so indicated in the exercise notice). The Investor may not exercise or exchange the Pre-funded Warrants to the extent (but only to the extent) the Investor or any of its affiliates would beneficially own (as determined in accordance with Section 13(d) of the Exchange Act) a number of shares of the Company's common stock which would exceed 9.99% of the total number of shares issued and outstanding.

Representations

The Investor represented to the Company in the Purchase Agreement that it is an institutional "accredited investor" as that term is defined in Rule 501(a) of Regulation D of the Securities Act. The Investor further represented that neither it nor any of its agents, representatives and affiliates engaged prior to the Closing Date in any direct or indirect short-selling or hedging of the Company's common stock.

Issuance of Additional Securities

Pursuant to the Purchase Agreement, the Company agreed that for the period commencing on the date thereof and ending on the date immediately following the 30th day after the satisfaction of the requirement that a registration statement registering the Securities be declared effective (as set forth on the Buyer Schedule thereto) (the “Restricted Period”), the Company shall not directly or indirectly issue, offer, sell, grant any option or right to purchase, or otherwise dispose of (or announce any issuance, offer, sale, grant of any option or right to purchase or other disposition of) any equity security or any equity-linked or related security (including, without limitation, any “equity security” (as that term is defined under Rule 405 promulgated under the Securities Act), any securities that are convertible into common stock of the Company, any preferred stock or any purchase rights for equity securities of the Company.

Notwithstanding the foregoing, the Company may issue during the Restricted Period the following: (i) issuances pursuant to acquisitions, joint ventures, license arrangements, leasing arrangements and similar transaction arrangements; (ii) equity awards or other compensatory issuances of the Company’s equity securities to the Company’s and its subsidiaries’ employees, independent contractors, consultants, officers and/or directors; or (iii) the exercise of preexisting rights under financing agreements, including issuances pursuant to prior equity lines and warrants or preferred shares currently outstanding, provided, however, that the Company shall not have modified the terms of any financing agreements or warrants to increase the number of securities that are existing or reduce the conversion or exercise price, as applicable, except as provided in such financing agreements or warrants.

The Company further agreed that, without prior consent of the Investor, until the earlier of (A) 6 months after the date on which the registration statement is declared effective or (B) the date on which the Investor has sold or disposed of all Securities, the Company will not issue any floating conversion rate or variable priced securities convertible into common stock of the Company.

Effectiveness of Registration Statement Condition

A registration statement registering the Purchase Shares, the Purchase Warrant Shares, and the Pre-Funded Warrant Shares must be filed and declared effective by the SEC covering the sale by Investor (in accordance with the plan of distribution called for by the Registration Rights Agreement) of the common stock contemplated by, and in the amount of, the Required Registration Amount (as defined in the Registration Rights Agreement). If the registration statement is not declared effective within 90 days of the Closing Date, the Company will incur penalties of 1% of the aggregate purchase price of the Securities per month for each month, or partial month, that the SEC fails to declare the registration statement effective. Such penalties shall be payable in cash or in common stock of the Company and shall lapse upon the six-month anniversary of the Closing Date so long as the Investor’s common stock are eligible for sale, without restriction, under Rule 144.

Events of Default

An "Event of Default" shall be deemed to have occurred under the Purchase Agreement when any of the following events occurs:

- while any registration statement is required to be maintained effective pursuant to the terms of the Registration Rights Agreement, the effectiveness of such registration statement lapses for any reason (including, without limitation, the issuance of a stop order) or is unavailable to the Investor for the sale of all of the securities required to be registered by the Registration Rights Agreement, and such lapse or unavailability continues for a period of 10 consecutive business days or for more than an aggregate of 30 business days in any 365-day period, which is not in connection with a post-effective amendment to any such registration statement or the filing of a new registration statement; provided, however, that in connection with any post-effective amendment to such registration statement or filing of a new registration statement that is required to be declared effective by the SEC, such lapse or unavailability may continue for a period of no more than 60 consecutive business days, which such period shall be extended for up to an additional 30 business days if the Company receives a comment letter from the SEC in connection therewith;

- the suspension of the common stock of the Company from trading for a period of 3 consecutive trading days;

- the delisting of the common stock of the Company from the Nasdaq Capital Market, and such stock is not promptly thereafter trading on the New York Stock Exchange, the NYSE MKT, the Nasdaq Global Select Market, the Nasdaq Global Market, the OTC Bulletin Board or either of the OTCQB marketplace or the OTCQX marketplace of the OTC Markets Group;

- the Company's breach of any representation or warranty (as of the dates made), covenant or other term or condition under the Purchase Agreement or the Registration Rights Agreement if such breach could reasonably be expected to have a Material Adverse Effect (as defined in the Purchase Agreement) and except only if such breach continues uncured for a period of at least 20 business days;

- if the Company pursuant to or within the meaning of any bankruptcy law; (A) commences a voluntary case, (B) consents to the entry of an order for relief against it in an involuntary case, (C) consents to the appointment of a custodian of it or for all or substantially all of its and its subsidiaries' property, or (D) makes a general assignment for the benefit of its creditors;

- unless dismissed within 90 days from each of the following events, a court of competent jurisdiction enters an order or decree under any bankruptcy law that (A) is for relief against the Company in an involuntary case, (B) appoints a custodian of the Company or for all or substantially all of its and its subsidiaries' property, or (C) orders the liquidation of the Company; or

- the Company ceases for more than 3 consecutive business days to be eligible, through its transfer agent, to issue and transfer shares of Common Stock electronically to third parties via the DTC FAST Program of the DWAC system of the Depository Trust Company.

Restrictive Legends

The Securities issued under the Purchase Agreement will bear a restrictive legend until such time as the selling shareholder resells the Securities pursuant to an effective registration statement or pursuant to Rule 144 under the Securities Act.

USE OF PROCEEDS

The selling stockholder will receive all of the proceeds from the sale of the shares offered for sale by it under this prospectus. We will not receive proceeds from the sale of the shares by the selling stockholder. We will, however, receive the exercise price of the Purchase Warrants (with the exercise price of $11.12 per share) and the Pre-Funded Warrants (with the exercise price of $0.01 per share) held by the selling stockholder if and when exercised by the selling stockholder exercised in cash, which, if exercised in cash at the current applicable exercise price with respect to all of the Warrants, would result in gross proceeds to the Company of $4,503,236.19.

SELLING Stockholder

The shares of common stock being offered by the selling stockholder are the Purchase Shares (as defined in the Unit Purchase Agreement) and those issuable to the selling stockholder upon exercise or exchange of the warrants. For additional information regarding the issuance of the common stock and the warrants, see “Private Placement of Common Stock and Warrants” above. We are registering the shares of common stock in order to permit the selling stockholder to offer the shares for resale from time to time. Except for the ownership of the Purchase Shares and the warrants issued pursuant to the Unit Purchase Agreement, the selling stockholder has not had any material relationship with us within the past three years.

The table below lists the selling stockholder and other information regarding the beneficial ownership (as determined under Section 13(d) of the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder) of the shares of common stock held by each of the selling stockholder. The second column lists the number of shares of common stock beneficially owned by the selling stockholder, based on its respective ownership of the shares of common stock and warrants, as of February 14, 2018, assuming exercise or exchange of the warrants held by such selling stockholder on that date but taking account of any limitations on conversion and exercise or exchange set forth therein.

The third column lists the shares of common stock being offered by this prospectus by the selling stockholder and does not take into account any limitations on exercise or exchange of the warrants set forth therein.

In accordance with the terms of a registration rights agreement with the holders of the warrants issued pursuant to the Unit Purchase Agreement, this prospectus generally covers the resale of the 100% of the Purchase Shares and the initial number of shares issued and issuable pursuant to the warrants (or the number of shares so issued and issuable as of the filing of the registration statement to which this prospectus relates, if more). This prospectus also or otherwise covers such other shares of common stock issued or issuable pursuant to the warrants as more fully set forth in this prospectus. Because the exercise price of the warrants may be adjusted for recapitalizations, stock splits, reverse stock splits and the like as set forth in the warrants, the number of shares that will actually be issued may be more or less than the number of shares being offered by this prospectus. The fourth column assumes the sale of all of the shares offered by the selling stockholder pursuant to this prospectus.

Under the terms of the warrants, the selling stockholder may not exercise or exchange the warrants to the extent (but only to the extent) such selling stockholder or any of its affiliates would beneficially own a number of shares of our common stock which would exceed 9.99%. The number of shares in the second column reflects these limitations. The selling stockholder may sell all, some or none of its shares in this offering. See “Plan of Distribution.”

Name of Selling Stockholder	**Number of Shares of Common Stock Owned Prior to Offering**	**Maximum Number of Shares of Common Stock to be Sold Pursuant to this Prospectus**	**Number of Shares of Common Stock Owned After Offering**
Esousa Holdings LLC(1)	-	1,079,136	-

(1) Rachel Glicksman has voting and investment control over the shares held by the selling stockholder.

Plan of Distribution

We are registering the Purchase Shares and the shares of common stock issuable to the selling stockholder upon exercise or exchange of the warrants to permit the resale of these shares of common stock by the holders of the common stock and warrants from time to time after the date of this prospectus. We will not receive any of the proceeds from the sale by the selling stockholder of the shares of common stock. We will bear all fees and expenses incident to our obligation to register the shares of common stock.

The selling stockholder may sell all or a portion of the shares of common stock held by them and offered hereby from time to time directly or through one or more underwriters, broker-dealers or agents. If the shares of common stock are sold through underwriters or broker-dealers, the selling stockholder will be responsible for underwriting discounts or commissions or agent's commissions. The shares of common stock may be sold in one or more transactions at fixed prices, at prevailing market prices at the time of the sale, at varying prices determined at the time of sale or at negotiated prices. These sales may be effected in transactions, which may involve crosses or block transactions, pursuant to one or more of the following methods:

- on any national securities exchange or quotation service on which the securities may be listed or quoted at the time of sale;
- in the over-the-counter market;
- in transactions otherwise than on these exchanges or systems or in the over-the-counter market;
- through the writing or settlement of options, whether such options are listed on an options exchange or otherwise;

- ordinary brokerage transactions and transactions in which the broker-dealer solicits purchasers;
- block trades in which the broker-dealer will attempt to sell the shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;
- purchases by a broker-dealer as principal and resale by the broker-dealer for its account;
- an exchange distribution in accordance with the rules of the applicable exchange;
- privately negotiated transactions;
- short sales made after the date the Registration Statement is declared effective by the SEC;
- broker-dealers may agree with a selling securityholder to sell a specified number of such shares at a stipulated price per share;
- a combination of any such methods of sale; and
- any other method permitted pursuant to applicable law.

The selling stockholder may also sell shares of common stock under Rule 144 promulgated under the Securities Act of 1933, as amended, if available, rather than under this prospectus. In addition, the selling stockholder may transfer the shares of common stock by other means not described in this prospectus. If the selling stockholder effects such transactions by selling shares of common stock to or through underwriters, broker-dealers or agents, such underwriters, broker-dealers or agents may receive commissions in the form of discounts, concessions or commissions from the selling stockholder or commissions from purchasers of the shares of common stock for whom they may act as agent or to whom they may sell as principal (which discounts, concessions or commissions as to particular underwriters, broker-dealers or agents may be in excess of those customary in the types of transactions involved). The selling stockholder may also loan or pledge shares of common stock to broker-dealers that in turn may sell such shares.

The selling stockholder may pledge or grant a security interest in some or all of warrants or shares of common stock owned by it and, if the selling stockholder defaults in the performance of its secured obligations, the pledgees or secured parties may offer and sell the shares of common stock from time to time pursuant to this prospectus or any amendment to this prospectus under Rule 424(b)(3) or other applicable provision of the Securities Act amending, if necessary, the list of selling stockholders to include the pledgee, transferee or other successors in interest as selling stockholders under this prospectus. The selling stockholder also may transfer and donate the shares of common stock in other circumstances in which case the transferees, donees, pledgees or other successors in interest will be the selling beneficial owners for purposes of this prospectus.

To the extent required by the Securities Act and the rules and regulations thereunder, the selling stockholder and any broker-dealer participating in the distribution of the shares of common stock may be deemed to be “underwriters” within the meaning of the Securities Act, and any commission paid, or any discounts or concessions allowed to, any such broker-dealer may be deemed to be underwriting commissions or discounts under the Securities Act. At the time a particular offering of the shares of common stock is made, which will set forth the aggregate amount of shares of common stock being offered and the terms of the offering, including the name or names of any broker-dealers or agents, any discounts, commissions and other terms constituting compensation from the selling stockholder and any discounts, commissions or concessions allowed or re-allowed or paid to broker-dealers.

Under the securities laws of some states, the shares of common stock may be sold in such states only through registered or licensed brokers or dealers. In addition, in some states the shares of common stock may not be sold unless such shares have been registered or qualified for sale in such state or an exemption from registration or qualification is available and is complied with.

There can be no assurance that the selling stockholder will sell any or all of the shares of common stock registered pursuant to the registration statement, of which this prospectus forms a part.

The selling stockholder and any other person participating in such distribution will be subject to applicable provisions of the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder, including, without limitation, to the extent applicable, Regulation M of the Exchange Act, which may limit the timing of purchases and sales of any of the shares of common stock by the selling stockholder and any other participating person. To the extent applicable, Regulation M may also restrict the ability of any person engaged in the distribution of the shares of common stock to engage in market-making activities with respect to the shares of common stock. All of the foregoing may affect the marketability of the shares of common stock and the ability of any person or entity to engage in market-making activities with respect to the shares of common stock.

We will pay all expenses of the registration of the shares of common stock pursuant to the registration rights agreement, estimated to be $43,301.67 in total, including, without limitation, Securities and Exchange Commission filing fees and expenses of compliance with state securities or "blue sky" laws; provided, however, a selling stockholder will pay all underwriting discounts and selling commissions, if any. We will indemnify the selling stockholder against liabilities, including some liabilities under the Securities Act in accordance with the registration rights agreements or the selling stockholder will be entitled to contribution. We may be indemnified by the selling stockholder against civil liabilities, including liabilities under the Securities Act that may arise from any written information furnished to us by the selling stockholder specifically for use in this prospectus, in accordance with the related registration rights agreements or we may be entitled to contribution.

Once sold under the registration statement, of which this prospectus forms a part, the shares of common stock will be freely tradable in the hands of persons other than our affiliates.

DESCRIPTION OF SECURITIES TO BE REGISTERED

The following information describes our common stock, as well as provisions of our certificate of incorporation and bylaws. This description is only a summary. You should also refer to our certificate of incorporation and bylaws, both as filed with the Commission as exhibits to our registration statement, of which this prospectus forms a part.

Common Stock

We are authorized to issue up to 100,000,000 shares of common stock, par value $0.0001 per share. As of February 14, 2018, approximately 3,862,352 shares of common stock were outstanding. All outstanding shares of our common stock are fully paid and non-assessable.

Each holder of our common stock is entitled to a pro rata share of cash distributions made to our stockholders, including dividend payments. The holders of our common stock are entitled to receive dividends when, as and if declared by our board of directors from funds legally available therefore. Cash dividends will be paid at the sole discretion of our board of directors.

The holders of our common stock are entitled to one vote for each share of record on all matters to be voted on by our stockholders. There is no cumulative voting with respect to the election of our directors or any other matter. Therefore, the holders of more than 50% of the shares of our common stock voting for the election of our directors can elect all of our directors.

In the event of our liquidation, dissolution or winding up, the holders of our common stock are entitled to share ratably in all assets remaining available for distribution to them after payment of our liabilities and after provision has been made for each class of stock, if any, having any preference in relation to our common stock.

Holders of our common stock have no conversion, preemptive or other subscription rights, and there are no redemption provisions applicable to our common stock.

Summary of Certain Provisions of Certificate of Incorporation and Bylaws

Our certificate of incorporation and bylaws, as applicable, among other things, (1) provide our board with the ability to alter the bylaws without stockholder approval, and (2) provide that vacancies on our board of directors may be filled by a majority of directors in office. These provisions, while designed to reduce vulnerability to an unsolicited acquisition proposal, and to discourage certain tactics used in proxy fights, may negatively impact a third-party’s decision to acquire us even if it would be beneficial to our stockholders.

Anti-Takeover Effects of Delaware Law and Certificate of Incorporation and Bylaws

We are subject to the Delaware anti-takeover laws regulating corporate takeovers, including Section 203 of the Delaware General Corporation Law ("DGCL"). These anti-takeover laws prevent Delaware corporations from engaging in a merger or sale of more than 10% of its assets with any stockholder, including all affiliates and associates of the stockholder, who owns 15% or more of the corporation's outstanding voting stock, for three years following the date that the stockholder acquired 15% or more of the corporation's assets unless:

- the board of directors approved the transaction in which the stockholder acquired 15% or more of the corporation's assets;
- after the transaction in which the stockholder acquired 15% or more of the corporation's assets, the stockholder owned at least 85% of the corporation's outstanding voting stock, excluding shares owned by directors, officers and employee stock plans in which employee participants do not have the right to determine confidentially whether shares held under the plan will be tendered in a tender or exchange offer; or
- on or after this date, the merger or sale is approved by the board of directors and the holders of at least two-thirds (2/3) of the outstanding voting stock that is not owned by the stockholder.

A Delaware corporation may opt out of the Delaware anti-takeover laws if its certificate of incorporation or bylaws so provides. We have not opted out of the provisions of the anti-takeover laws. As such, these laws could prohibit or delay mergers or other takeover or change of control of us and may discourage attempts by other companies to acquire us even if it would be beneficial to stockholders.

Transfer Agent and Registrar

We have appointed Continental Stock Transfer & Trust Company, 17 Battery Place, 8th Floor, New York, NY 10004 as our transfer agent and registrar.

Listing

Our common stock is listed on the NASDAQ Capital Market under the symbol “NETE”.

LEGAL MATTERS

The validity of the issuance of the common stock offered by this prospectus will be passed upon for us by Snell & Wilmer L.L.P., Los Angeles, California.

EXPERTS

Daszkal Bolton LLP, independent registered public accounting firm, has audited our financial statements as of, and for the years ended, December 31, 2016 and 2015, included in our Annual Reports on Form 10-K/A for the years ended December 31, 2016 and December 31, 2015, as set forth in their reports, which are incorporated by reference in this prospectus. Our financial statements are incorporated by reference in reliance on Daszkal Bolton LLP’s reports, given on their authority as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. We have also filed a registration statement on Form S-3, including exhibits, under the Securities Act with respect to the securities offered by this prospectus. This prospectus is part of the registration statement, but does not contain all of the information included in the registration statement or the exhibits. You may read and copy the registration statement and any other document that we file with the Commission at the Commission’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the Commission at 1-800-SEC-0330 for further information on the Public Reference Room. Our Commission filings are also available to the public on the internet at a website maintained by the Commission located at http://www.sec.gov.

INFORMATION INCORPORATED BY REFERENCE

The Commission allows us to "incorporate by reference" information into this document. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this document, except for any information superseded by information that is included directly in this document or incorporated by reference subsequent to the date of this document.

This prospectus incorporates by reference the documents listed below and any future filings (including the filings after the date of the first registration statement which this prospectus is a part of and prior to effectiveness of such registration statement) that we make with the Commission under Section 13(a), 13(c), 14 or 15(d) of the Exchange Act (other than current reports on Form 8-K furnished under Item 2.02 or Item 7.01 and exhibits filed on such form that are related to such items), until all the securities offered under this prospectus are sold or the offering is otherwise terminated.

The information incorporated by reference is an important part of this prospectus. Any statement in a document incorporated by reference into this prospectus will be deemed to be modified or superseded to the extent a statement contained in (1) this prospectus or (2) any other subsequently filed document that is incorporated by reference into this prospectus modifies or supersedes such statement

- Our Annual Report on Form 10-K for the fiscal year ended December 31, 2016, as filed with the Commission on March 31, 2017, and Annual Report on Form 10-K/A for the fiscal year ended December 31, 2016, as filed with the Commission on October 19, 2017;
- Our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2017, as filed with the Commission on May 15, 2017, June 30, 2017, as filed with the Commission on August 14, 2017, September 30, 2017, as filed with the Commission on November 14, 2017 and Quarterly Reports on Form 10-Q/A for the quarters ended March 31, 2017, as filed with the Commission on October 19, 2017, and June 30, 2017, as filed with the Commission on October 19, 2017;
- Our Current Reports on Form 8-K filed with the Commission on January 20, 2017, January 27, 2017, February 10, 2017, March 3, 2017, March 8, 2017, March 17, 2017, March 24, 2017, April 3, 2017 (only with respect to Item 9.01), April 28, 2017, May 15, 2017 (only with respect to Item 9.01), May 23, 2017, May 25, 2017, June 9, 2017, July 3, 2017, July 6, 2017, July 7, 2017, August 2, 2017, August 4, 2017, August 14, 2017 (only with respect to Item 9.01), August 21, 2017, September 1, 2017, September 29, 2017, October 4, 2017, October 20, 2017, November 14, 2017 (only with respect to Item 9.01), December 15, 2017, December 29, 2017, and January 2, 2018, and Current Report on Form 8-K/A, as filed with the Commission on March 22, 2017;
- Our Proxy Statement on Schedule 14A, as filed with the Commission on August 10, 2017; and
- The descriptions of our Common Stock contained in our Registration Statement on Form 8-A, filed with the Commission on September 28, 2010 and amended on October 2, 2012, and any other amendment or report filed for the purposes of updating such descriptions.

Documents incorporated by reference are available from the Commission as described above or from us without charge, excluding any exhibits to those documents unless the exhibit is specifically incorporated by reference as an exhibit in this document. You can obtain documents incorporated by reference in this document by requesting them in writing or by telephone at the following address:

Net Element, Inc.

3363 NE 163rd St., Suite 705

North Miami Beach, Florida 33160

(305) 507-8808

Attention: Chief Financial Officer

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NET ELEMENT, INC.

1,079,136 Shares

Common Stock

February 14, 2018

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PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

Item 14. Other Expenses of Issuance and Distribution.

The following table sets forth the expenses to be borne by the Registrant in connection with the issuance and distribution of the securities registered hereby. Other than the Commission registration fee, all of the amounts below are estimates.

Commission registration fee	$ 897.47
Accounting fees and expenses	$ 5,000.00
Legal fees and expenses	$ 30,000.00
Financial printing and miscellaneous expenses	$ 5,000.00
Transfer Agent fees	$ 1,500.00
Total	$ 42,397.47

Item 15. Indemnification of Directors and Officers.

Section 102 of the Delaware General Corporation Law (the “DGCL”) allows a corporation to eliminate the personal liability of directors of a corporation to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, except where the director breached the duty of loyalty, failed to act in good faith, engaged in intentional misconduct or knowingly violated a law, authorized the payment of a dividend or approved a stock repurchase in violation of the DGCL or obtained an improper personal benefit.

Under Section 145 of the DGCL, we can indemnify our directors and officers against liabilities they may incur in such capacities, including liabilities under the Securities Act of 1933, as amended (the “Securities Act”). Our certificate of incorporation provides that, pursuant to the DGCL, our directors shall not be liable for monetary damages for breach of the directors’ fiduciary duty of care to us and our stockholders. This provision in the certificate of incorporation does not eliminate the duty of care, and in appropriate circumstances equitable remedies such as injunctive or other forms of non-monetary relief will remain available under the DGCL. In addition, each director will continue to be subject to liability for breach of the director’s duty of loyalty to us or our stockholders, for acts or omissions not in good faith or involving intentional misconduct or knowing violations of the law, for actions leading to improper personal benefit to the director, and for payment of dividends or approval of stock repurchases or redemptions that are unlawful under the DGCL. The provision also does not affect a director's responsibilities under any other law, such as the federal securities laws or state or federal environmental laws.

Section 174 of the DGCL provides, among other things, that a director who willfully or negligently approves of an unlawful payment of dividends or an unlawful stock purchase or redemption may be held liable for such actions. A director who was either absent when the unlawful actions were approved or dissented at the time, may avoid liability by causing his or her dissent to such actions to be entered in the books containing minutes of the meetings of our board of directors at the time such action occurred or immediately after such absent director receives notice of the unlawful acts.

In addition, our directors and officers are covered under directors' and officers' liability insurance policies maintained by us, subject to the limits of the policies, insuring such persons against various liabilities.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Registrant pursuant to the foregoing provisions, or otherwise, the Registrant has been advised that, in the opinion of the Commission, such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable.

Item 16. Exhibits.

Exhibit No.	Description of Exhibit
2.1	Agreement and Plan of Merger, dated as of June 12, 2012, by and between Cazador Acquisition Corporation Ltd. and Net Element, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the Commission on June 12, 2012)
2.2	Contribution Agreement, dated April 16, 2013, among Net Element International, Inc., Unified Payments, LLC, TOT Group, Inc., Oleg Firer, and Georgia Notes 18 LLC (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the Commission on April 17, 2013.
2.3	Term Sheet, dated May 20, 2013, among TOT Group, Inc., Net Element International, Inc. and Aptito.com, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the Commission on May 22, 2013)
2.4	Asset Purchase Agreement, dated June 18, 2013, between Aptito, LLC and Aptito.com, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the Commission on June 24, 2013)
2.5	Contribution Agreement, dated September 25, 2013, among T1T Lab, LLC, Net Element International, Inc. and T1T Group, LLC (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed with the Commission on September 25, 2013)
2.6	Assignment of Membership Interest, dated February 11, 2014, among T1T Group, LLC, Net Element, Inc., and T1T LAB, LLC (incorporated by reference to Exhibit 2.7 to the Company's Annual Report on Form 10-K filed with the Commission on April 15, 2014)
2.7	Binding Offer Letter, dated March 16, 2015, among TOT Group Europe Ltd., Maglenta Enterprises Inc. and Champfremont Holding Ltd. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K/A filed with the Commission on March 20, 2015)
4.1	Specimen Common Stock Certificate of Net Element International, Inc. (incorporated by reference to Exhibit 4.2 to the Registration Statement on Form S-4 filed by the Company with the Commission on August 31, 2012)
4.2	

	Warrant Certificate of Cazador Acquisition Corporation Ltd. (incorporated by reference to Exhibit 4.3 to the Registration Statement on Form F-1 filed by the Company with the Commission on September 3, 2010)
4.3	Registration Rights Agreement by and between Cazador Acquisition Corporation Ltd., Cazador Sub Holdings Ltd. and Others (incorporated by reference to Exhibit 10.5 to the Registration Statement, as amended, on Form F-1/A filed by the Company with the Commission on October 6, 2010)
4.4	Warrant Agreement by and between Cazador Acquisition Corporation Ltd. and Continental Stock Transfer & Trust Company (incorporated by reference to Exhibit 4.4 to the Registration Statement, as amended, on Form F-1/A filed by the Company with the Commission on October 6, 2010)

4.5	Secured Convertible Senior Promissory Note dated April 21, 2014 between the Company and Cayman Invest, S.A. (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the Commission on April 22, 2014)
4.6	Form of Amended and Restated Restricted Options to Purchase Shares of Restricted Common Stock (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the Commission on October 7, 2015)
4.7	Form of Option to Kenges Rakishev to Purchase Shares of Restricted Common Stock (incorporated by reference to Exhibit 4.1 to Net Element's Current Report on Form 8-K filed with the Commission on January 22, 2016)
4.8	Registration Rights Agreement, dated as of July 6, 2016, between the Company and Esousa Holdings LLC (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the Commission on July 12, 2016)
4.9	Registration Rights Agreement, dated as of July 5, 2017, between the Company and Cobblestone Capital Partners LLC (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the Commission on July 7, 2017)
4.10	Registration Rights Agreement, dated as of December 29, 2017, between the Company and Esousa Holdings LLC (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the Commission on January 2, 2018)
4.11	Form of Warrant to Purchase Common Stock issued to Esousa Holdings LLC (incorporated by reference to Exhibit A-1 to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on January 2, 2018)
4.12	Form of Pre-Funded Warrant to Purchase Common Stock issued to Esousa Holdings LLC (incorporated by reference to Exhibit A-2 to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on January 2, 2018)
5.1*	Opinion of Snell & Wilmer L.L.P.
10.1	Unit Purchase Agreement, dated as of December 29, 2017, between the Company and Esousa Holdings, LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on January 2, 2018)
23.1*	Consent of Independent Registered Public Accounting Firm (Daszkal Bolton LLP)
23.2*	Consent of Snell & Wilmer L.L.P. (included in Exhibit 5.1)
24.1	Power of Attorney (included on signature page) (previously filed)

* Filed herewith.

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Item 17. Undertakings.

(a) The undersigned Registrant hereby undertakes:

(1) To file, during any period in which offers or sales are being made, a post-effective amendment to this registration statement:

(i) To include any prospectus required by Section 10(a)(3) of the Securities Act of 1933;

(ii) To reflect in the prospectus any facts or events arising after the effective date of the registration statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represent a fundamental change in the information set forth in the registration statement. Notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation from the low or high end of the estimated maximum offering range may be reflected in the form of prospectus filed with the Commission pursuant to Rule 424(b) if, in the aggregate, the changes in volume and price represent no more than 20% change in the maximum aggregate offering price set forth in the "Calculation of Registration Fee" table in the effective registration statement; and

(iii) To include any material information with respect to the plan of distribution not previously disclosed in the registration statement or any material change to such information in the registration statement;

provided, however, that paragraphs (a)(1)(i), (ii), and (iii) of this section do not apply if the information required to be included in a post-effective amendment by those paragraphs is contained in reports filed with or furnished to the Commission by the Registrant pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 that are incorporated by reference in the registration statement.

(2) That, for the purpose of determining any liability under the Securities Act of 1933, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(3) To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

(4) That, for the purpose of determining liability under the Securities Act of 1933 to any purchaser, if the Registrant is subject to Rule 430C, each prospectus filed pursuant to Rule 424(b) as part of a registration statement relating to an offering, other than registration statements relying on Rule 430B or other than prospectuses filed in reliance on Rule 430A, shall be deemed to be part of and included in the registration statement as of the date it is first used after effectiveness. *Provided*, *however*, that no statement made in a registration statement or prospectus that is part of the registration statement or made in a document incorporated or deemed incorporated by reference into the registration statement or prospectus that is part of the registration statement will, as to a purchaser with a time of contract of sale prior to such first use, supersede or modify any statement that was made in the registration statement or prospectus that was part of the registration statement or made in any such document immediately prior to such date of first use.

(5) That, for the purpose of determining liability of the Registrant under the Securities Act of 1933 to any purchaser in the initial distribution of the securities, the undersigned Registrant undertakes that in a primary offering of securities of the undersigned Registrant pursuant to this registration statement, regardless of the underwriting method used to sell the securities to the purchaser, if the securities are offered or sold to such purchaser by means of any of the following communications, the undersigned Registrant will be a seller to the purchaser and will be considered to offer or sell such securities to such purchaser:

(i) Any preliminary prospectus or prospectus of the undersigned Registrant relating to the offering required to be filed pursuant to Rule 424;

(ii) Any free writing prospectus relating to the offering prepared by or on behalf of the undersigned Registrant or used or referred to by the undersigned Registrant;

(iii) The portion of any other free writing prospectus relating to the offering containing material information about the undersigned Registrant or its securities provided by or on behalf of the undersigned Registrant; and

(iv) Any other communication that is an offer in the offering made by the undersigned Registrant to the purchaser.

(b) The undersigned Registrant hereby undertakes that, for purposes of determining any liability under the Securities Act of 1933, each filing of the Registrant’s annual report pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 (and, where applicable, each filing of an employee benefit plan’s annual report pursuant to Section 15(d) of the Securities Exchange Act of 1934) that is incorporated by reference in the registration statement shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

(e) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the Registrant pursuant to the provisions set forth or described in Item 15 of this registration statement, or otherwise, the Registrant has been advised that in the opinion of the Commission such indemnification is against public policy as expressed in the Securities Act of 1933 and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the Registrant of expenses incurred or paid by a director, officer or controlling person of the Registrant in the successful defense of any action, suit N="bottom">

United States	$68,070	$76,417
International	1,119	544
Total net revenue	$69,189	$76,961

	September 30, 2014	June 30, 2014
Property and equipment, net:		
United States	$ 9,848	$ 10,878
International	240	248
Total property and equipment, net:	$ 10,088	$ 11,126

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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, 2014, 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, targe 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, 2014, 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 months ended September 30, 2014 and 2013. 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 financial services and education. Our financial services client vertical represented 44% and 41% of net revenue in the three months ended September 30, 2014 and 2013. Our education client vertical represented 36% and 43% of net revenue in the three months ended September 30, 2014 and 2013. Other DMS client verticals, consisting primarily of business-to-business technology, home services and medical, represented 20% and 16% of net revenue in the three months ended September 30, 2014 and 2013.

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 months ended September 30, 2014 or 2013.

Trends Affecting our Business

Client Verticals

To date, we have generated the majority of our revenue from clients in our financial services and education client verticals. We expect that a majority of our revenue for the remainder of fiscal year 2015 will continue to be generated from clients in these two client verticals.

Our financial services client vertical continued to be negatively affected due to the limited 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. To offset this impact, we have broadened our product set with the launch of enhanced click, lead, call, and policy products, where we expect better monetization to provide greater access to high quality media sources.

Our education client vertical has been significantly affected by regulations and enforcement activity affecting for-profit educational institutions over the past several years. For example, a publicly traded for-profit education client signed an agreement with the Department of Education in July 2014 which limits its enrollment and disbursement activities in certain respects. Similar regulatory and enforcement activities have affected and are expected to continue to affect our clients businesses and marketing practices, which may result in a decrease in these clients spending with us, and fluctuations in the volume and mix of our business with these clients. To offset the impact these activities have had on the for-profit education clients, we have broadened our product set from our traditional lead business with the addition of clicks, calls and higher quality leads to our product mix. We are also broadening our markets in education to include not-for-profit schools as well as expanding internationally in Brazil and India.

Acquisitions

We did not complete any acquisitions during the three months ended September 30, 2014 or 2013.

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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 provide a sound financial outcome for us. 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 recently 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 have thus far had a relatively small negative effect on traffic conversion rates. However, 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 governmental 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

We operate in one reportable segment, DMS. The remainder of our business, which has historically been immaterial, is classified as All Other . See Note 11, Segment Information, to our condensed consolidated financial statements for further discussion and financial information regarding our reporting segment.

Net Revenue

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). All other revenue generated less than 1% of net revenue in the three months ended September 30, 2014 and 2013. We expect all other revenue to continue to represent an immaterial portion of our business.

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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 increase in absolute dollars in the future as we believe that continuous investment in technology is critical to attaining our strategic objectives.

Sales and Marketing. Sales and marketing expenses consist primarily of personnel costs, advertising, professional services fees, and travel costs. We expect sales and marketing expenses to continue to increase in absolute dollars as we increase advertising spend and 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 to increase in absolute dollars in future periods as we continue to invest in corporate infrastructure.

Interest and Other Income (Expense), Net

Interest and other income (expense), net, consists primarily of interest income, interest expense, and other income and expense, which includes foreign currency exchange gains and losses, sale of non-strategic websites and domain names, and other non-operating items. 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.

Benefit from Income Taxes

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.

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Critical Accounting Policies, Estimates and Judgments

In presenting our condensed 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, 2014. 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, 2014, filed with the SEC.

Recently Issued Accounting Standards

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

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Results of Operations

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

	Three Months Ended September 30, 2014		2013	
	(In thousands)			
Net revenue	$ 69,189	100.0%	$ 76,961	100.0%
Cost of revenue [1]	63,409	91.6	63,592	82.6
Gross profit	5,780	8.4	13,369	17.4
Operating expenses: [1]				
Product development	4,956	7.2	5,159	6.7
Sales and marketing	3,667	5.3	4,156	5.4
General and administrative	4,615	6.7	4,134	5.4
Operating loss	(7,458)	(10.8)	(80)	(0.1)
Interest income	26		27	
Interest expense	(1,180)	(1.7)	(1,026)	(1.3)
Other (expense) income, net	2,325	3.4	(19)	
Loss before income taxes	(6,287)	(9.1)	(1,098)	(1.4)
Benefit from taxes			159	0.2
Net loss	$ (6,287)	(9.1)%	$ (939)	(1.2)%

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

Cost of revenue	$ 644	0.9%	$ 874	1.1%
Product development	595	0.9	732	1.0
Sales and marketing	464	0.7	770	1.0
General and administrative	572	0.8	659	0.9

Net Revenue

	Three Months Ended September 30, 2014	2013	Three Months % Change
	(in thousands)		
Net revenue	$ 69,189	$ 76,961	(10%)

Cost of revenue	63,409	63,592	(0%)
Gross profit	$ 5,780	$ 13,369	(57%)

Net revenue decreased $7.8 million, or 10%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013. Our financial services client vertical revenue decreased $1.2 million, or 4%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013, primarily due to lower client budgets and the limited availability of high quality media in our auto insurance client vertical as well as due to a reduction in mortgage inquiry traffic caused by an increase in interest rates, offset by increased demand in our other financial services client verticals. Our education client vertical revenue decreased $8.0 million, or 24%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013, as a result of our education clients lower budgets, largely due to uncertainty surrounding regulations and enforcement activity affecting for-profit educational institutions and their operational adjustment to this activity.

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Our other client verticals revenue increased $1.4 million or 12%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013, primarily due to increased client demand in our business-to-business technology and home services client verticals and partially offset by decreased client demand in our medical client vertical.

Cost of Revenue and Gross Margin

Cost of revenue decreased $0.2 million for the three months ended September 30, 2014, compared to the three months ended September 30, 2013, driven by decreased amortization of intangible assets of $1.3 million and decreased media costs of $1.3 million, offset by increased personnel costs of $1.6 million and increased marketing and media services costs of $0.8 million. The decreased amortization of intangible assets was attributable to 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. The increased marketing and media services costs were attributable to an increase in call center services. Gross margin, which is the difference between net revenue and cost of revenue as a percentage of net revenue, was 8% for the three months ended September 30, 2014 and 17% for the three months ended September 30, 2013. The decrease in gross margin is attributable to lower revenue levels and a lower mix of traffic from owned and operated websites which have higher margins than traffic generated from third party publishers.

Operating Expenses

	Three Months Ended September 30,		Three Months
	2014	2013	% Change
	(in thousands)		
Product development	$ 4,956	$ 5,159	(4%)
Sales and marketing	3,667	4,156	(12%)
General and administrative	4,615	4,134	12%
Operating expenses	$ 13,238	$ 13,449	(2%)

Product Development Expenses

Product development expenses decreased $0.2 million, or 4%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013. This was primarily due to decreased stock-based compensation of $0.1 million.

Sales and Marketing Expenses

Sales and marketing expenses decreased $0.5 million, or 12%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013. This was primarily due to decreased stock-based compensation of $0.3 million and personnel costs of $0.2 million due to a decrease in average headcount.

General and Administrative Expenses

General and administrative expenses increased $0.5 million, or 12%, for the three months ended September 30, 2014, compared to the three months ended September 30, 2013. This was primarily due to an increase in professional services in legal and audit fees of $0.5 million.

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Interest and Other Income (Expense), Net

	Three Months Ended September 30, 2014	2013	Three Months % Change
	(in thousands)		
Interest income	$ 26	$ 27	(4%)
Interest expense	(1,180)	(1,026)	15%
Other income (expense), net	2,325	(19)	12337%
Interest and other income (expense), net	$ 1,171	$ (1,018)	215%

Interest and other income (expense), net increased $2.2 million, or 215% for the three months ended September 30, 2014, compared to the three months ended September 30, 2013 due to the sale of domain names for a gain of $2.5 million, partially offset by the accelerated amortization of $0.3 million of unamortized deferred upfront costs incurred in connection with the Second Amendment to Credit Agreement in the three months ended September 30, 2014.

Benefit from Taxes

	Three Months Ended September 30, 2014	2013	Three Months % Change
	(in thousands)		
Benefit from taxes	$	$ 159	(100%)

We recorded a valuation allowance against the majority of our deferred tax assets at the end of fiscal year 2014 and in order to maintain a full valuation allowance against our deferred tax assets for the three months ended September 30, 2014, we did not record an income tax expense. Additionally, we had immaterial foreign expenses that were offset by other immaterial benefits that resulted in a zero quarterly provision. We estimate our annual effective tax rate for the three months ended September 30, 2014 to be 36%, which was the result of immaterial profit before taxes from foreign subsidiaries and related foreign tax provision that were offset by other immaterial benefits resulting in a zero quarterly provision. Our annual effective rate differs from the annual statutory rate of 35% due to the small impact of the foreign rate differential.

We recognized a tax benefit of $0.2 million for the three months ended September 30, 2013. We estimate our annual effective tax rate to be 53%. This differs from the annual statutory rate of 35% due to various permanent differences most significantly stock based compensation. The current quarter tax benefit was determined based on applying the estimated annual effective rate to the pre-tax book loss and applying the impact of the discrete reporting of stock based compensation incurred during the three months ended September 30, 2013.

Liquidity and Capital Resources

As of September 30, 2014, our principal sources of liquidity consisted of cash and cash equivalents of $76.4 million, short-term marketable securities of $39.5 million, cash we expect to generate from operations, and our $50.0 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 $73.8 million term loan balance at September 30, 2014, 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 to fund anticipated liquidity requirements, 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.

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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:

	Three Months Ended September 30, 2014	2013
	(in thousands)	
Cash flows (used in) provided by operating activities	$ (3,501)	$ 3,882
Net cash used in investing activities	(711)	(2,702)
Cash flows used in financing activities	(3,560)	(2,973)

Operating Activities

Cash flows from operating activities are primarily the result of our net loss adjusted for depreciation and amortization, stock-based compensation expense, and changes in working capital components.

Cash flows used in operating activities were $3.5 million for the three months ended September 30, 2014, compared to cash flows provided by operating activities of $3.9 million for the three months ended September 30, 2013.

Cash flows used in operating activities for the three months ended September 30, 2014 consisted of a net loss of $6.3 million, which includes a one-time restructuring charge of $0.4 million, and changes in working capital of $3.0 million, partially offset by non-cash adjustments of $5.8 million. The changes in working capital accounts was primarily due a net decrease in accounts payable and accrued liabilities of $2.3 million, an increase in prepaid expenses and other current assets of $1.3 million, and a net decrease in deferred revenue and other noncurrent liabilities of $0.1 million, offset by a decrease in accounts receivable of $0.7 million. The net decrease in accounts payable and accrued liabilities as well as the increase in accounts receivable, are primarily due to timing of payments. The non-cash adjustments primarily consisted of depreciation and amortization of $5.4 million, gain on sale of domain names of $2.5 million, and stock-based compensation expense net of tax benefits of $2.2 million.

Cash flow provided by operating activities for the three months ended September 30, 2013 consisted of non-cash charges of $9.6 million, partially offset by contributions to working capital of $4.8 million and net loss of $0.9 million. The non-cash charges primarily consisted of depreciation and amortization of $6.7 million and stock-based compensation expense net of tax benefits of $2.9 million. The contribution to working capital accounts was primarily due to a net decrease in accounts payable and accrued liabilities of $3.1 million, an increase in accounts receivable of $1.7 million and a net decrease in deferred revenue and other noncurrent liabilities of $0.6 million offset by a decrease in prepaid expenses and other assets of $0.6 million. The increase 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 $0.7 million for the three months ended September 30, 2014, compared to cash flows used in investing activities of $2.7 million for the three months ended September 30, 2013.

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Cash used in investing activities in the three months ended September 30, 2014 was primarily due to capital expenditures and internal software development costs of $2.6 million and net investments in marketable securities of $0.8 million, partially offset by proceeds from the sale of domain names of $2.7 million.

Cash used in investing activities in the three months ended September 30, 2013 was primarily due to capital expenditures and internal software development costs of $1.8 million. Net investments in marketable securities totaled $0.8 million in the three months ended September 30, 2013.

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 $3.6 million for the three months ended September 30, 2014, compared to cash flows used in financing activities of $3.0 million for the three months ended September 30, 2013.

Cash used in financing activities in the three months ended September 30, 2014 was primarily due to principal payments on our term loan and acquisition-related notes payable of $4.5 million and withholding taxes related to restricted stock net share settlements of $0.4 million, partially offset by proceeds from exercises of stock options of $1.3 million and excess tax benefits from exercises of stock options of $0.1 million.

Cash used in financing activities in the three months ended September 30, 2013 was primarily due to principal payments on acquisition-related notes payable and our term loan of $3.0 million and withholding taxes related to restricted stock net share settlements of $1.0 million, partially offset by exercises of stock options of $1.0 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, 2014.

Credit Facility

In November 2011, we entered into the Second Amended and Restated Revolving Credit and Term Loan Agreement (Second Loan Agreement) with Comerica Bank (the Bank), the administrative agent and lead arranger. The Second Loan Agreement consists of a $100.0 million five-year term loan, with annual principal amortization of 5%, 10%, 15%, 20% and 50%, and a $200.0 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) with the Bank to, among other things: (1) amend the definition of EBITDA, effective as of December 31, 2012, to exclude extraordinary or non-recurring non-cash expenses or losses including, without limitation, goodwill impairments, and any extraordinary or non-recurring cash expenses in an aggregate amount not to exceed $5.0 million for the life of the Second Loan

Agreement; and (2) reduce the $200.0 million five-year revolving credit line portion of the facility to $100.0 million, effective as of February 15, 2013. On July 17, 2014, we entered into the Second Amendment to Credit Agreement (Second Amendment) with the Bank to, among other things, amend the financial covenants and reduce the revolving loan facility from $100.0 million to $50.0 million, each effective as of June 30, 2014.

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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 Eurodollar rate plus an applicable margin, at our option. Base rate is defined as an 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 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 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 EBITDA ratio. Pursuant to the Second Amendment, for the period beginning on the effective date of the Second Amendment until the delivery of financial statements for the fiscal quarter ending December 31, 2015, (1) the applicable margin for Base rate borrowings is set at (a) 1.375% for revolving loans or (b) 1.75% for term loans, and (2) the applicable margin for Eurodollar rate borrowings is set at (a) 2.375% for revolving loans or (b) 2.75% for term loans. Thereafter, the applicable margin varies depending on our funded debt to EBITDA ratio, as described above.

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 or 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 loan facility 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, as amended, 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 covenants as follows:

1. A minimum fixed charge coverage ratio as of the end of each fiscal quarter of not less than:

(a) 1.00:1:00 for the period between September 30, 2015 and June 30, 2016; and

(b) 1.15:1:00 for the period beginning July 1, 2016 and thereafter.

The fixed charge coverage ratio is not tested until the fiscal quarter ending September 30, 2015.

2. Minimum EBITDA as of the end of each fiscal quarter of not less than:

(a) $1 for the period between April 1, 2014 and June 30, 2015;

(b) $3,400,000 for the period between July 1, 2015 and September 30, 2015;

(c) $3,200,000 for the period between October 1, 2015 and December 31, 2015.

EBITDA is not tested after the fiscal quarter ending December 31, 2015.

3. Minimum liquidity as of the end of each month of not less than $20,000,000.

We were in compliance with the covenants of our Second Loan Agreement, as amended, as of September 30, 2014 and June 30, 2014.

Upfront arrangement fees incurred in connection with the Second Amendment totaled $0.3 million and will be deferred and amortized over the remaining term of the arrangement. In connection with the reduction of the revolving credit line capacity, we accelerated amortization of approximately $0.3 million of unamortized deferred upfront costs.

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 outstanding as of January 1, 2014 and scheduled to be outstanding 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 September 30, 2014, we had approximately $73.8 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 September 30, 2014, 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 condensed consolidated 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.

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 September 30, 2014, our credit facility consisted of a $73.8 million outstanding term loan and a $50 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 Base 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 September 30, 2014 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 condensed consolidated financial condition or results of operations.

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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 September 30, 2014. 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 September 30, 2014, 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.

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, alleging that we had infringed a patent held by IPC. 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 January 2014, IPC filed its appeal in the United States Court of Appeals for the Federal Circuit. The United States Court of Appeals for Federal Circuit heard oral arguments on the appeal on August 6, 2014, and we are still awaiting a decision. 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 dependence on unimpeded access to the Internet by us and Internet visitors;
- our ability to accurately forecast our results of operations 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 audits, investigations or allegations of noncompliance with laws.

If we are unable to address these risks, our business, results of operations and prospects could suffer.

Negative changes in the economic condition, market dynamics or regulatory environment have caused, and may continue to cause, our revenue to decline and our business and growth to suffer.

Adverse macroeconomic conditions could cause decreases or delays in spending by our advertisers and could harm our ability to generate revenue and our results of operations. Moreover, 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 diverse financial services client verticals. Changes in the market conditions or the regulatory environment in these two highly-regulated client verticals in particular 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 us, our third-party publishers or clients could result in 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 not had a material impact 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 customers 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 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 to 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.

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 school s 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.

For example, one of our publicly traded for-profit education clients signed an agreement with the Department of Education in July 2014 which limits its enrollment and disbursement activities in certain respects. Similar regulatory and enforcement activities, including the Department of Education s new gainful employment rules, issued October 31, 2014, either have affected and or in the future may affect our for-profit education clients businesses and marketing practices, which may result in a decrease in these clients spending with us, and fluctuations in the volume and mix of our business with these clients. 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.

We depend on third-party 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, third-party publishers can change the media inventory they make available to us at any time and, therefore, impact our results of operations. In addition, third-party publishers may place significant restrictions on our offerings. These restrictions may prohibit

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advertisements from specific clients or specific industries, or restrict the use of certain creative content or formats. If a third-party 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 third-party 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 results of operations 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 results of operations to fall short of analysts and investors expectations.

Historically, quarterly and annual results of operations have fluctuated due to changes in our business, our industry and the general economic climate. We expect our future results of operations to vary significantly from quarter to quarter due to a variety of factors, many of which are beyond our control. Our fluctuating results of operations 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 results of operations may not be useful to you in predicting our future results of operations. Factors that may increase the volatility of our results of operations include the following:

- changes in client volume;
- loss of or reduced demand by existing clients;
- 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.

As a result of changes in our business model and increased expenditures for certain businesses, products, services and technologies, we anticipate downward pressure on our Adjusted EBITDA margin.

We have invested and expect to continue to invest in new businesses, products, services and technologies, including more expensive forms of media. We may have insufficient revenue to fully offset liabilities and expenses in connection with these investments and may experience inadequate, unpredictable return of capital on our investments. As a result of these investments, we expect downward pressure on our Adjusted EBITDA margin.

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 and our third-party publishers websites, as well as 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.

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In addition, we may fail to optimally manage our paid listings, or our proprietary bid management technologies may fail. To attract and retain visitors, we use search engine optimization (SEO) which involves developing content to optimize ranking in search engine results. Our ability to successfully manage SEO efforts across our owned and operated websites and our third-party publishers websites depends on our timely and effective modification of SEO practices implemented in response to periodic changes in search engine algorithms and methodologies and changes in search query trends. If we fail to successfully manage our SEO strategy, our websites may receive less favorable placement in organic or paid listings, which would reduce the number of visitors to our sites, decrease conversion rates and repeat business 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. Even if we succeed in driving traffic to our owned and operated websites and to our clients websites, we may not be able to effectively monetize this traffic or otherwise retain customers. Our failure to do so could result in lower advertising revenue from our owned and operated websites as well as third-party publishers websites, which would have an adverse effect on our business, financial condition and results of operations.

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;

- third-party 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;

- 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 customers 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

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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.

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 we expect the trend 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 content 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 the monetization capabilities of our mobile marketing services, we may not remain competitive, which may negatively affect our business and results of operations.

A reduction in online marketing spend by our clients, a loss of clients or lower advertising yields may seriously harm our business, financial condition and results of operations. In addition, 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 may be harmed.

We rely on clients marketing spend on our owned and operated websites and on our network of third-party publisher websites. We have historically derived, and we expect to continue to derive, the majority of our revenue through the delivery of qualified leads, clicks, calls and customers. One component of our platform that we use to generate client interest is our system of monetization tools, which is designed to match content with client offerings in a manner that optimizes revenue yield and end-user experience. Clients will stop spending marketing funds on our owned and operated websites or our third-party publisher websites if their investments do not generate sales leads, and ultimately customers or if we do not deliver advertisements in an appropriate and effective manner. The failure of our yield-optimized monetization technology to effectively match advertisements or client offerings with our content in a manner that results in increased revenue for our clients would have an adverse impact on our ability to maintain or increase our revenue from client marketing spend.

Even if our content is effectively matched with advertisements or client offerings, our current clients may not fulfill their obligations under their existing contracts with us and they may not continue to place marketing spend or advertisements on our websites beyond the terms of their existing contracts. If any of our clients decided not to continue marketing spend or advertising on our owned and operated websites or on our third-party publisher websites, we could experience a rapid decline in our revenue over a relatively short period of time. Any factors that limit the amount our clients are willing to and do spend on marketing or advertising with us, or to purchase leads from us, could have a material adverse effect on our business.

Furthermore, a substantial portion of our revenue is generated from a limited number of clients. None of our clients account for 10% or more of our revenue. However, we have a few clients that account for a large portion of our net revenue. Our clients can generally terminate their contracts with us at any time, with limited prior notice or penalty. Clients who have longer-term contracts may fail to honor their existing contracts, fail to renew their contracts or reduce their level of business with us, leading to lower revenue.

In addition, reductions in business by one or more significant clients may trigger price reductions for our other clients whose prices for certain products 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 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, we could incur 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, including third-party security reviews, 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 or result in cancellation of client contracts. 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 results of operations. In addition, we could incur significant costs in complying with the multitude of state, Federal and foreign laws regarding personally identifiable information.

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.

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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 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 September 30, 2014, we had debt with a principal balance of $73.8 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.

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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. Certain other companies within our industry 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 customers and, thereby, clients, also depends in part on customers receiving competitive levels of customer service, responsiveness and prices from our lead purchaser clients. If our clients do not provide competitive levels of service to customers, our reputation and therefore our ability to attract additional clients and customers 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.

We also believe that building brand awareness is important to achieving increased demand for certain of our products and services. Accordingly, we have dedicated, and expect to continue to dedicate, significant operating capital and resources to building brand awareness, which may not be successful. Our failure to build brand awareness may adversely affect our ability to attract and retain clients in a cost-effective manner and as a result, our business, financial condition and results of operations.

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 or if we are not able to scale our business quickly enough to meet our clients growing needs, 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 scaling our technology to accommodate a larger business and integrate acquisitions;

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

maintaining our client service standards; and

developing and improving our operational, financial and management controls and maintaining adequate reporting systems and procedures.

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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. We may spend substantial amounts to purchase or lease data centers and equipment, upgrade our technology and network infrastructure to handle increased traffic on our owned and operated websites and roll out new products and services. This expansion could be expensive and complex and could result in inefficiencies or operational failures. If we do not implement this expansion successfully, or if we experience inefficiencies and operational failures during its implementation, the quality of our products and services and our users experience could decline. This could damage our reputation and cause us to lose current and potential customers and clients. The costs associated with these adjustments to our architecture could harm our operating results. Accordingly, 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 results of operations.

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 of operations 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 may 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 third-party 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 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.

Our business depends on continued and unimpeded access to the Internet by us and our users. Internet access providers may be able to block, degrade, or charge for access to certain of our products and services, which could lead to additional expenses and the loss of customers and clients.

Our products and services depend on the ability of our users to access the Internet. Currently, this access is provided by companies that have significant market power in the broadband and Internet access marketplace, including incumbent telephone companies, cable companies, mobile communications companies, and government-owned service providers. Some of these providers have taken, or have stated that they may take measures, including legal actions, that could degrade, disrupt, or increase the cost of user access to our advertisements or our third-party publishers advertisements by restricting or prohibiting the use of infrastructure to support or facilitate our offerings, or by charging increased fees to us or our users to provide our offerings. Such interference could result in a loss of existing customers and clients, and increased costs, and could impair our ability to attract new customers and clients, thereby harming our revenue and growth.

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 results of operations may fluctuate significantly from quarter to quarter due to seasonal fluctuations in advertising spending.

In addition to other factors that cause our results of operations 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 from 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 companies 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. Certain of our metrics are subject to inherent challenges in measurement, and real or perceived inaccuracies in such metrics may harm our reputation and negatively affect our business. We present key metrics such as cost-per-click, cost-per-lead and cost-per-acquisition some of which are calculated using internal data. We periodically review and refine our some of our methodologies for monitoring, gathering, and calculating these metrics. Based on this process, from time to time we update our methodologies. While our metrics are based on what we believe to be reasonable measurements and methodologies, there are inherent challenges in deriving our metrics. In addition, our user metrics may differ from estimates published by third-parties or from similar metrics of our competitors due to differences in methodology. If advertisers or publishers do not perceive our metrics to be accurate, or if we discover material inaccuracies in our metrics, it could negatively affect our business model and current or potential clients willingness to adopt our metrics.

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 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 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, as well as new technologies that block our ability to deliver Internet-based advertising, 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 data derived from the use of cookies. Technologies, tools, software and applications (including new and enhanced web browsers) have been developed and are likely to continue to be developed that can block or allow users to opt out of display, search, and Internet-based advertising and content, delete or block the cookies used to deliver such advertising, or shift the location in which advertising appears on pages so that our advertisements do not show up in the most monetizable places on our pages or are obscured. As a result, the adoption of such technologies, tools, software, and applications could reduce the number of display and search advertisements that we are able to deliver and/or our ability to deliver Internet-based advertising and this, in turn, could reduce our results of operations.

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.

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

In order to comply with the Sarbanes-Oxley Act of 2002, 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 results of operations 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.

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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.

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 results of operations 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 and June 30, 2014 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 in those periods.

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 our 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 viewing the underlying content. Action fraud occurs when online lead 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 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.

As a public company, we are subject to compliance initiatives that will require substantial time from our management and result in significantly increased costs that may adversely affect our operating results and financial condition.

The Securities Exchange Act of 1934, Sarbanes-Oxley Act of 2002, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, and other rules implemented by the SEC and NASDAQ, impose various requirements on public companies, including requiring changes in corporate governance practices. These and proposed corporate governance laws and regulations under consideration may further increase our compliance costs. If compliance with these various legal and regulatory requirements diverts our management s attention from other business concerns, it could have a material adverse effect on our business, financial condition and results of operations. We also expect that these laws and regulations may make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage than used to be available. As a result, it may be more difficult for us to attract and retain qualified individuals to serve on our board of directors, on committees of our board of directors, or as executive officers.

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;

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, which 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;

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- 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 September 30, 2014, 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;

- 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 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;

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- 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 have not declared or paid dividends on our common stock and we do not intend to do so 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)	Second Amendment to Credit Agreement dated as of July 17, 2014.
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.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Filed herewith.
Furnished herewith.
(1) Incorporated by reference to Exhibit 10.1 to QuinStreet, Inc. s Current Report on Form 8-K (SEC File No. 001-34628) filed on July 22, 2014.

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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: November 6, 2014

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