

ELLIE MAE INC  
Form 10-Q  
July 29, 2016  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2016

OR

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

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

Commission File Number: 001-35140

ELLIE MAE, INC.

(Exact name of registrant as specified in its charter)

Delaware 94-3288780  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

4420 Rosewood Drive, Suite 500 94588  
Pleasanton, California (Zip Code)  
(Address of principal executive offices) (925) 227-7000  
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer  Accelerated filer

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

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

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

As of July 27, 2016:

Class	Number of Shares
Common Stock, \$0.0001 par value	30,215,306

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## PART I—FINANCIAL INFORMATION

## ITEM 1—CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Ellie Mae, Inc.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands, except share and per share amounts)

	June 30, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$44,609	\$ 34,396
Short-term investments	46,859	48,975
Accounts receivable, net of allowance for doubtful accounts of \$218 and \$124 as of June 30, 2016 and December 31, 2015, respectively	44,306	28,568
Prepaid expenses and other current assets	11,262	9,874
Total current assets	147,036	121,813
Property and equipment, net	105,787	81,360
Long-term investments	41,592	55,473
Intangible assets, net	19,861	22,810
Deposits and other assets	8,248	8,888
Goodwill	74,547	74,547
Total assets	\$397,071	\$ 364,891
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$9,526	\$ 9,911
Accrued and other current liabilities	27,385	37,307
Deferred revenue	18,824	15,864
Total current liabilities	55,735	63,082
Leases payable, net of current portion	151	685
Other long-term liabilities	14,926	10,273
Total liabilities	70,812	74,040
Commitments and contingencies (Note 8)		
Stockholders' equity:		
Common stock, \$0.0001 par value per share; 140,000,000 authorized shares, 30,198,074 and 29,566,511 shares issued and outstanding as of June 30, 2016 and December 31, 2015, respectively	3	3
Additional paid-in capital	307,227	285,342
Accumulated other comprehensive income (loss)	172	(257 )
Retained earnings	18,857	5,763
Total stockholders' equity	326,259	290,851
Total liabilities and stockholders' equity	\$397,071	\$ 364,891

See accompanying notes to these condensed consolidated financial statements (unaudited).

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Ellie Mae, Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

(in thousands, except share and per share amounts)

	Three Months ended		Six Months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Revenues	\$90,098	\$ 65,942	\$ 163,723	\$ 120,131
Cost of revenues	28,453	20,862	55,084	38,212
Gross profit	61,645	45,080	108,639	81,919
Operating expenses:				
Sales and marketing	12,506	8,804	27,792	18,564
Research and development	14,662	9,282	27,115	17,579
General and administrative	17,793	14,149	33,525	26,451
Total operating expenses	44,961	32,235	88,432	62,594
Income from operations	16,684	12,845	20,207	19,325
Other income, net	162	153	361	285
Income before income taxes	16,846	12,998	20,568	19,610
Income tax provision	6,258	5,368	7,474	8,396
Net income	\$ 10,588	\$ 7,630	\$ 13,094	\$ 11,214
Net income per share of common stock:				
Basic	\$0.36	\$ 0.26	\$0.44	\$ 0.39
Diluted	\$0.34	\$ 0.25	\$0.42	\$ 0.37
Weighted average common shares used in computing net income per share of common stock:				
Basic	29,578,630	30,092,149	29,643,779	28,931,042
Diluted	31,188,590	30,807,417	31,279,512	30,643,071
Net income	\$ 10,588	\$ 7,630	\$ 13,094	\$ 11,214
Other comprehensive income, net of taxes:				
Unrealized gain (loss) on investments	101	(41)	) 429	130
Comprehensive income	\$ 10,689	\$ 7,589	\$ 13,523	\$ 11,344

See accompanying notes to these condensed consolidated financial statements (unaudited).

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Ellie Mae, Inc.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)

	Six Months ended June 30,	
	2016	2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 13,094	\$ 11,214
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	8,679	4,310
Provision for uncollectible accounts receivable	111	(6 )
Amortization of intangible assets	2,949	2,511
Stock-based compensation expense	14,708	11,084
Excess tax benefit from stock-based compensation	(1,234 )	(3,852 )
Deferred income taxes	6,153	6,433
Loss on disposal of property and equipment	5	90
Amortization of investment premium	490	530
Changes in operating assets and liabilities:		
Accounts receivable	(15,849 )	(8,759 )
Prepaid expenses and other current assets	(1,388 )	4,592
Deposits and other assets	(1,580 )	(762 )
Accounts payable	(432 )	(984 )
Accrued, other current and other liabilities	(6,629 )	7,821
Deferred revenue	2,895	4,628
Net cash provided by operating activities	21,972	38,850
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Acquisition of property and equipment	(15,566 )	(17,196 )
Acquisition of internal-use software	(16,373 )	(13,260 )
Proceeds from sale of property and equipment	—	37
Purchases of investments	(35,615 )	(28,306 )
Maturities of investments	31,551	28,703
Sale of investments	20,000	—
Net cash used in investing activities	(16,003 )	(30,022 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payment of capital lease obligations	(2,080 )	(1,730 )
Proceeds from issuance of common stock under employee stock plans	9,127	8,579
Payments for repurchase of common stock	—	(8,830 )
Tax payments related to shares withheld for vested restricted stock units	(4,037 )	(2,537 )
Excess tax benefit from stock-based compensation	1,234	3,852
Net cash provided by (used in) financing activities	4,244	(666 )
NET INCREASE IN CASH AND CASH EQUIVALENTS	10,213	8,162
CASH AND CASH EQUIVALENTS, Beginning of period	34,396	26,756
CASH AND CASH EQUIVALENTS, End of period	\$ 44,609	\$ 34,918



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Ellie Mae, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - (continued)

(UNAUDITED)

(in thousands)

	Six Months ended June 30,	
	2016	2015
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$ 145	\$ 69
Cash paid for income taxes	\$ 129	\$ 511
Supplemental disclosure of non-cash investing and financing activities:		
Fixed asset purchases accrued but not paid	\$ 3,709	\$ 1,687
Stock-based compensation capitalized to property and equipment	\$ 1,125	\$ 464
Acquisition of property and equipment under capital leases	\$ —	\$ 7,020

See accompanying notes to these condensed consolidated financial statements (unaudited).



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Ellie Mae, Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1—Description of Business

Ellie Mae, Inc. (“Ellie Mae,” “the Company,” “we,” “our” or “us”) is a leading provider of innovative on-demand software solutions and services for the residential mortgage industry in the United States. The Company’s Encompass all-in-one mortgage management solution provides one system of record that allows banks, credit unions, and mortgage lenders to originate and fund mortgages and improve compliance, loan quality, and efficiency.

NOTE 2—Basis of Presentation and Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (“U.S. GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015, which was filed with the SEC on February 25, 2016 (“2015 Form 10-K”). The condensed consolidated balance sheet as of December 31, 2015, included herein, was derived from the audited financial statements as of that date but does not include all disclosures, including notes required by U.S. GAAP. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial positions, results of operations and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full year 2016 or any future period.

Principles of Consolidation

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

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management evaluates estimates on a regular basis including those relating to revenue recognition, allowance for doubtful accounts, goodwill, intangible assets, valuation of deferred income taxes, stock-based compensation, and unrecognized tax benefits, among others. Actual results could differ from those estimates and such differences may have a material impact on the Company’s condensed consolidated financial statements and footnotes.

Significant Accounting Policies

The Company’s significant accounting policies are described in Note 2 of the Notes to Consolidated Financial Statements in its 2015 Form 10-K. There have been no significant changes to these policies during the six months ended June 30, 2016.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes certain changes in equity that are excluded from net income, specifically unrealized gains on available-for-sale investments. Except for net realized gain on investments which was not significant, there were no reclassifications out of accumulated other comprehensive income that affected net income during the three and six months ended June 30, 2016 and 2015.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This standard also requires significantly expanded

disclosures about revenue recognition. In August 2015, the FASB deferred the effective date of this standard by one year. In March, April and May 2016, the FASB clarified the implementation guidance on principal versus agent, identifying performance obligations, licensing, collectability,

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noncash consideration, presentation of sales tax, and certain other transition matters. The new effective date for public entities will be for fiscal years, and interim periods within those years, beginning after December 15, 2017, but entities will be permitted to early adopt the standard as of the original effective date. The Company has not yet developed an expectation of the impact that adoption will have on its consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (“ASU 2016-01”), which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017 and early adoption is not permitted. The Company has not yet developed an expectation of the impact that adoption may have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU 2016-02”), which requires lessees to put most leases on their balance sheets but recognize the expenses on their income statements in a manner similar to current practice. ASU 2016-02 states that a lessee would recognize a lease liability for the obligation to make lease payments and a right-to-use asset for the right to use the underlying asset for the lease term. The new standard is effective for interim and annual periods beginning after December 15, 2018 and early adoption is permitted. The Company has not yet developed an expectation of the impact that adoption may have on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, Compensation—Stock Compensation (Topic 718) (“ASU 2016-09”). This standard makes several modifications to Topic 718 related to the accounting for forfeitures, employer tax withholding on share-based compensation and the financial statement presentation of excess tax benefits or deficiencies. ASU 2016-09 also clarifies the statement of cash flows presentation for certain components of share-based awards. The standard is effective for interim and annual reporting periods beginning after December 15, 2016, although early adoption is permitted. The Company has not yet developed an expectation of the impact that adoption may have on its consolidated financial statements.

**NOTE 3—Net Income Per Share of Common Stock**

Net income per share of common stock is calculated by dividing net income by the weighted average shares of common stock outstanding during the period. Diluted net income per share of common stock is calculated by dividing net income by the weighted average shares of common stock outstanding and potential shares of common stock during the period. Potential shares of common stock include dilutive shares attributable to the assumed exercise of stock options, restricted stock unit awards (“RSUs”), performance-vesting RSUs, performance share awards (“Performance Awards”), and Employee Stock Purchase Plan (“ESPP”) shares using the treasury stock method, if dilutive.

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The components of net income per share of common stock were as follows:

	Three Months ended June 30,		Six Months ended June 30,	
	2016	2015	2016	2015
	(in thousands, except share and per share amounts)			
Net income	\$10,588	\$ 7,630	\$13,094	\$ 11,214
Basic shares:				
Weighted average common shares outstanding	29,578,630	29,092,149	29,643,778	28,931,042
Diluted shares:				
Weighted average shares used to compute basic net income per share	29,578,630	29,092,149	29,643,778	28,931,042
Effect of potentially dilutive securities:				
Employee stock options, RSUs, performance-vesting RSUs, Performance Awards and ESPP shares	1,609,969	1,715,268	1,635,733	1,712,029
Weighted average shares used to compute diluted net income per share	31,188,599	30,807,417	31,279,511	30,643,071
Net income per share:				
Basic	\$0.36	\$ 0.26	\$0.44	\$ 0.39
Diluted	\$0.34	\$ 0.25	\$0.42	\$ 0.37

The following potential weighted average common shares were excluded from the computation of diluted net income per share, as their effect would have been anti-dilutive:

	Three Months ended June 30,		Six Months ended June 30,	
	2016	2015	2016	2015
Employee stock options and awards	31,721	190,186	237,177	395,182

Performance-vesting RSUs and Performance Awards are included in the diluted shares outstanding for each period if the established performance criteria have been met at the end of the respective periods. However, if none of the required performance criteria have been met for such awards, the Company includes the number of shares that would be issuable if the end of the reporting period were the end of the contingency period. Accordingly, in addition to the employee stock options and awards noted above, 136,598 and 186,312 shares underlying performance-vesting RSUs and Performance Awards were excluded from the dilutive shares outstanding for each of the three and six months ended June 30, 2016 and 2015, respectively.

**NOTE 4—Financial Instruments and Fair Value Measurements**

Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are classified and disclosed in one of the following three categories:

Level 1 — Valuations based on quoted prices in active markets for identical assets or liabilities.

Level 2 — Valuations based on other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 — Valuations based on inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the assets or liabilities.

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The following tables set forth by level within the fair value hierarchy the Company's financial assets that were accounted for at fair value on a recurring basis:

	Fair Value at June 30, 2016	Fair Value Measurements Using Inputs Considered as Level 1	Level 2
Cash equivalents:			
Money market funds	\$2,687	\$2,687	\$—
Corporate notes and obligations	191	—	191
U.S. government and government agency obligations	225	—	225
Investments:			
Certificates of deposit	11,593	—	11,593
Corporate notes and obligations	31,009	—	31,009
Municipal obligations	7,176	—	7,176
U.S. government and government agency obligations	38,673	5,314	33,359
	\$91,554	\$8,001	\$83,553

	Fair Value at December 31, 2015	Fair Value Measurements Using Inputs Considered as Level 1	Level 2
Cash equivalents:			
Money market funds	\$6,788	\$6,788	\$—
Investments:			
Certificates of deposit	12,928	—	12,928
Corporate notes and obligations	28,205	—	28,205
Municipal obligations	2,648	—	2,648
U.S. government and government agency obligations	60,667	19,429	41,238
	\$111,236	\$26,217	\$85,019

The Company classifies its money market funds that are specifically backed by debt securities and U.S. government obligations as Level 1 instruments, due to the use of observable market prices for identical securities that are traded in active markets.

Valuation of the Company's marketable securities investments classified as Level 2 is achieved primarily through broker quotes when such investments exist in a non-active market.

At June 30, 2016 and December 31, 2015, the Company did not have any assets or liabilities that were valued using Level 3 inputs. For the three and six months ended June 30, 2016 and 2015, there were no transfers of financial instruments between the levels.

For the three and six months ended June 30, 2016, the Company recognized interest income from financial instruments of \$0.2 million and \$0.4 million, respectively. For the three and six months ended June 30, 2015, the Company recognized interest income from financial instruments of \$0.2 million and \$0.3 million, respectively. Gross realized gains and losses from the sale of investments were not significant during the three and six months ended June

30, 2016 and 2015.

At June 30, 2016, \$50.0 million of the Company's investments had a contractual maturity of one year or less and \$41.6 million had a contractual maturity of one to three years.

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The carrying amounts, gross unrealized gains and losses and estimated fair value of cash and cash equivalents and both short-term and long-term investments consisted of the following:

	June 30, 2016			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Carrying or Fair Value
	(in thousands)			
Cash and cash equivalents:				
Cash	\$41,506	\$ —	\$ —	\$ 41,506
Money market funds	2,687	—	—	2,687
Corporate notes and obligations	191	—	—	191
U.S. government and government agency obligations	225	—	—	225
	\$44,609	\$ —	\$ —	\$ 44,609
Investments:				
Corporate notes and obligations	\$30,951	\$ 66	\$ (8 )	\$ 31,009
Certificates of deposit	11,563	31	(1 )	11,593
Municipal obligations	7,159	17	—	7,176
U.S. government and government agency obligations	38,606	71	(4 )	38,673
	\$88,279	\$ 185	\$ (13 )	\$ 88,451
	December 31, 2015			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Carrying or Fair Value
	(in thousands)			
Cash and cash equivalents:				
Cash	\$27,608	\$ —	\$ —	\$ 27,608
Money market funds	6,788	—	—	6,788
	\$34,396	\$ —	\$ —	\$ 34,396
Investments:				
Corporate notes and obligations	\$28,314	\$ 1	\$ (110 )	\$ 28,205
Certificates of deposit	12,945	5	(22 )	12,928
Municipal obligations	2,647	1	—	2,648
U.S. government and government agency obligations	60,799	10	(142 )	60,667
	\$104,705	\$ 17	\$ (274 )	\$ 104,448

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The following table shows the gross unrealized losses and the related fair values of the Company's investments that have been in a continuous unrealized loss position. The Company did not identify any investments as other-than-temporarily impaired at June 30, 2016 or December 31, 2015.

	June 30, 2016		12 Months or		Total	
	Less than 12 Months	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(in thousands)					
Corporate notes and obligations	\$5,107	\$ (8 )	\$919	\$ (1 )	\$6,026	\$ (9 )
Certificates of deposit	1,043	(1 )	201	—	1,244	(1 )
U.S. government, government agency, and municipal obligations	3,749	(3 )	384	—	4,133	(3 )
	\$9,899	\$ (12 )	\$1,504	\$ (1 )	\$11,403	\$ (13 )
	December 31, 2015		12 Months or		Total	
	Less than 12 Months	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(in thousands)					
Corporate notes and obligations	\$23,969	\$ (99 )	\$2,514	\$ (11 )	\$26,483	\$ (110 )
Certificates of deposit	9,284	(22 )	—	—	9,284	(22 )
U.S. government, government agency, and municipal obligations	48,394	(139 )	1,793	(3 )	50,187	(142 )
	\$81,647	\$ (260 )	\$4,307	\$ (14 )	\$85,954	\$ (274 )

The following table summarizes the maturities of the Company's investments at June 30, 2016:

	Carrying or Fair Value (in thousands)
Remainder of 2016	\$ 22,109
2017	38,936
2018	22,244
2019	3,916
Thereafter	1,246
Total	\$ 88,451

Actual maturities may differ from the contractual maturities because borrowers may have the right to call or prepay certain obligations.



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## NOTE 5—Balance Sheet Components

## Property and Equipment

Property and equipment, net, consisted of the following:

	June 30, 2016	December 31, 2015
	(in thousands)	
Computer equipment and software <sup>(1)</sup>	\$87,731	\$55,928
Furniture and fixtures	6,706	5,292
Leasehold improvements	18,488	14,405
Property and equipment	112,925	75,625
Accumulated depreciation and amortization <sup>(1)</sup>	(37,210 )	(28,552 )
Net property and equipment	75,715	47,073
Internal-use software and other assets not placed in service	30,072	34,287
	\$105,787	\$81,360

<sup>(1)</sup> Includes computer equipment and software under capital leases

Computer equipment and software under capital leases, net, consisted of the following:

	June 30, 2016	December 31, 2015
	(in thousands)	
Computer equipment	\$8,715	\$8,715
Software	1,517	1,517
Accumulated amortization	(4,999 )	(3,371 )
Net computer equipment and software under capital leases	\$5,233	\$6,861

Depreciation expense for the three and six months ended June 30, 2016 was \$4.7 million and \$8.7 million, respectively. Depreciation expense for the three and six months ended June 30, 2015 was \$2.5 million and \$4.3 million, respectively. Amortization of assets under capital leases which is included in depreciation expense for the three and six months ended June 30, 2016 was \$0.8 million and \$1.6 million, respectively. Amortization of assets under capital leases which is included in depreciation expense for the three and six months ended June 30, 2015 was \$0.6 million and \$0.9 million, respectively.

## Accrued and Other Current Liabilities

Accrued and other current liabilities consisted of the following:

	June 30, 2016	December 31, 2015
	(in thousands)	
Accrued payroll and related expenses	\$17,439	\$23,938
Accrued commissions	1,101	1,993
Accrued professional fees	457	223
Accrued royalties	2,526	1,546
Sales and other taxes	1,885	1,536
Current portion of leases payable	2,300	3,845
Other accrued expenses	1,677	4,226
	\$27,385	\$37,307

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## NOTE 6— Goodwill and Intangible Assets

The carrying value of goodwill at June 30, 2016 was \$74.5 million. There were no changes in the carrying value of goodwill during the three and six months ended June 30, 2016.

Other intangible assets, net, consisted of the following:

	June 30, 2016			
	Gross Carrying Amount	Accumulated Amortization	Net Intangibles	Weighted Average Remaining Useful Life
	(in thousands)			(in years)
Assets subject to amortization:				
Developed technology	\$ 11,535	\$ (7,109 )	\$ 4,426	2.9
Trade names	331	(322 )	9	0.3
Customer relationships	19,400	(8,319 )	11,081	4.4
Order backlog	370	(64 )	306	3.3
Total assets subject to amortization:	31,636	(15,814 )	15,822	4.0
Assets not subject to amortization:				
Trade name	4,039	—	4,039	
	\$35,675	\$ (15,814 )	\$ 19,861	

	December 31, 2015			
	Gross Carrying Amount	Accumulated Amortization	Net Intangibles	Weighted Average Remaining Useful Life
	(in thousands)			(in years)
Assets subject to amortization:				
Developed technology	\$ 11,535	\$ (5,668 )	\$ 5,867	3.1
Trade names	331	(307 )	24	0.8
Customer relationships	19,400	(6,875 )	12,525	4.8
Order backlog	370	(15 )	355	3.8
Total assets subject to amortization:	31,636	(12,865 )	18,771	4.2
Assets not subject to amortization:				
Trade name	4,039	—	4,039	
	\$35,675	\$ (12,865 )	\$ 22,810	

Amortization expense associated with intangible assets for the three and six months ended June 30, 2016 was \$1.5 million and \$2.9 million, respectively. Amortization expense associated with intangible assets for the three and six months ended June 30, 2015 was \$1.2 million and \$2.5 million, respectively.

Minimum future amortization expense for intangible assets at June 30, 2016 was as follows:

	Amortization (in thousands)
Remainder of 2016	\$ 2,572
2017	4,294
2018	3,443
2019	3,166
2020	1,778
2021	314
Thereafter	255
	\$ 15,822



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## NOTE 7—Income Taxes

The Company computes its interim provision for income taxes by applying the estimated annual effective tax rate to the year-to-date income from recurring operations and adjusts the provision for discrete tax items recorded in the period. The Company evaluates and updates its estimated annual effective income tax rate on a quarterly basis. The estimated annual effective tax rate as of June 30, 2016 and 2015 was 37.4% and 42.0%, respectively.

	Three Months		Six Months	
	ended June 30,		ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Income tax provision	6,258	5,368	7,474	8,396
Effective tax rate	37.2 %	41.3 %	36.3 %	42.8 %

The difference between the federal statutory rate of 35% and the Company's estimated effective tax rate for the three and six months ended June 30, 2016 was primarily due to the Company's state income tax provision, non-deductible stock-based compensation expenses, and R&D credits.

The Company realized a tax benefit of \$1.2 million for the three and six months ended June 30, 2016 related to the exercise of employee stock options and the vesting of RSUs, performance-vesting RSUs and Performance Awards. The Company realized a tax benefit of \$0.9 million and \$3.9 million for the three and six months ended June 30, 2015 related to the exercise of employee stock options and the vesting of RSUs, performance-vesting RSUs and Performance Awards. The net income tax benefit in excess of the expenses recorded for financial reporting purposes has been recorded as an increase to additional paid-in capital and is reflected as a financing cash inflow in the condensed consolidated statements of cash flows.

The Company's tax positions are subject to income tax audits by multiple tax jurisdictions. The Company accounts for uncertain tax positions and believes that it has provided adequate reserves for its unrecognized tax benefits for all tax years still open for assessment. The Company also believes that it does not have any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within the next twelve months.

The Company has a policy to classify accrued interest and penalties associated with uncertain tax positions together with the related liability in the balance sheet, and to include the expenses incurred related to such accruals in the provision for income taxes. There were no interest or penalties included in the provision for income taxes during the six months ended June 30, 2016 and 2015, respectively.

The Company is currently under examination by the U.S. Internal Revenue Service for the 2013 tax year. At this time, the Company is not able to estimate the potential impact that the examination may have on income tax expense. If the examination is resolved unfavorably, it may have a negative impact on the Company's results of operations.

## NOTE 8—Commitments and Contingencies

## Leases

As of June 30, 2016, the Company leased eight facilities under operating lease arrangements. The lease expiration dates range from September 2016 to December 2025. Certain leases contain escalation clauses calling for increased rents. The Company recognizes rent expense on a straight-line basis over the lease period and has recorded deferred rent for the difference between rent payments and rent expense recognized. Pursuant to the expiration of the Company's Irvine office lease, in February 2016, the Company entered into a new lease agreement for approximately 4,600 square feet of office space in Irvine, California. The term of the lease commenced on June 1, 2016 with an initial term of 60 months, with payments ranging from \$12,800 per month to \$15,000 per month.

## Legal Proceedings

From time to time, the Company is involved in litigation that it believes is of the type common to companies engaged in the Company's line of business, including commercial and employment disputes. As of the date of this Quarterly Report on Form 10-Q, the Company is not involved in any pending legal proceedings whose outcome the Company expects to have a material adverse effect on its financial position, results of operations or cash flows. However, litigation is unpredictable and excessive verdicts, both in the form of monetary damages and injunctions, could occur. In the future, litigation could result in substantial costs and diversion of resources and the Company could incur

judgments or enter into settlements of claims that could have a material adverse effect on its business.

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## NOTE 9—Equity and Stock Incentive Plans

The Company recognized stock-based compensation expense related to awards granted under its 2009 Stock Option and Incentive Plan (the “2009 Plan”), 2011 Equity Incentive Award Plan (the “2011 Plan”), and ESPP.

Total stock-based compensation expense recognized consisted of:

	Three Months ended June 30, 2016		Six Months ended June 30, 2015	
	2016	2015	2016	2015
	(in thousands)			
Cost of revenues	\$ 1,132	\$ 813	\$ 2,102	\$ 1,428
Sales and marketing	1,059	673	1,937	1,190
Research and development	1,944	1,376	3,448	2,523
General and administrative	3,883	3,215	7,221	5,943
	\$ 8,018	\$ 6,077	\$ 14,708	\$ 11,084

2009 Stock Option and Incentive Plan and 2011 Equity Incentive Award Plan

## Stock Options

The following table summarizes the Company’s stock option activity under the 2009 Plan and 2011 Plan:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2016	2,515,329	\$ 24.40	7.14	\$ 90,818
Granted	14,506	59.78		
Exercised	(349,910 )	17.88		
Forfeited or expired	(39,112 )	38.42		
Outstanding at June 30, 2016	2,140,813	\$ 25.45	6.75	\$ 141,716
Ending vested and expected to vest at June 30, 2016	2,104,986	\$ 25.19	6.73	\$ 139,894
Exercisable at June 30, 2016	1,434,519	\$ 19.44	6.12	\$ 103,590

There were no stock options granted during the three months ended June 30, 2016. Stock options granted during the six months ended June 30, 2016 were made under the 2011 Plan. There were no grants under the 2009 Plan during the six months ended June 30, 2016.

The aggregate intrinsic value of the stock options outstanding at June 30, 2016 represents the value of the Company’s closing stock price of \$91.65 on June 30, 2016 in excess of the exercise price multiplied by the number of options outstanding for options that were in-the-money. Options outstanding that are expected to vest are net of estimated future option forfeitures.

Following is additional information pertaining to the Company’s stock option activity:

	Three Months ended June 30, 2016		Six Months ended June 30, 2015	
	2016	2015	2016	2015
	(in thousands, except per option amounts)			
Weighted average fair value per option granted	\$ —	\$ 29.12	\$ 27.57	\$ 25.55
Grant-date fair value of options vested	\$ 2,750	\$ 2,619	\$ 5,261	\$ 4,348
Intrinsic value of options exercised	\$ 8,318	\$ 10,287	\$ 21,244	\$ 23,116
Proceeds received from options exercised	\$ 2,409	\$ 3,509	\$ 6,255	\$ 6,858

As of June 30, 2016, total unrecognized stock-based compensation expense related to unvested stock options, adjusted for estimated forfeitures, was \$11.7 million and is expected to be recognized over a weighted average period of 2.1 years.



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## Restricted Stock Units, Performance-Vesting Restricted Stock Units, and Performance Awards

The Performance Awards granted represent the right to receive shares of the Company's common stock, contingent upon the achievement of certain of the Company's performance metrics during the performance period. On a date subsequent to the performance period, the Compensation Committee of the Board of Directors (the "Compensation Committee") determines and approves the achievement of the performance goals (the "Determination Date") and the earned shares are issued, with 25% of the shares vested upon issuance and the remaining shares to vest 25% on each of the first three anniversaries of the Determination Date, subject to the continuous employment of the participant through such dates.

In October 2015, in connection with the acquisition of Mortgage Returns, the Company agreed to pay up to 29,006 of performance-vesting RSUs for a total value of \$2.0 million to the former Chief Executive Officer of Mortgage Returns upon achievement of certain performance criteria and a service requirement during the performance period of October 23, 2015 through October 23, 2019. The performance-vesting RSUs will vest annually based on the achievement of the performance criteria and the service requirement.

In February 2016, the Company granted Mr. Anderman 6,692 performance-vesting RSUs and an option to purchase 14,506 shares of Company common stock. Mr. Anderman may earn between zero and 2.0 shares of common stock for each performance-vesting RSU. As of June 30, 2016, the Company expects that each of these performance-vesting RSUs will convert to 1.15 shares of common stock on the Determination Date. Additionally, in February 2016, the Company granted 64,449 Performance Awards with a performance period of January 1, 2016 through December 31, 2016 to designated participants under the 2011 Plan. The designated participants may earn between zero and 2.0 shares of common stock for each Performance Award. As of June 30, 2016, the Company expects that each of these Performance Awards will convert to 1.55 shares of common stock on the Determination Date in 2017.

The following table summarizes the Company's RSU, Performance Award and performance-vesting RSU activity:

	RSUs		Performance Awards and Performance-Vesting RSUs	
	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Outstanding at January 1, 2016	748,688	\$ 45.52	508,282	\$ 34.68
Granted	474,368	75.02	107,573	59.78
Released	(178,689 )	38.92	(109,219 )	32.44
Forfeited or expired	(43,138 )	52.97	—	—
Outstanding at June 30, 2016	1,001,229	\$ 60.35	506,636	\$ 40.49
Ending vested and expected to vest at June 30, 2016	877,158		506,636	

RSUs, performance-vesting RSUs and Performance Awards that are expected to vest are presented net of estimated future forfeitures. RSUs released during the six months ended June 30, 2016 and 2015 had an aggregate intrinsic value of \$14.6 million and \$8.2 million, respectively, and had an aggregate grant-date fair value of \$7.0 million and \$3.3 million, respectively. Performance-vesting RSUs and Performance Awards released during the six months ended June 30, 2016 and 2015 had an aggregate intrinsic value of \$9.3 million and \$3.2 million, respectively, and had an aggregate grant-date fair value of \$3.5 million and \$1.4 million, respectively. The number of RSUs released includes shares that the Company withheld on behalf of employees to satisfy the minimum statutory tax withholding requirements.

As of June 30, 2016, total unrecognized compensation expense related to unvested RSUs, performance-vesting RSUs and Performance Awards was \$57.5 million and is expected to be recognized over a weighted average period of 2.7 years.



Employee Stock Purchase Plan

For the six months ended June 30, 2016 and 2015, employees purchased 47,819 shares and 58,239 shares, respectively, under the ESPP for a total of \$2.9 million and \$1.7 million, respectively. As of June 30, 2016, unrecognized compensation expense related to the current semi-annual ESPP period, which ends on August 31, 2016, was \$0.4 million and is expected to be recognized over two months.

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## Executive Incentive Plan

On March 14, 2016, the compensation committee adopted the Ellie Mae, Inc. Executive Incentive Plan (the “Executive Incentive Plan”). The Executive Incentive Plan was approved by the Company’s stockholders on May 25, 2016. The Executive Incentive Plan has a term of five years from the date of approval by the stockholders, expiring May 25, 2021, and may be terminated, amended or suspended by the compensation committee at any prior time, and may also be reinstated. The Company currently expects to issue cash bonus and performance-based equity awards under the Executive Incentive Plan to the Company’s executive officers commencing in 2017. The equity awards have the following limitations:

**Stock Option Limitations.** The maximum number of shares that may be granted as an incentive stock option under the Executive Incentive Plan is 70,000,000. No participant will be eligible to receive a stock option covering more than 1,000,000 shares in any calendar year.

**Performance Units/Performance Share Limitations.** No participant will be eligible to receive performance units or performance shares having a grant date value (assuming maximum payout) greater than \$10,000,000 or covering more than 1,000,000 shares, whichever is greater, in any calendar year.

## Valuation Information

The fair value of stock options and stock purchase rights granted under the 2009 Plan, the 2011 Plan, and the ESPP were estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions:

	Three months ended June 30, 2016		Six Months ended June 30, 2015	
Stock option plans:				
Risk-free interest rate	— %	1.73 %	1.38 %	1.74 %
Expected life of options (in years)	0	5.90	6.08	5.99
Expected dividend yield	— %	— %	— %	— %
Volatility	— %	48 %	47 %	48 %
Employee Stock Purchase Plan:				
Risk-free interest rate	0.36 %	0.13 %	0.36 %	0.13 %
Expected life of options (in years)	0.50	0.50	0.50	0.50
Expected dividend yield	— %	— %	— %	— %
Volatility	46 %	35 %	46 %	35 %

## Common Stock

The following numbers of shares of common stock were reserved and available for future issuance at June 30, 2016:

	Reserved Shares
Options and awards outstanding under stock option plans	3,648,678
Shares available for future grant under the 2011 Equity Incentive Award Plan	3,900,222
Shares available under the Employee Stock Purchase Plan	1,452,840
Total	9,001,740

In February 2016, 295,665 additional shares were reserved under the ESPP and 1,478,325 additional shares were reserved under the 2011 Plan, pursuant to the automatic increase provisions in the plan.

## Stock Repurchase Program

In May 2014, the Company’s board of directors approved a stock repurchase program under which the Company is authorized to repurchase up to \$75.0 million of its common stock, which expires in May 2017. All shares are retired upon repurchase. The Company did not repurchase any shares during the six months ended June 30, 2016. As of June 30, 2016, \$43.5 million remained available for future repurchases under the program.



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## NOTE 10—Segment Information

The Company operates in one industry—mortgage-related software and services. The Company’s chief operating decision maker is its chief executive officer, who makes decisions about resource allocation and reviews financial information presented on a consolidated basis. Accordingly, the Company has determined that it has a single reporting segment and operating unit structure, specifically technology-enabled solutions to help streamline and automate the residential mortgage origination process for its network participants.

The Company is organized primarily on the basis of service lines. Supplemental disclosure of revenues by type is as follows:

	Three months ended June 30,		Six Months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
On-demand revenues <sup>(1)</sup>	\$89,906	\$64,785	\$163,005	\$117,757
On-premise revenues <sup>(1)</sup>	192	1,157	718	2,374
	\$90,098	\$65,942	\$163,723	\$120,131

<sup>(1)</sup> Certain reclassifications of prior period amounts have been made to conform to the current period presentation, such reclassification did not materially change previously reported consolidated financial statements.

On-demand revenue is generated from company-hosted software subscriptions that customers access through the Internet. On-demand revenue is comprised of fees for software services sold both as a subscription and transactionally including fees based on a per closed loan, or success, basis subject to monthly base fees, which the Company refers to as Success-Based Pricing; Ellie Mae Network fees; education and training, loan product, policy and guideline data and analytics services under the AllRegs brand; and professional services which include consulting, implementation, and training services.

On-premise revenue is generated from maintenance services, sales of customer-hosted software licenses, and related professional services. Effective May 1, 2016, the Company no longer provides software releases or technical support for the on-premise version of Encompass.

## NOTE 11—Subsequent Events

In July 2016, the Company entered into an amendment to its existing office lease in Pleasanton, California to expand office space by four floors, or approximately 143,500 square feet. The term of the lease for two of the four floors will commence on April 1, 2017 and for the remaining two floors, will commence on February 1, 2018. The term of the lease for the aggregate leased space ends on December 31, 2025 with payments ranging from approximately \$201,600 per month to \$527,300 per month during the lease period.

## ITEM 2—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q, including this Management’s Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements relate to future events or our future financial performance. Forward-looking statements may include words such as “may,” “will,” “should,” “expect,” “plan,” “intend,” “anticipate,” “believe,” “estimate,” “predict,” “potential,” “could,” or other similar wording indicating future results or expectations. Forward-looking statements are subject to risks and uncertainties and actual events or results may differ materially. Factors that could cause our actual results to differ materially include, but are not limited to, those discussed under “Risk Factors” in this report. We also face risks and uncertainties relating to our business including: outages and other system interruptions in our hosted Encompass software or the Ellie Mae Network service and any related impact on our reputation; our ability to protect the confidential information of our Encompass users, Ellie Mae Network participants and their respective customers; fluctuations in mortgage lending volume; the volume of mortgages originated by our Encompass users; the impact of changes in mortgage interest rates; changes in mortgage originator, lender, investor or service provider behavior and any related impact on the residential mortgage industry; our ability to accurately forecast revenues and appropriately plan our expenses; the

number of Encompass users, including contracted Encompass users; the effectiveness of our marketing and sales efforts to attract new and retain existing Encompass users and Ellie Mae Network participants; transaction volume on the Ellie Mae Network; the level of demand for our Encompass Docs Solution, our Encompass Product and Pricing Service, and other services we offer; the level of adoption of our Total Quality Loan, or TQL, program; our ability to enhance the features and functionality of our Encompass software and the Ellie Mae Network including the development and successful deployment of our next generation Encompass platform; the timing of the introduction and acceptance of new Ellie Mae Network offerings and new on-demand services; customer

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renewal and upgrade rates; the increased time, cost, and complexity that may be required to successfully target larger customers; our ability to scale our operations and increase productivity to support our existing and growing customer base; our ability to successfully manage our growth and any future acquisitions of businesses, solutions or technologies; the risk that the anticipated benefits and growth prospects expected from our recent acquisitions may not be fully realized or may take longer to realize than expected; the timing of future acquisitions of businesses, solutions or technologies, and new product launches; the impact of uncertain domestic and worldwide economic conditions, including the resulting effect on residential mortgage volumes; changes in government regulation affecting mortgage lending, Ellie Mae Network participants or our services, and potential structural changes in the U.S. residential mortgage industry; the attraction and retention of qualified employees and key personnel; our ability to compete effectively in a highly competitive market and adapt to technological changes; our ability to successfully incorporate changes in consumer protection laws and other laws relating to mortgage lending into our products and services so that our customers remain compliant with such laws, including Encompass and our Encompass Compliance Service; our ability to protect our intellectual property, including our proprietary Encompass software; costs associated with defending intellectual property infringement and other claims and our ability to maintain effective internal controls and the risk of natural and man-made catastrophic interruptions to our business. We undertake no obligation to revise or update any forward-looking statements to reflect any event or circumstance that arises after the date of this report, or to conform such statements to actual results or changes in our expectations.

This discussion should be read in conjunction with the condensed consolidated financial statements and notes presented in this Quarterly Report on Form 10-Q and the consolidated financial statements and notes in our Annual Report on Form 10-K for the year ended December 31, 2015, or 2015 Form 10-K.

In this report, references to “Ellie Mae,” “the Company,” “we,” “our” or “us” refer to Ellie Mae, Inc. together with its subsidiaries, unless the context requires otherwise.

Overview

We are a leading provider of innovative on-demand software solutions and services for the residential mortgage industry in the United States. Our Encompass all-in-one mortgage management solution provides one system of record that allows banks, credit unions, and mortgage lenders to originate and fund mortgages and improve compliance, loan quality, and efficiency.

Mortgage originators use our Encompass software, a comprehensive mortgage management system that handles key business and management functions involved in running a residential mortgage origination business. Mortgage originators use Encompass as a single tool for loan processing, marketing, and customer communication and to interact electronically with lenders, investors, and service providers over the Ellie Mae Network. Our software also enables enforcement of rules and business practices designed to ensure loan quality, adherence to processing standards and regulatory compliance.

The Ellie Mae Network electronically connects approximately 153,000 mortgage professionals using Encompass to the broad array of mortgage lenders, investors, and third-party service providers integral to the origination and funding of residential mortgages. During the mortgage origination process, mortgage originators may order various services through the Ellie Mae Network, including credit reports; product eligibility and pricing services; automated underwriting services; appraisals; title reports; insurance; flood certifications and flood insurance; compliance reviews; fraud detection; document preparation; and verification of income, identity, and employment. Mortgage originators can also initiate secure data transmission to and from lenders and investors.

On-demand revenues are generated primarily from subscriptions to software we host that customers access through the Internet, including customers who pay fees based on the number of loans they fund, or success basis, subject to monthly base fees, which we refer to as Success Based Pricing, and related professional services such as consulting, implementation, and training services. On-demand revenues also include software services that are sold transactionally; Ellie Mae Network transaction fees paid by lender-investors, service providers, and certain government-sponsored entities participating on the Ellie Mae Network; education and training; and loan product and guideline data and analytics services that are provided under the AllRegs brand. On-premise revenues are generated from customer-hosted software licenses and related professional services and maintenance services. Effective May 1, 2016, we no longer provide software releases or technical support for the on-premise version of Encompass. As of

June 30, 2016, all on-premise customers completed migrating to our on-demand Encompass offering, and we do not expect significant future on-premise revenues.

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Our on-demand revenues typically, but not always, track the seasonality of the residential mortgage industry, with increased activity in the second and third quarters and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. Mortgage volumes are also impacted by other factors such as interest rate fluctuations, home sale activity, regulatory changes such as the TILA-RESPA Integrated Disclosure rule which became effective in October 2015, and general economic conditions, which can lead to departures from the typical seasonal pattern. For example, increases in mortgage interest rates could reduce the volume of new mortgages originated and, in particular, the volume of mortgage refinancings. Conversely, recent decreases in interest rates may increase the volume of new mortgages and mortgage refinancings. We currently estimate that approximately 30% to 40% of our revenues have some direct sensitivity to volume. The base fee portion of success-based revenues, subscription revenues, professional services revenues, and revenues from sales of AllRegs services, are not affected by fluctuations in mortgage origination volume.

We are investing aggressively in initiatives that we believe will help us continue to grow our business, improve our products and services, and strengthen our competitive advantage while bringing sustainable long-term value to our customers. During 2015 and the first two quarters of 2016, we increased our investments in our sales and client services capabilities, research and development, technology infrastructure, and data security to support our user additions and overall business growth and maintain the confidentiality of our customers' data. These investments include expanding our talent across the organization by hiring additional personnel. To support customers and further differentiate ourselves, we currently anticipate that throughout 2016 and into the foreseeable future, we will continue to increase our investment in key areas such as research and development, enterprise sales, services, technical support, data security, and data center infrastructure. This investment includes the development of our next generation Encompass platform, which we anticipate will be incrementally introduced over the coming quarters and through 2017. The costs associated with these investments decreased our gross margin percentage and increased operating expenses in the first six months of 2016 as compared to the same period in 2015. We expect to continue investing in these areas, and such expenditures may affect our ability to improve our margins as we grow revenue.

In addition to our internal initiatives, our business strategy has evolved to address recent industry trends, including:

- increased quality standards imposed by regulators, lenders, and investors;
  - increased regulation affecting lenders and investors;
- greater focus by our customers on operational efficiencies;
- customers adopting multi-channel strategies; and
- greater focus by customers and regulators on data security and consumer privacy

We are responding to these trends as follows:

Increased quality standards imposed by regulators, lenders and investors. Encompass is designed to automate and streamline the process of originating mortgages to, among other things, satisfy increased quality requirements of investors. Relevant features of Encompass include enabling customers' management to impose processing rules and formats, and providing milestone and process reminders, automated population of forms with accurate data, and accurate and automated transmission of loan files and data from originators to investors and lenders. Our TQL program is designed to further enhance the quality, compliance, and salability of loans that are originated through Encompass. Additionally, TQL is intended to reduce the possibility of errors in the process of transferring information from originator to investor and to give investors confidence in the accuracy and regulatory compliance of the information that is underlying loan files.

In response to the increased quality standards and compliance mandates affecting the industry, we expect an increased number of non-Encompass mortgage lenders to assess new platform options and replace their legacy systems. We have increased the size of our customer acquisition, implementation, and support teams in order to address anticipated demand for our software solutions.

Increased regulation affecting lenders and investors. Regulatory reforms have significantly increased the complexity and importance of regulatory compliance. We devote considerable resources to continually upgrading our software to help our customers address regulatory changes. We offer Encompass Compliance Service, which analyzes mortgage



loan data for compliance with consumer protection laws and institutionally mandated compliance policies and also alerts users to possible violations of these laws and policies. In addition, we have a staff of attorneys that work with compliance experts who help ensure that documents prepared using our software and the processes recommended by the Encompass workflow comply with applicable rules and regulations. For example, additional tools and product updates were required to address the Ability-to-Repay/Qualified Mortgage and Federal and State High Cost rules that became effective in January 2014. In addition, we updated certain of our products to comply with the TILA-RESPA Integrated Disclosure rule changes that took effect in October 2015. We believe we are also well-positioned to help our customers meet future Dodd-Frank Act or other similar requirements as they are published and become effective. However, changes to existing laws or regulations or adoption of new laws or regulations relating to the residential mortgage industry could require us to incur significant costs to update our products and services so that our customers remain compliant with such laws and regulations.

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Greater focus on operational efficiencies. The average total production cost per loan was \$8,025 in the first quarter of 2014<sup>1</sup>, \$7,195 in the first quarter of 2015<sup>2</sup>, and \$7,845 in the first quarter of 2016<sup>3</sup>. We expect operational costs to continue to be a significant consideration for mortgage originators due to continued increased regulation and heightened quality standards. By automating many of the functions of mortgage origination, we enable our users to comply with regulations and process quality loans more efficiently and effectively. This reduces the cost of originating a loan and lowers the risk of buy-back demands from investors resulting from poorly originated or documented loans or loans that fail to comply with applicable regulations. We continually address the changing needs of our customers by developing and enhancing tools to allow for simplified regulatory compliance, increased availability of information, and enhanced system functionality and performance.

With an eye towards providing customers with ever-improving tools to enhance efficiency, we currently anticipate that we will continue to develop new service offerings through the Ellie Mae Network and pursue adoption of our services through initiatives such as our TQL program. By integrating and expanding our current and new services, we aim to provide a more comprehensive solution to our users.

Customers adopting multi-channel strategies. Customers are developing multi-channel strategies beyond a single retail, correspondent or wholesale mortgage lending channel in order to grow their businesses. The requirements of these different channels vary and in order to maintain a single operating system, customers must use a robust system with customizable functionality. Encompass includes support for multi-channel workflows, allowing our customers to drive efficiencies and boost productivity by creating distinct workflows for each channel that map to our customers' business needs. Encompass users can customize workflows based on channel, loan purpose or specific loan criteria - all of which can vary between lending channels. Additionally, Encompass Consumer Direct enables our customers to originate loans directly from borrowers by offering an online loan application that can be accessed by anyone with a web browser.

Greater focus by customers and regulators on data security and consumer privacy. Recent high-profile data security incidents affecting banking institutions and cloud-service software providers have resulted in an increased focus on data security by our customers and our customers' regulators. We are making significant investments in the security of the Encompass service, as well as our internal systems, processes and monitoring capabilities to protect our customers' data and help minimize the risk of data security loss. We expect the industry focus on data security to continue to increase, and we anticipate that our investments in data security will increase substantially over time.

Acquisition Strategy

Our industry is highly fragmented, and we believe there are strategic opportunities available to acquire technology based companies that offer mortgage origination functionality that will complement and increase the attractiveness of our solutions. In October 2015, we acquired substantially all the assets of Mortgage Returns, LLC, a company that provides on-demand customer relationship management or CRM and marketing automation solutions for the residential mortgage industry. With the acquisition of Mortgage Returns we are responding to the needs of our customers by adding a robust CRM solution for lenders of all sizes. We believe this acquisition enhances our marketing platform and furthers our mission of automating the entire end-to-end mortgage process for our customers. In October 2014, we acquired substantially all the assets of AllRegs, a provider of research and reference, education, documentation, and data analytics products relating to the mortgage industry. The assets that we acquired from AllRegs allow us to strengthen our products through product integration and introduce new products related to training, compliance management systems, and loan product eligibility.

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<sup>1</sup> Mortgage Bankers Association, Independent Mortgage Bankers Report Net Production Losses in the First Quarter of 2014, June 10, 2014.

<sup>2</sup> Mortgage Bankers Association, Independent Mortgage Banks' Profits Up in 1st Quarter 2015, June 3, 2015.

<sup>3</sup> Mortgage Bankers Association, Independent Mortgage Banks Profits Up from Previous Quarter, Down Year-over-Year, June 7, 2016.



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## Operating Metrics

We use certain operational metrics to evaluate our business, determine allocation of our resources, and make decisions regarding corporate strategy. We focus on these metrics to determine our success in leveraging our user base to increase our revenues and to gauge the degree of our market penetration.

These metrics are defined below.

**Contracted revenues.** Contracted revenues are those revenues that are fixed by the terms of a contract and are not affected by fluctuations in mortgage origination volume. These revenues consist of the base fee portion of success-based revenues, monthly per-user subscription revenues, professional services revenues, revenues from sales of AllRegs services, and subscription revenues paid for products other than Encompass.

**Active users.** An active user is a mortgage origination professional who has used Encompass at least once within a 90-day period preceding the measurement date. A user is a mortgage origination professional working at an Encompass mortgage lender, such as a mortgage bank, commercial bank, thrift or credit union, which sources and funds loans and generally sells these funded loans to investors; or a mortgage brokerage, which typically processes and submits loan files to a mortgage lender or mega lender that funds the loan.

**Contracted users.** A contracted user is a mortgage origination professional who has a license to use Encompass and has an obligation to pay for this license, but who is not necessarily an active user.

**Average active users.** Average active users during a period is calculated by averaging the monthly active users during a reporting period.

**Revenue per average active Encompass user.** Revenue per average active Encompass user is calculated by dividing total revenues by average active Encompass users.

The following table shows these operating metrics as of and for the three and six months ended June 30, 2016 and 2015:

	Three Months ended		Six Months ended June	
	June 30,		30,	
	2016	2015	2016	2015
Revenues (in thousands):				
Total revenues	\$90,098	\$65,942	\$163,723	\$120,131
Total contracted revenues	\$49,582	\$35,778	\$95,538	\$67,664
Users at end of period:				
Contracted users	192,980	141,498	192,980	141,498
Active users	153,334	126,862	153,334	126,862
Active users as a percentage of contracted users	79	% 90	% 79	% 90
Average active users:				
Average active users during the period	149,876	125,341	145,478	119,877
Revenue per average active user during the period	\$601	\$526	\$1,125	\$1,002

## Basis of Presentation

## General

Our consolidated financial statements include the accounts of Ellie Mae, Inc. and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated upon consolidation.

## Revenue Recognition

We generate revenue primarily from transaction-based fees, and fees for software and related services including our annual user conference and fees from professional services. Our software can be accessed either through a company-hosted subscription or a customer-hosted license. Accordingly, our revenue is described as on-demand or on-premise. Sales taxes assessed by governmental authorities are excluded from revenue.

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### On-demand Revenue

On-demand revenue is generated from company-hosted software subscriptions that customers access through the Internet. On-demand revenue is comprised of fees for software services sold both as a subscription and transactionally including fees based on a per closed loan, or success, basis subject to monthly base fees, which we refer to as Success-Based Pricing; Ellie Mae Network fees; education and training, loan product, policy and guideline data and analytics services under the AllRegs brand; and professional services which include consulting, implementation, and training services.

### On-premise Revenue

On-premise revenue is generated from maintenance services, sales of customer-hosted software licenses, and related professional services.

### Cost of Revenues and Operating Expenses

#### Cost of Revenues

Our cost of revenues consists primarily of: salaries and benefits, including stock-based compensation expense; third-party royalty expenses; customer support; data centers; depreciation on data center computer equipment; amortization of acquired intangible assets such as developed technology and trade names; amortization of internal-use software; professional services associated with implementation of our software; and allocated facilities costs. We expect that our cost of revenues will continue to increase in absolute dollars as our revenues increase, as we make additional and accelerated investments to bolster our infrastructure and enhance our system capacity, reliability, and data security, as we pursue additional strategic acquisitions, as we place new internal-use software into service and as we continue to hire additional personnel in our implementation and customer support departments to support new customers and provide new services. To support customers and further differentiate ourselves, we currently anticipate that throughout 2016 we will continue to increase our investment in key areas such as research and development, enterprise sales, services, technical support, data security, and data center infrastructure. This will include development of our next generation Encompass platform, which we expect to incrementally introduce over the coming quarters and throughout 2017.

#### Sales and Marketing

Our sales and marketing expenses consist primarily of: salaries, benefits, and incentive compensation, including stock-based compensation expense and commissions; allocated facilities costs; expenses for trade shows, public relations, our annual user conference, and other promotional and marketing activities; expenses for travel and entertainment; and amortization of acquired intangible assets such as customer relationships. We expect that our sales and marketing expense will continue to increase as we continue to hire additional sales personnel in order to address anticipated demand for our software solutions and as we pursue additional strategic acquisitions. We also intend to increase marketing activities focused on Encompass, our Ellie Mae Network offerings and our other Encompass services.

#### Research and Development

Our research and development expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense; fees to contractors engaged in the development and support of the Ellie Mae Network, Encompass software, and other products; and allocated facilities costs. We expect that our research and development expenses will continue to increase in absolute dollars as we continue to invest in our products and services and related next-generation enhancements, including hiring additional engineering and product development personnel and as we pursue additional strategic acquisitions.

#### General and Administrative

Our general and administrative expenses consist primarily of: salaries and benefits, including bonuses and stock-based compensation expense for employees involved in finance, accounting, human resources, administrative, information technology, and legal roles; third-party provider expenses such as general consulting, legal, accounting, and other professional services; and allocated facilities costs. We expect general and administrative expenses to continue to increase in absolute dollars as we hire additional personnel and grant stock-based awards to attract and retain the employees needed to continue to grow our business and as we pursue additional strategic acquisitions.

#### Other Income, Net

Other income, net consists of interest income earned on investments and cash accounts, offset by investment discount amortization and imputed interest expense related to our acquisition holdback payments, and interest expense paid on equipment and software leases.

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## Income Taxes

On a quarterly basis, we evaluate our expected income tax expense or benefit based on our year-to-date operations, and we record an adjustment in the current quarter. The net tax provision is the result of the mix of profits earned by us and our subsidiaries in tax jurisdictions with a broad range of income tax rates. We are required to estimate deferred tax assets and liabilities based on the differences between the financial reporting and tax bases of assets and liabilities measured using the enacted tax rates that will be in effect when the differences are expected to reverse. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in our consolidated statements of operations become deductible expenses under applicable income tax laws or loss or credit carry forwards are utilized. Accordingly, realization of our deferred tax assets is dependent on future taxable income against which these deductions, losses, and credits can be utilized. We use management judgment to assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not more likely than not, we must establish a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not to be realized.

## Critical Accounting Policies and Estimates

There have been no material changes during the three and six months ended June 30, 2016 to our critical accounting policies and estimates previously disclosed in our 2015 Form 10-K.

## Results of Operations

The following tables set forth our results of operations for the periods presented and as a percentage of our revenues for those periods. The period-to-period comparison of financial results is not necessarily indicative of future results.

	Three Months ended June 30,		Six Months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
Revenues	\$90,098	\$65,942	\$163,723	\$120,131
Cost of revenues <sup>(1)</sup>	28,453	20,862	55,084	38,212
Gross profit	61,645	45,080	108,639	81,919
Operating expenses:				
Sales and marketing <sup>(1)</sup>	12,506	8,804	27,792	18,564
Research and development <sup>(1)</sup>	14,662	9,282	27,115	17,579
General and administrative <sup>(1)</sup>	17,793	14,149	33,525	26,451
Total operating expenses	44,961	32,235	88,432	62,594
Income from operations	16,684	12,845	20,207	19,325
Other income, net	162	153	361	285
Income before income taxes	16,846	12,998	20,568	19,610
Income tax provision	6,258	5,368	7,474	8,396
Net income	\$10,588	\$7,630	\$13,094	\$11,214

<sup>(1)</sup> Stock-based compensation included in the above line items:

	Three Months ended June 30,		Six Months ended June 30,	
	2016	2015	2016	2015
	(in thousands)			
Cost of revenues	\$1,132	\$813	\$2,102	\$1,428
Sales and marketing	1,059	673	1,937	1,190
Research and development	1,944	1,376	3,448	2,523
General and administrative	3,883	3,215	7,221	5,943
	\$8,018	\$6,077	\$14,708	\$11,084





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	Three Months ended June 30, 2016		Six Months ended June 30, 2015	
Revenues	100.0%	100.0%	100.0%	100.0%
Cost of revenues	31.6	31.6	33.6	31.8
Gross profit	68.4	68.4	66.4	68.2
Operating expenses:				
Sales and marketing	13.9	13.4	17.0	15.5
Research and development	16.3	14.1	16.6	14.6
General and administrative	19.7	21.5	20.4	22.0
Total operating expenses	49.9	49.0	54.0	52.1
Income from operations	18.5	19.4	12.4	16.1
Other income, net	0.2	0.2	0.2	0.2
Income before income taxes	18.7	19.6	12.6	16.3
Income tax provision	6.9	8.1	4.6	7.0
Net income	11.8 %	11.5 %	8.0 %	9.3 %

Comparison of the Three and Six Months Ended June 30, 2016 and 2015

## Revenues

The following table sets forth our revenues by type for the periods presented:

	Three Months ended June 30, 2016		Six Months ended June 30, 2015	
	2016	2015	2016	2015
	(dollars in thousands)			

## Revenue by type:

On-demand <sup>(1)</sup>	\$89,906	\$64,785	\$163,005	\$117,757
On-premise <sup>(1)</sup>	192	1,157	718	2,374
Total	\$90,098	\$65,942	\$163,723	\$120,131

	Three Months ended June 30, 2016		Six Months ended June 30, 2015	
	2016	2015	2016	2015

## Revenue by type:

On-demand	99.8 %	98.2 %	99.6 %	98.0 %
On-premise	0.2 %	1.8 %	0.4 %	2.0 %
Total	100.0 %	100.0 %	100.0 %	100.0 %

<sup>(1)</sup> Certain reclassifications of prior period amounts have been made to conform to the current period presentation, such reclassification did not materially change previously reported consolidated financial statements.

Three months ended June 30, 2016. Total revenues increased \$24.2 million, or 36.6%, for the three months ended June 30, 2016 as compared to the same period of 2015.

On-demand revenues increased by \$25.1 million, or 38.8% during the three months ended June 30, 2016, consisting primarily of a \$16.4 million increase in Encompass revenue. The increase in Encompass revenue resulted partially from a \$10.9 million, or 44.0%, increase in base fees due to a 36.4% increase in contracted users as of June 30, 2016 compared to the same period in 2015, and an increase of \$5.5 million in closed loan fees, which are assessed for loans closed in excess of base fees under our Success Based Pricing model. The closed loan fee increase was driven by an increase in contracted users.

Additional contributors to the growth in on-demand revenue included a \$3.9 million increase in network revenues due to an increase in contracted users as well as an increase in adoption and usage of network services of third party Flood,

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and Credit providers to process loans, a \$2.0 million increase in revenues from professional services, driven primarily by implementation and training services provided to new customers and to customers that upgraded from our on-premise product offering, a \$1.7 million increase in revenue due to subscription revenues from our Mortgage Returns acquisition, a \$0.8 million increase in revenues from AllRegs products and services, and a \$0.7 million increase in revenues from other software and services due to an increase in TQL adoption and usage by Encompass users.

On-premise revenues decreased by \$1.0 million for the three months ended June 30, 2016 compared to the same period in 2015, primarily due to our strategy of completing the phase-out of the on-premise version of Encompass effective May 1, 2016.

Six months ended June 30, 2016. Total revenues increased \$43.6 million, or 36.3%, for the six months ended June 30, 2016 as compared to the same period of 2015.

On-demand revenues increased by \$45.2 million, or 38.4% during the six months ended June 30, 2016, consisting primarily of a \$24.8 million increase in Encompass revenue. The increase in Encompass revenue resulted partially from a \$19.8 million, or 41.3%, increase in base fees due to a 36.4% increase in contracted users as of June 30, 2016 compared to the same period in 2015, and an increase of \$5.0 million in closed loan fees, which are assessed for loans closed in excess of base fees under our Success Based Pricing model. The closed loan fee increase was driven by an increase in contracted users.

Additional contributors to the growth in on-demand revenue included a \$6.6 million increase in network revenues due to an increase in contracted users as well as an increase in adoption and usage of network services of third party Flood, Appraisal, Credit, and Title providers to process loans, a \$4.7 million increase in revenues from professional services driven primarily by training and implementation services provided to new customers and to customers that upgraded from our on-premise product offering, a \$4.0 million increase in revenues from other software and services due to an increase in TQL adoption and our user conference, a \$3.2 million increase in revenue due to subscription revenues from our Mortgage Returns acquisition, and a \$2.7 million increase of revenues from AllRegs products and services. On-premise revenues decreased by \$1.7 million for the six months ended June 30, 2016 compared to the same period of 2015, primarily due to our strategy of completing the phase-out of the on-premise version of Encompass effective May 1, 2016.

## Gross Profit

	Three Months ended		Six Months ended June	
	June 30,		30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Gross profit	\$61,645	\$45,080	\$108,639	\$81,919
Gross margin	68.4	% 68.4	% 66.4	% 68.2

Gross profit increased by \$16.6 million and gross margin percentage remained relatively flat during the three months ended June 30, 2016 as compared to the same period in 2015. Revenues increased by \$24.2 million and cost of revenues increased by \$7.6 million. The flat gross margin percentage was a result of an increase in revenue offset by an increase in fixed costs associated with headcount added to our implementation, professional services, and customer support organizations, investments we have made in expanding our data centers, and enhancing data security for our customers. The increase in costs primarily include a \$3.0 million increase in salaries, employee benefits, and stock-based compensation expenses associated with additional headcount for our professional services and customer support organizations in anticipation of continued increasing demand for our software solutions, a \$1.7 million increase in third-party royalty expenses arising from the increased revenues, a \$1.6 million increase in depreciation expense related to internal-use software placed into production, and a \$1.3 million increase in expenses related to upgrades to our data centers hardware and technology and third-party services to assist in data security and infrastructure upgrades.

Gross profit increased by \$26.7 million and gross margin percentage decreased by 1.8% during the six months ended June 30, 2016 as compared to the same period in 2015. Revenues increased by \$43.6 million and cost of revenues

increased by \$16.9 million. The decrease in the gross margin percentage was a result of an increase in fixed costs associated with headcount added to our implementation, professional services, and customer support organizations, investments we have made in expanding our data centers, and enhancing data security for our customers. The increase in cost of revenues was primarily due to a \$6.8 million increase in salaries, employee benefits, and stock-based compensation expenses associated with increased headcount in our professional services and customer support organizations in anticipation of continued increasing demand for our software solutions, a \$3.7 million increase in third-party royalty expenses arising from the increased revenues, a \$2.9 million increase in depreciation expense related to internal-use software placed into service, a \$1.7 million increase in third-party services to assist in security

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upgrades and infrastructure upgrades, and a \$1.6 million increase in expenses related to upgrades to our data centers hardware and technology.

## Sales and Marketing

	Three Months ended		Six Months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Sales and marketing	\$12,506	\$8,804	\$27,792	\$18,564
Sales and marketing as a % of revenues	13.9	% 13.4	% 17.0	% 15.5

Sales and marketing expenses increased by \$3.7 million, or 42.0%, for the three months ended June 30, 2016 as compared to the same period in 2015. Sales and marketing expenses as a percentage of revenues increased by 0.5%.

The increase in sales and marketing expenses was primarily due to a \$2.4 million increase in salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to grow our sales and marketing department in an effort to increase our market share and address anticipated demand for our software solutions and additional headcount from the Mortgage Returns acquisition, a \$0.5 million increase in commissions paid to our sales representatives arising from increased bookings, and a \$0.5 million increase in other marketing and promotion expenses.

Sales and marketing expenses increased by \$9.2 million, or 49.7%, for the six months ended June 30, 2016 as compared to the same period in 2015. Sales and marketing expenses as a percentage of revenues increased by 1.5%.

The increase to the sales and marketing expenses were primarily due to a \$3.8 million increase in salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to grow our sales and marketing department in an effort to increase our market share and address anticipated demand for our software solutions and increased headcount from the Mortgage Returns acquisition, a \$3.6 million increase in marketing and promotion expenses including our user conference, and a \$1.2 million increase in commissions paid to our sales representatives arising from the increased revenues.

## Research and Development

	Three Months ended		Six Months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Research and development	\$14,662	\$9,282	\$27,115	\$17,579
Research and development as a % of revenues	16.3	% 14.1	% 16.6	% 14.6

Research and development expenses increased by \$5.4 million, or 58.0%, for the three months ended June 30, 2016 as compared to the same period in 2015. Research and development expenses as a percentage of revenues increased by 2.2%. The increase in research and development expenses was due to a \$6.4 million increase in total research and development costs, primarily driven by salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to invest in our products and services and additional headcount from the Mortgage Returns acquisition, partially offset by approximately a \$1.0 million decrease as a result of the capitalization of research and development expenses related to internal-use software and website development projects. Costs associated with the development of internally developed software are capitalized to property and equipment rather than expensed, and amortized over their respective useful lives when the related assets are placed into service.

Research and development expenses increased by \$9.5 million, or 54.2%, for the six months ended June 30, 2016 compared to the same period in 2015. Research and development expenses as a percentage of revenues increased by 2.0%. The increase in research and development expenses was due to a \$11.4 million increase in total research and development costs, primarily driven by salaries, employee benefits, and stock-based compensation expenses related to increased headcount as we continue to invest in our products and services and additional headcount from the Mortgage Returns acquisition, offset by a \$1.9 million decrease as a result of the capitalization of research and development expenses related to internal-use software and website development projects. Costs associated with the development of internal-use software and website development are capitalized to property and equipment rather than

expensed, and amortized over their respective useful lives when the related assets are placed into service.

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## General and Administrative

	Three Months ended		Six Months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
General and administrative	\$17,793	\$14,149	\$33,525	\$26,451
General and administrative as a % of revenues	19.7 %	21.5 %	20.4 %	22.0 %

General and administrative expenses increased by \$3.6 million, or 25.8%, for the three months ended June 30, 2016 as compared to the same period in 2015. General and administrative expenses as a percentage of revenues decreased by 1.8%. The increase in general and administrative expenses was primarily due to a \$2.0 million increase in salaries, stock-based compensation, and employee benefits related to increased headcount from both the Mortgage Returns acquisition and hiring within the Information Technology organization. The remainder of the increase is due to several items including an increase in depreciation expense related to the release of new systems and internally developed software placed into production, an increase in third-party services related to system upgrades, and an increase in technology expenses to support increased headcount.

General and administrative expenses increased by \$7.1 million, or 26.7%, for the six months ended June 30, 2016 as compared to the same period in 2015. General and administrative expenses as a percentage of revenues decreased by 1.6%. The increase in general and administrative expenses were primarily due to a \$3.8 million increase in salaries, stock-based compensation, and employee benefits related to increased headcount from both the Mortgage Returns acquisition and hiring within the Information Technology organization, and a \$1.1 million increase in depreciation expense related to the release of new systems and internally developed software placed into production. The remainder of the increase is due to several items including an increase in third-party services related to system upgrades and an increase in technology expenses to support increased headcount.

## Income Tax Provision

Income tax provision was \$6.3 million for the three months ended June 30, 2016, compared to \$5.4 million for the three months ended June 30, 2015. The increase in income tax provision was primarily due to the increase in income before income taxes.

Income tax provision was \$7.5 million for the six months ended June 30, 2016, compared to \$8.4 million for the six months ended June 30, 2015. The decrease in income tax provision was primarily due to a decrease in effective tax rate from 42.8% for the six months ended June 30, 2015 to 36.3% for the six months ended June 30, 2016. This reduction in the effective tax rate was primarily due to the reduction of nondeductible stock option expense and benefits from R&D credits as the credits became permanent in 2016.

The Company is currently under examination by the U.S. Internal Revenue Service for the 2013 tax year. At this time, the Company is not able to estimate the potential impact that the examination may have on income tax expense. If the examination is resolved unfavorably, it may have a negative impact on the Company's results of operations.

## Liquidity and Capital Resources

At June 30, 2016, we had cash, cash equivalents, and short-term investments of \$91.5 million and long-term investments of \$41.6 million. Cash and cash equivalents consist of cash and money market accounts. Both short and long-term investments consist of corporate bonds and obligations, certificates of deposit, municipal obligations, U.S. government notes, and U.S. government agency securities.

We believe that our existing cash, cash equivalents, and short-term investments will be sufficient to fund capital expenditures, operating expenses and other cash requirements for at least the next 12 months. We may enter into acquisitions in the future, which could require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

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The following table sets forth our statement of cash flows data for the periods presented:

	Six Months ended		Net Change
	June 30, 2016	2015	
	(in thousands)		
Net cash provided by operating activities	\$21,972	\$38,850	(16,878)
Net cash used in investing activities	(16,003 )	(30,022 )	14,019
Net cash provided by (used in) financing activities	4,244	(666 )	4,910
Net increase in cash and cash equivalents	\$10,213	\$8,162	\$2,051

**Operating Activities**

Cash provided by operating activities for the six months ended June 30, 2016 decreased by \$16.9 million as compared to the same period in 2015. In the condensed consolidated statements of cash flows, cash provided by operating activities is presented as net income adjusted for non-cash items and changes in operating assets and liabilities. Net income increased by \$1.9 million for the six months ended June 30, 2016 as compared to the same period in 2015. Non-cash items resulted in an increase in cash from operations of \$10.8 million for the six months ended June 30, 2016 as compared to the same period in 2015. Changes in operating assets and liabilities resulted in a decrease in cash from operations of \$29.5 million for the six months ended June 30, 2016 as compared to the same period in 2015. The \$10.8 million increase in the net contribution of non-cash items to cash provided by operating activities was primarily due to a \$4.4 million increase in depreciation from data center equipment, internal-use software, leasehold improvements, and furniture and fixtures placed into service, a \$3.6 million increase in stock-based compensation expense due to increased headcount, and a \$2.6 million increase in the tax benefit from stock-based compensation. Changes in operating assets and liabilities resulted in a net decrease of \$29.5 million to cash used in operating activities for the six months ended June 30, 2016 as compared to the same period in 2015. Our net accounts receivable balance fluctuates from period to period, depending on the amount and timing of sales and billing activity, our customers' payment method, and cash collections. Additionally, we experienced overall growth in our accounts receivable balance due to increased revenue for the six months ended June 30, 2016 as compared to the same period in 2015. The change in prepaid expenses and other current assets was primarily due to the timing of payments for internal-use software maintenance and other maintenance services. The change in deposits and other assets was due to increased deferred commission expenses associated with continuing sales of our products. The change in accounts payable and accrued and other liabilities was due to an increase in compensation costs associated with increased headcount as well as the timing of additional liabilities and payments in general, and does not reflect any significant change in the nature of accrued liabilities. The increase in deferred revenue is primarily the result of continued sales of subscriptions following the acquisition of Mortgage Returns as well as an increase in sales of professional services, offset by a decrease in undelivered software maintenance as customers have adopted our on-demand platform which does not include the sale of stand-alone maintenance.

**Investing Activities**

Our primary investing activities have consisted of purchases and maturities of investments, and purchases of property and equipment (including costs incurred to develop internal-use software). Purchases of property and equipment may vary from period to period due to the timing of the expansion of our operations and the timing of our internal-use software projects subject to capitalization. We plan to continue to increase investments in hardware and software to support our growth and corporate infrastructure as well as the next generation Encompass platform, and we intend to continue pursuing strategic acquisitions.

Cash used in investing activities of \$16.0 million for the six months ended June 30, 2016 was primarily the result of \$15.6 million in expenditures for purchases of property, including capital improvements to our new corporate headquarters, investments to bolster our infrastructure and enhance our system capacity, reliability, and security, and \$16.4 million in expenditures incurred to develop internal-use software and website applications, including the development of our next generation Encompass platform. Additionally, we sold net \$15.9 million of investments to fund these expenditures.



Cash used in investing activities of \$30.0 million for the six months ended June 30, 2015 was the result of \$30.5 million for purchases of property and equipment and costs incurred to develop internal-use software and website applications, including capital improvements to our new corporate headquarters, investments to bolster our infrastructure and enhance our system capacity, reliability, and security and costs to develop our next generation Encompass platform. We also incurred \$0.4 million in net purchases of investments.

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## Financing Activities

Financing activities have consisted primarily of cash provided from the exercise of stock options and purchases under the employee stock purchase plan and excess tax benefits from stock-based compensation, reduced by the payments related to capital lease obligations, repurchases of common stock and tax payments related to shares withheld for vested restricted stock units, or RSUs. In May 2014, our board of directors approved a stock repurchase program under which we are authorized to repurchase up to \$75.0 million of our common stock over a 36-month period ending in May 2017, \$43.5 million of which remains available as of June 30, 2016. Under the program, purchases may be made from time to time on the open market, and will be funded from available working capital.

Cash provided by financing activities of \$4.2 million for the six months ended June 30, 2016 consisted primarily of \$9.1 million in proceeds from employee stock purchases and the exercise of stock options, and \$1.2 million in excess tax benefits from stock-based compensation, partially offset by \$6.1 million in payments on capital leases and tax payments related to shares withheld for vested RSUs.

Cash used in financing activities of \$0.7 million for the six months ended June 30, 2015 consisted primarily of \$8.6 million in proceeds from employee stock purchases and the exercise of stock options, and \$3.9 million in excess tax benefits from stock-based compensation, offset in part by \$8.8 million in common stock repurchases, and \$4.3 million in payments on capital leases and tax payments related to shares withheld for vested RSUs.

## Off Balance Sheet Arrangements

As of June 30, 2016, we had no off-balance sheet arrangements and operating leases were the only financing arrangements not reported on our condensed consolidated financial statements.

## Contractual Obligations

At June 30, 2016, our contractual payment obligations are as follows:

	Payment due by period (as of June 30, 2016)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
	(in thousands)				
Capital lease obligations	\$2,488	\$1,782	\$706	\$—	\$—
Operating lease obligations*	42,795	2,485	9,802	10,026	20,482
Purchase obligations	11,032	6,136	4,775	121	—
Total	\$56,315	\$10,403	\$15,283	\$10,147	\$20,482

\*Does not reflect lease amendment entered into with SFI Pleasanton, LLC as of July 21, 2016.

Purchase obligations are associated with agreements that are enforceable and legally binding and that specify all significant terms, including: fixed or minimum services to be used; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Purchase obligations include noncancelable contractual obligations for the purchase of services, licenses of third-party software, and construction commitments. Obligations under contracts that we can cancel without a significant penalty are not included in the table above.

In July 2016, the Company entered into an amendment to its existing office lease in Pleasanton, California to expand office space by four floors, or approximately 143,500 square feet. The term of the lease for two of the four floors will commence on April 1, 2017 and for the remaining two floors, will commence on February 1, 2018. The term of the lease for the aggregate leased space ends on December 31, 2025 with payments ranging from approximately \$201,600 per month to \$527,300 per month during the lease period.

## ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We believe that there have been no significant changes in our market risk exposures for the three and six months ended June 30, 2016, as compared with those discussed in our 2015 Form 10-K.

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ITEM 4—CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2016. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the 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 Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the Securities and Exchange Commission’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 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 June 30, 2016, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at a 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 Rule 13a-15(d) and 15d-15(d) of the 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.

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PART II—OTHER INFORMATION

ITEM 1—LEGAL PROCEEDINGS

For a description of the material legal proceedings, please see Note 8 of the Notes to Condensed Consolidated Financial Statements.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below and the other information in this report. If any of the following risks materialize, our business could be materially harmed, and our financial condition and results of operations could be materially and adversely affected. The risks described below are not the only ones facing us. Additional risks not currently known to us or that we currently believe are immaterial may also impair our business, results of operations, financial condition, and liquidity.

The following discussion of risk factors contains forward-looking statements. These risk factors may be important to understanding other statements in this Quarterly Report on Form 10-Q. The following information should be read in conjunction with the condensed consolidated financial statements and related notes in Part I, Item 1, “Financial Statements” and Part I, Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Quarterly Report on Form 10-Q.

Because of the following risks, as well as other factors affecting our financial condition and operating results, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

Any future system interruptions that impair access to Encompass, the Ellie Mae Network or our other services could damage our reputation and brand and may substantially harm our business and operating results.

The satisfactory performance, reliability, and availability of Encompass, the Ellie Mae Network and our other services, including our Encompass Compliance Service, are critical to our reputation and our ability to attract and retain Encompass users and Ellie Mae Network participants. Because our services are complex and incorporate a variety of hardware and proprietary and third-party software, our services may have errors or defects that could result in unanticipated downtime for our customers. Internet-based services frequently contain undetected errors when first introduced or when new versions or enhancements are released, and we have from time to time found errors and defects in our services and new errors and defects in our services may be detected in the future.

Moreover, we have experienced and may in the future continue to experience temporary system interruptions to Encompass, the Ellie Mae Network, or our other services for a variety of other reasons, including network failures, power failures, problems with Encompass and other third-party firmware updates, as well as an overwhelming number of Encompass users or Ellie Mae Network participants trying to access our services during periods of strong demand. In addition, our services may be subject to security or denial of services attacks which result in service interruptions or our customers may use our services in unanticipated ways that may cause a disruption in services for other customers. Since our customers use our service for important aspects of their business, any errors, defects, disruptions in service or other performance problems could result in negative publicity, damage to our reputation and brand, reduce our revenue, increase our operating expenses, negatively impact our ability to run our business, hinder our ability to enroll new customers, cause us to incur legal liability or issue refunds or service credits to our customers and cause us to lose current customers, all of which could substantially harm our business and operating results.

In addition, our two primary data centers, located in Santa Clara, California, and Chicago, Illinois, are hosted by a third-party service provider over which we maintain regular oversight but have little direct control. We depend on this third-party service provider to provide continuous and uninterrupted access to our products and services, including Encompass and the Ellie Mae Network. If for any reason our relationship with this third party were to end unexpectedly, it could require a significant amount of time to transition the hosting of our data centers to a new third-party service provider. We are also subject to interruptions beyond our and our third-party service provider’s control, such as disruptions or congestion in the portions of the Internet linking us to our customers. We are dependent on third parties for the implementation and maintenance of certain aspects of our systems and because some of the causes of system interruptions may be outside of our control, we may not be able to remedy such interruptions in a timely manner. These interruptions may affect our customers’ experience or cause us to lose customers, and may materially harm our reputation and operating results.

Our failure to protect the confidential information of our Encompass users, our Ellie Mae Network participants, and their respective customers could damage our reputation and brand and substantially harm our business and operating results.

We collect, process, transmit, and maintain certain confidential information relating to our Encompass users, our Ellie Mae Network participants and their respective customers, including personally identifiable information. This information resides on

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data center servers hosted by third-party providers, and is transmitted to, across, and from our networks. While we have security measures in place to protect this information and prevent security breaches, these security measures may be compromised as a result of third-party action, including intentional misconduct by computer hackers, advanced persistent cyber-attacks (by hacktivists or cybercriminal organizations), employee error or malfeasance, service provider or vendor error, malfeasance or other intentional or unintentional acts by third parties. Furthermore, customer data, including personally identifiable information, may be lost, exposed, or subject to unauthorized access and/or use as a result of accidents, errors, or malfeasance by our employees, independent contractors, or others working with us or on our behalf. Our servers and systems, and those of our service providers, may also be vulnerable to computer malware, break-ins, denial-of service attacks, and similar disruptions from unauthorized tampering with our computer systems, which could result in someone obtaining unauthorized access to our customers' data or our data, including our intellectual property and other confidential business information. Because the techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and often are not recognized until launched against a target, we may be unable to anticipate these techniques or implement adequate preventative measures. We may also experience security breaches that may remain undetected for an extended period. The possession and use of personal information in conducting our business subjects us to legislative and regulatory burdens that may require notification to customers in the event of a security breach, restrict our use of personal information, and hinder our ability to acquire new customers or market to existing customers.

We cannot guarantee that our security measures will prevent security breaches or the loss or exposure of confidential information or other information we maintain or process. Any actual or perceived compromise of our security could result in the loss of customer data, intellectual property or trade secrets, and could damage our reputation and brand, negatively affect our ability to attract new customers and retain existing customers, adversely affect investor confidence, and expose us to a risk of litigation or regulatory actions and orders, penalties for violation of applicable laws, regulations, or contractual obligations and/or other liabilities, which would substantially harm our business and operating results. We will need to expend significant resources to protect against and remedy any potential security breaches and their consequences, including costs to deploy additional personnel and protection technologies, train employees, and engage third-party experts and consultants.

Our future performance will be highly dependent on our ability to continue to attract Encompass customers and grow revenues from new on-demand services.

To maintain or increase our revenues, we must increase the number of users of our on-demand Encompass software and other services. We cannot guarantee our on-demand SaaS strategy, including our Success Based Pricing model, will continue to be successful. If we are unable to increase the number of Encompass customers or users of our other services, our business may be materially adversely affected.

Our success will depend, to a large extent, on the willingness of mortgage lenders to continue to accept the SaaS model for delivering software applications that they view as critical to the success of their business. Our success will depend on our ability to convince enterprises using on-premise enterprise software solutions to invest significant personnel and financial resources to migrate to our SaaS offering. We will need to continue to expand and optimize our sales infrastructure in order to grow our customer base and our business. Identifying and recruiting qualified personnel and training them in the use of our software requires significant time, expense, and attention. Our business may be adversely affected if our efforts to expand and train our direct sales force do not generate a corresponding increase in revenues.

It is difficult to predict customer adoption rates and demand for our services, the future growth rate and size of the SaaS market or the entry of competitive applications. The growth of the SaaS market depends on a number of factors, including the cost, performance, and perceived value associated with SaaS offerings, as well as the ability of SaaS companies to address security and reliability concerns. If other SaaS providers experience security incidents, loss of customer data, disruptions in delivery or other problems, the market for SaaS applications as a whole, including our own products and services, may be negatively affected. If there is a reduction in demand for SaaS caused by technological challenges, weakening economic conditions, security or privacy concerns, competing technologies, and products, decreases in corporate spending or otherwise, it could result in decreased revenues and our business could be adversely affected.

Our future performance will be highly dependent on our ability to expand the use of settlement services on, and increase the number of transactions effected through, the Ellie Mae Network.

To grow our base of Ellie Mae Network participants, we and settlement service providers must continue to enhance the features and functionality of offerings to them. In addition, increasing the number of settlement service transactions effected through the Ellie Mae Network will depend, in part, on settlement service providers enhancing their technical capabilities, which is largely beyond our control.

We must also convince a variety of potential Ellie Mae Network participants, including mortgage lenders, originators, settlement service providers, and mega lenders, of the benefits of electronic origination and network participation as compared to traditional mortgage origination methods including paper, facsimile, courier, mail, and email.

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We cannot guarantee that our Ellie Mae Network and other service offerings will achieve market acceptance. In the event these efforts are not successful, our business and growth prospects would be adversely affected.

We cannot accurately predict subscription renewal or upgrade rates and the impact these rates may have on our future revenues and operating results.

Our customers have no obligation to renew their subscriptions for our service after the expiration of their initial subscription period, which ranges from one to five years. They may also choose to renew their subscriptions at lower levels. In addition, in the first year of a subscription, customers often purchase a higher level of professional services than they do in renewal years. As a result, our ability to grow is dependent in part on customers purchasing additional subscriptions and services after the initial subscription term. We cannot accurately predict renewal rates given our varied customer base and the number of multi-year subscription contracts. Our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, the prices of services offered by our competitors or reductions in our customers' spending levels due to the macroeconomic environment or other factors. If our customers do not renew their subscriptions for our services, renew on less favorable terms or do not purchase additional subscriptions or services, our revenues may grow more slowly than expected or decline and our profitability and gross margin percentage may be harmed.

Mortgage lending volume was significantly higher in 2015 and in the first half of 2016 than in 2014, but may decrease during the remainder of 2016 and future years, which could materially adversely affect our business.

Mortgage lending volume was significantly higher in 2015 and in the first half of 2016 than in 2014, but may decrease during the remainder of 2016 and future years, which could materially adversely affect our business. Factors that adversely impact mortgage lending volumes include increasing mortgage interest rates, reduced consumer and investor demand for mortgages, more stringent underwriting guidelines, decreased liquidity in the secondary mortgage market, high levels of unemployment, high levels of consumer debt, lower consumer confidence, changes in tax and other regulatory policies, the number of existing mortgages eligible for refinancing, and other macroeconomic factors. Mortgage interest rates are influenced by a number of factors, including monetary policy. In December 2015, the Federal Reserve Bank raised the target federal funds rate from near zero to between 0.25% and 0.50% and signaled that the federal funds rate could be increased further over the next several years. The increase in the federal funds rate may cause mortgage interest rates to rise. Increases in mortgage interest rates could reduce the volume of new mortgages originated, in particular the volume of mortgage refinancings. Additionally, because the ratio of applications to closed loans typically is greater with refinancings than with purchase loans, a continued decrease in refinancings could result in fewer mortgage applications per funded loan. Since we generate some Ellie Mae Network revenues during the application process, regardless of whether the loan is eventually funded, this may negatively impact our transaction based revenue. In addition, our on-demand revenues typically, but not always, track the seasonality of the residential mortgage industry, with increased activity in the second and third quarter and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. As a result, a higher percentage of our on-demand revenues have historically been recognized during those quarters.

We currently estimate that approximately 30% to 40% of our revenues have some direct sensitivity to volume. A decrease in residential mortgage volumes could materially adversely affect our business and operating results.

Furthermore, a significant decrease in mortgage volume could negatively impact our customers, resulting in a reduction of their Encompass users, consolidation with other lenders or cessation of operations. If any of these occurs, it could materially adversely affect our business and operating results.

We expect a number of factors to cause our operating results to fluctuate on a quarterly and annual basis, which may make it difficult to predict our future performance.

Our revenues and operating results have in the past varied and could in the future vary significantly from quarter-to-quarter and year-to-year because of a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be indicative of future operating results. In addition to other risk factors discussed in this section, factors that may contribute to the variability of our quarterly and annual results include:

• the number of Encompass users;



- the volume of mortgages originated by Encompass users, especially users on our Success Based Pricing model;
- transaction volume on the Ellie Mae Network;
- fluctuations in mortgage lending volume;
- the relative mix of purchase and refinance volume handled by Encompass users;
- the level of demand for our services;

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the timing of the introduction and acceptance of Ellie Mae Network offerings and new on-demand services; any write-downs in the value of our property and equipment, goodwill or intangible assets as a result of our investment or acquisition activities;

costs associated with defending intellectual property infringement and other litigation claims; and

changes in government regulation affecting Ellie Mae Network participants or our business.

Due to these and other factors, our future results may not reach our financial projections. In addition, our operating results in future periods may not meet the expectations of investors or public market analysts who follow our company, which could cause our stock price to decline rapidly and significantly. The results of any prior quarterly or annual periods should not be relied upon as indications of our future operating performance.

Since part of our sales efforts are targeted at larger customers, our sales cycle may become longer and more expensive, we may encounter pricing pressure and implementation challenges, and we may have to delay revenue recognition for some complex transactions, all of which could harm our business and operating results.

Part of our business strategy is to target larger mortgage lenders that handle greater volumes of loans. As we target more of our sales efforts at larger customers, we could face greater costs, longer sales cycles, and less predictability in completing some of our sales. In this market, the customer's decision to use our products and services may be an enterprise-wide decision and, if so, this type of sale could require us to provide greater levels of education regarding the use and benefits of our products and services. In addition, larger customers may demand more complex integration, implementation services, and features. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting our own sales and professional services resources to a smaller number of larger transactions, while potentially requiring us to delay revenue recognition on some of these transactions until the technical or implementation requirements have been met.

Supporting our existing and growing customer base could strain our personnel resources, and if we are unable to scale our operations and increase productivity, we may not be able to successfully implement our business plan.

We continue to experience significant growth in our customer base, which has placed a strain on our management and administrative, operational, and financial infrastructure. Additional investments in our implementation capabilities, technical support, technical operations, research and development, and general and administrative functions will be required to scale our operations and increase productivity, address the needs of our customers, further develop and enhance our products and services, and scale with the overall growth of our company.

In addition, professional services, such as implementation services, are a key aspect of on-boarding new customers. The implementation process is complicated and we will need to scale our capabilities in this area to meet future revenue targets. If a customer is not satisfied with the quality of work performed by us or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the customer's dissatisfaction with our products and services could damage our ability to obtain additional work from that customer. In addition, negative publicity related to our customer relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

Our growth strategy will require significant expenditures and resources to improve our technology, systems, and operational infrastructure in order to support a growing number of customers. We will need to make such expenditures with no assurance that the volume of our business or revenues will actually increase.

Our strategy of growing our business and increasing the number of Encompass users has placed and may continue to place significant demands on our technology systems and operational infrastructure. As our operations grow in size, scope, and complexity, we will need to expand, improve, and upgrade our technology systems and, operational infrastructure, including our data centers to offer an increasing number of customers enhanced solutions, features and functionality, and to ensure that our services are reliable.

Our growth and the improvement of our technology systems and operational infrastructure will require significant lead time and substantial financial, operational and technical resources in advance of the anticipated increase in the volume of business, with no assurance that the volume of business or our revenues will actually increase.

If we are not able to provide successful enhancements, new features and modifications to our services, our business could be adversely affected. Further, impairment of software-related assets and other assets may materially adversely affect our operating results.

If we are unable to provide enhancements, new features, and modifications of our existing services, including the successful completion and deployment of our next generation Encompass platform and changes to our services to reflect changes in laws

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and regulations relating to residential mortgage lending, our business and operating results could be adversely affected. In addition, we will need to continuously modify and enhance our services to keep pace with changes in Internet-related and mobile-related technologies and other software, communication, browser and database technologies. We may not be successful in either developing these modifications and enhancements or in bringing them to market in a timely fashion which could increase our costs and adversely affect our business. The failure of our services to operate effectively with future technologies could reduce the demand for our services, result in customer dissatisfaction and adversely affect our business.

We have invested and continue to invest significant resources to develop and acquire technology related to our services that is capitalized to property and equipment or intangible assets and treated as an asset on our balance sheet. We may not launch this new technology, the launch of such technology may result in disruptions to our business operations or such technology might not meet our and our customers' expectations. Also, changes to any of our implementation strategies or the failure of this technology to meet our and our customers' expectations could result in the impairment of software-related assets, and our future operating results could be materially adversely affected if we are required to write down the carrying value of capitalized software development or other intangible assets.

We have experienced rapid growth. If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service and operational controls or adequately address competitive challenges.

We have experienced, and are continuing to experience, a period of rapid growth in our customers, headcount, and operations. In particular, we grew from approximately 270 employees as of December 31, 2011 to approximately 967 employees as of June 30, 2016, and have also significantly increased the number of customers and active users of Encompass. We anticipate that we will significantly expand our operations and headcount in the near term, and will continue to expand our customer base. This growth has placed, and future growth will place, a significant strain on our management, general and administrative resources, and operational infrastructure.

Our success will depend in part on our ability to manage this growth effectively and to scale our operations. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls, and our reporting systems and procedures. As we continue to grow, we also need to ensure that our policies and procedures evolve to reflect our current operations and are appropriately communicated to and observed by employees, and that we appropriately manage our corporate information assets, including confidential and proprietary information. Failure to effectively manage growth could result in difficulty or delays in deploying customers, declines in quality or customer satisfaction, increases in costs, difficulties in introducing new features or other operational difficulties, and any of these difficulties could adversely impact our business performance and results of operations.

Completing and integrating future acquisitions could disrupt our business, harm our financial condition, and operating results or dilute or adversely affect the price of our common stock.

Our success will depend in part on our ability to expand our solutions and services and to grow our business in response to changing technologies, customer demands and competitive pressures. In some circumstances, we may pursue growth through the acquisition of complementary businesses, solutions or technologies rather than through internal development. For example, in October 2015, we acquired substantially all the assets of Mortgage Returns, LLC, a company that provides on-demand CRM, and marketing automation solutions for the mortgage industry. In October 2014, we acquired substantially all the assets of Mortgage Resource Center, Inc., dba AllRegs, a provider of research and reference, education, documentation, and data analytics products relating to the mortgage industry. The identification of suitable acquisition candidates can be difficult, time-consuming, and costly, and we may not be able to complete acquisitions successfully. Moreover, if such acquisitions require us to seek additional debt or equity financing, we may not be able to obtain such financing on terms favorable to us or at all. Acquisitions and investments involve numerous risks which may have a negative impact on our results of operations, including:

- write-offs of acquired assets or investments;
- potential financial and credit risks associated with acquired customers;
- unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into existing technology;
- limitations to our ability to recognize revenue from acquired deferred revenue;

depreciation and amortization of amounts related to acquired intangible assets, fixed assets, and deferred compensation; and  
adverse tax consequences of any such acquisitions.

Even if we successfully complete an acquisition, we may not be able to assimilate and integrate effectively the acquired business, technologies, solutions, assets, personnel or operations, particularly if key personnel of an acquired company decide not

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to work for us. We may encounter difficulty in incorporating acquired technologies into our service and maintaining the quality standards that are consistent with our brand and reputation. In addition, we may issue debt or equity securities to complete an acquisition, which could dilute our stockholders' ownership and adversely affect the price of our common stock.

The residential mortgage industry is heavily regulated and changes in current legislation or new legislation could adversely affect our business.

The U.S. mortgage industry is heavily regulated. Federal and state governments and agencies could enact legislation or other policies that could negatively impact the business of our Encompass users and other Ellie Mae Network participants. Any changes to existing laws or regulations or adoption of new laws or regulations that increase restrictions on the residential mortgage industry may decrease residential mortgage volume or otherwise limit the ability of our Encompass users and Ellie Mae Network participants to operate their businesses, resulting in decreased usage of our solutions.

Changes in current legislation or new legislation may increase our costs by requiring us to update our products and services and if our products and services fail to address relevant laws and regulations our business could be adversely affected.

Changes to existing laws or regulations or adoption of new laws or regulations relating to the residential mortgage industry may require us to incur significant costs to update our products and services so that our customers remain compliant with such laws and regulation. Our Encompass Compliance Service analyzes mortgage loan data for compliance with consumer protection laws and institutionally mandated compliance policies and must continually be updated to incorporate changes to such laws and policies. The Dodd-Frank Act has caused and will continue to cause us to make similar updates to Encompass, Encompass Product and Pricing Service, Encompass Docs Solution, TQL, and the Ellie Mae Network to address, among other things, regulations that protect consumers against unfair, deceptive, and abusive practices by lenders. For example, additional tools and product updates were required to address the Ability-to-Repay/Qualified Mortgage and Federal and State High Cost rules that became effective in January 2014. In addition, we have updated certain products to comply with the TILA-RESPA Integrated Disclosure rule changes and the 2013 Loan Originator Rule under the Truth in Lending Act (Regulation Z) (TILA-RESPA Amendments) that became effective October 3, 2015. The final rule amending Regulation C to implement amendments to the Home Mortgage Disclosure Act made by section 1094 of the Dodd-Frank Act was published on October 15, 2015. It contained various effective compliance dates, starting with January 1, 2017 through May 30, 2020. The final "Qualified Residential Mortgage" rule which implements the risk retention requirements in the Dodd-Frank Act became effective on December 24, 2015. These additions and updates have caused us to incur significant expense, and future updates will likely similarly cause us to incur significant expense. In addition, if our products and services fail to address relevant laws and regulations, we could be subject to claims by our customers that we have breached our customer contracts as well as potential claims by borrowers or government agencies. Such claims could result in substantial costs and we could incur judgments or enter into settlements of claims that could have a material adverse effect on our business and operating results. Furthermore, if our products and services fail to address relevant laws and regulations this could result in negative publicity, damage to our reputation and brand, hinder our ability to enroll new customers and cause us to lose current customers, all of which could substantially harm our business and operating results.

Potential structural changes in the U.S. residential mortgage industry, in particular plans to diminish the role of Fannie Mae and Freddie Mac, could disrupt the residential mortgage market and have a material adverse effect on our business.

Fannie Mae and Freddie Mac play a very important role in providing liquidity, stability, and affordability in the current U.S. residential mortgage market. In particular, they participate in the secondary mortgage market by purchasing mortgage loans and mortgage-related securities for investment and by issuing guaranteed mortgage-related securities. In February 2011, the Obama administration delivered a report to Congress which proposed the winding down of Fannie Mae and Freddie Mac and shrinking the federal government's role in the housing market. This proposal includes the withdrawal of government guarantees currently available for certain residential loans and increasing the down payment requirements for borrowers, both of which could reduce mortgage lending volume. In

February 2012, the Federal Housing Finance Agency sent Congress a strategic plan to wind down Fannie Mae and Freddie Mac over the next several years. This proposal includes building a new infrastructure for the secondary mortgage market, continuing to shrink Fannie Mae's and Freddie Mac's operations by eliminating the direct funding of mortgages and shifting mortgage credit risk to private investors and maintaining foreclosure prevention activities and credit availability. In August 2012, the U.S. Department of the Treasury announced it would require Fannie Mae and Freddie Mac to reduce their investment portfolios more quickly, at an annual rate of 15% versus the previous rate of 10%. In June 2013, the U.S. Senate introduced a bill to wind down Fannie Mae and Freddie Mac over five years. This legislation would replace Fannie Mae and Freddie Mac with a new Federal Mortgage Insurance Corporation that would continue to guarantee mortgages, but only after private capital absorbs the first 10% of any losses. In July 2013, the U.S. House of Representatives also unveiled draft legislation to similarly wind down Fannie Mae and Freddie Mac over a five year period. In 2014, four Fannie Mae and Freddie Mac reform measures were active in Congress: the Senate's Johnson-Crapo and Corker-Warner bills, and the House's PATH Act and HOME Forward Act. In 2015, two Fannie Mae and Freddie Mac reform measures were active in Congress: the Partnership to Strengthen Homeownership Act of 2015 and the Mortgage Finance Act of 2015. The Federal Housing Finance Agency released in March 2015 its report on progress with the 2014 Strategic Plan for Fannie Mae and Freddie Mac Conservatorships. In April 2016, a new

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reform measure, the Housing Finance Restructuring Act of 2016 was introduced, which if enacted would recapitalize Fannie Mae and Freddie Mac. The effects of these proposals, the passage of similar bills into law or any significant structural change to the U.S. residential mortgage industry may cause significant disruption to the residential mortgage market. If we are unable to react effectively and quickly to changes in the residential mortgage industry, our business could be harmed.

We may be limited in the way in which we market our business or generate revenue by U.S. federal law prohibiting referral fees in real estate transactions, and if we are found to be in violation of such laws we would be subject to significant liability.

The Real Estate Settlement Procedures Act (“RESPA”) generally prohibits the payment or receipt of fees or any other thing of value for the referral of business related to a residential real estate settlement service and prohibits fee shares or splits or unearned fees in connection with the provision of such services. Encompass software and services and the Ellie Mae Network were designed with payment methods that are intended to comply with the restrictions under RESPA. Nonetheless, RESPA may restrict our ability to enter into marketing and distribution arrangements with third parties for existing or newly developed products and services, particularly to the extent that such arrangements may be characterized as involving payments for the referral of residential real estate settlement service business. Additionally, any amendments to RESPA, court opinions interpreting the provisions of RESPA, or changes in the manner that RESPA is interpreted by the regulatory agencies responsible for enforcing RESPA, that result in restrictions on our current payment methods, or any determination that our payment methods have been and currently are subject to the restrictions under RESPA, could have a material adverse effect on our business. If we were found to be in violation of RESPA rules, we would be exposed to significant potential liability that could have a material adverse effect on our reputation and business.

We depend on key and highly skilled personnel to operate our business, and if we are unable to retain our current or hire additional personnel, our ability to develop and successfully market our business could be harmed.

We believe our future success will depend in large part upon our ability to attract and retain highly skilled managerial, technical, finance, creative, and sales and marketing personnel. Moreover, we believe that our future success is highly dependent on the contributions of our named executive officers. All of our officers and other employees are at-will employees, which means they may terminate their employment relationship with us at any time, and their knowledge of our business and industry would be extremely difficult to replace. In addition, the loss of any key employees or the inability to attract or retain qualified personnel could delay the development and introduction of, and harm our ability to sell, our solutions and harm the market’s perception of us. Competition for qualified personnel is particularly intense in the San Francisco Bay Area, where our headquarters are located. Qualified individuals are in high demand, and we may incur significant costs to attract them. We may be unable to attract and retain suitably qualified individuals who are capable of meeting our growing sales, operational and managerial requirements, or may be required to pay increased compensation in order to do so. If we are unable to attract and retain the qualified personnel we need to succeed, our business will suffer.

Volatility or lack of performance in our stock price may also affect our ability to attract and retain our key employees. Our named executive officers are vested in a substantial amount of stock options and Performance Awards.

Employees may be more likely to leave us if the shares they own or the shares underlying their vested options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the vested options, or if the exercise prices of the options that they hold are significantly above the market price of our common stock. If we are unable to retain our named executive officers or other key employees, our business will be harmed.

We operate in a highly competitive market, which could make it difficult for us to attract and retain Encompass users and Ellie Mae Network participants.

The mortgage origination software market is highly competitive. There are many software providers that compete with us by offering loan origination software to mortgage originators, such as: Byte Software Inc., a subsidiary of CBCInnovis; Calyx Technology, Inc.; DH Corporation; Lending QB, Mortgage Builder Software, Inc., a subsidiary of Altisource Portfolio Solutions SA; Mortgage Cadence, which is owned by Accenture PLC; Wipro Gallagher Solutions, which is owned by Wipro, Ltd.; and LoanSphere Empower and LoanSphere LendingSpace, which are



owned by Black Knight Financial Services, LLC, a subsidiary of Fidelity National Financial, Inc. Some software providers, including Calyx Technology, Inc. and Black Knight Financial Services, LLC, also provide connectivity between their software users and lenders and service providers to make such services available to mortgage lenders. We also compete with compliance, document preparation service, and product eligibility and pricing service providers that are more established than us. There is vigorous competition among providers of these services and we may not succeed in convincing potential customers using other services to switch to ours. In addition, some of our competitors are consolidating which facilitates greater cross-selling of services, which could weaken our ability to differentiate our offering in the market. Some of our competitors also offer services on a per closed loan basis, which could adversely impact the effectiveness of our Success Based Pricing strategy for increasing the number of Encompass customers. If we are unsuccessful in competing effectively by providing attractive functionality, customer service or value, we could lose existing Encompass users to our competitors and our ability to attract new Encompass users could be harmed.

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There are many service providers that offer our Encompass users competing services, including borrower-facing websites, customer relationship management solutions, document preparation services, compliance services, product eligibility and pricing services, and electronic document management services. We may be unsuccessful in continuing to differentiate our Encompass service offerings to the extent necessary to effectively compete in some or all of these markets.

The Ellie Mae Network is only available to mortgage originators using Encompass. The principal alternative to the use of the Ellie Mae Network by Encompass users remains traditional methods of exchanging data and documents among mortgage industry participants by email, facsimile, phone, courier, and mail. In addition, mortgage originators may use standalone web browsers to go individually to each investor, lender or service provider's website, and then manually upload loan data or enter information into the website. Mortgage originators may continue to use these methods due to habit, personal business relationships or otherwise. The success of the Ellie Mae Network depends on our ability to achieve and offer access to both the critical mass of investors, lenders, and service providers necessary to attract and retain mortgage originators using Encompass on the Ellie Mae Network and the critical mass of active mortgage originators necessary to attract and retain investors, lenders, and service providers on our network.

Some of our actual and potential competitors have longer operating histories and significantly greater financial, technical, marketing, and other resources than we do and, as a result, these companies may be able to respond more quickly to changes in regulations, new technologies or customer demands, or devote greater resources to the development, promotion, and sale of their software and services than we can. In addition, we may face increased competition as a result of continuing industry consolidation. We expect the mortgage origination market to continue to attract new competitors and there can be no assurance that we will be able to compete successfully against current or future competitors or that competitive pressures we face will not materially adversely affect our business.

Failure to adapt to technological changes may render our technology obsolete or decrease the attractiveness of our solutions to our customers.

If new industry standards and practices emerge, or if competitors introduce new solutions embodying new services or technologies, Encompass and the Ellie Mae Network technology may become obsolete. Our future success will depend on our ability to:

- enhance our existing solutions;
- develop and potentially license new solutions and technologies that address the needs of our prospective customers;
- and
- respond to changes in industry standards and practices on a cost-effective and timely basis.

We must continue to enhance the features and functionality of Encompass, other Encompass services, and the Ellie Mae Network. The effective performance, reliability, and availability of Encompass, Encompass services, and the Ellie Mae Network infrastructure are critical to our reputation and our ability to attract and retain Encompass users and Ellie Mae Network participants. If we do not continue to make investments in product development and, as a result, or due to other reasons, fail to attract new and retain existing mortgage originators, lenders, investors, and service providers, we may lose existing Ellie Mae Network participants, which could significantly decrease the value of the Ellie Mae Network to all participants and materially adversely affect our business.

We are subject to the risks of current and future legal proceedings, which could have a material adverse effect on our business, financial condition, results of operations, and future prospects.

At any given time, we are a defendant in various legal proceedings and litigation matters arising in the ordinary course of business including commercial and employment disputes. We can give no assurance that the outcome of any such matter would not have a material adverse effect on our consolidated financial condition, results of operations or cash flows. We are unable to predict the ultimate outcome of these disputes or the actual impact of these matters on our profitability at this time, and any views we form as to the viability of these claims or the financial exposure in which they could result, could change from time to time as the matters proceed through their course, as facts are established, and various judicial determinations are made.

If we agree to settle these matters or judgments are secured against us, we may incur charges which may have a material and adverse impact on our business, financial conditions, results of operations, and future prospects.

Failure to adequately protect our intellectual property could harm our business.

The protection of our intellectual property rights, including our proprietary Encompass software and Ellie Mae Network technology, is crucial to the success of our business. We rely on a combination of patent, copyright, trademark and trade secret law, and contractual restrictions to protect our intellectual property. Our present and future patents may provide only limited protection for our technology and may not be sufficient to provide competitive advantage to us. Furthermore, we cannot guarantee any patents will be issued to us as a result of our patent applications. We also rely in part on confidentiality and invention assignment

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agreements with our employees, independent contractors, and consultants. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our Ellie Mae Network and Encompass features and functionality or obtain and use information that we consider proprietary. Enforcing our proprietary rights is difficult and may not always be effective.

We have registered “Ellie Mae,” “Encompass,” “Mortgage Returns,” and “AllRegs” and certain of our other trademarks as trademarks in the United States. Competitors may adopt service names similar to ours, thereby impeding our ability to build brand identity and possibly leading to customer confusion. In addition, there could be potential trade name or trademark infringement claims brought by owners of other registered trademarks or trademarks that incorporate variations of the terms Ellie Mae, Encompass or our other trademarks.

Litigation or proceedings before the U.S. Patent and Trademark Office or other governmental authorities and administrative bodies in the United States and abroad may be necessary in the future to enforce our intellectual property rights, protect our patent and copyright rights, trade secrets and domain names, and determine the validity and scope of the proprietary rights of others. Our efforts to enforce or protect our proprietary rights may be ineffective and could result in substantial costs and diversion of resources and could harm our business.

Assertions that we infringe third-party intellectual property rights could result in significant costs and substantially harm our business.

Other parties have asserted, and may in the future assert, that we have infringed their intellectual property rights. For example, in the third quarter of 2014, we settled a patent infringement lawsuit in which it was alleged that our Encompass system infringed certain patents. In addition, we generally agree to indemnify our customers against legal claims that our software products infringe intellectual property rights of third parties and, in the event of an infringement, to modify or replace the infringing product or, if those options are not reasonably possible, to refund the cost of the software, as pro-rated over a period of years. We cannot predict whether assertions of third-party intellectual property rights or claims arising from such assertions will substantially harm our business and operating results. If we are forced to defend against any infringement claims, whether they are with or without merit or are determined in our favor, we may face costly litigation and diversion of technical and management personnel.

Furthermore, an adverse outcome of a dispute may require us to: pay damages, potentially including treble damages and attorneys’ fees if the infringement were found to be willful; cease providing solutions that allegedly incorporate the intellectual property of others; expend additional development resources to redesign or re-engineer our solutions and products, if feasible; and enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies. We cannot be certain of the outcome of any litigation. Any royalty or licensing agreement, if required, may not be available to us on acceptable terms or at all. Our failure to obtain the necessary licenses or other rights could prevent the sale or distribution of some of our products and services and, therefore, could have a material adverse effect on our business.

Our internal information technology systems are critical to our business. System integration and implementation issues could disrupt our operations, which could have a material adverse impact on our business or results in significant deficiencies or material weaknesses in our internal controls.

We rely on the efficient and uninterrupted operation of complex information technology systems, including systems for customer billing, human resources, enterprise resource planning and customer relationship management. As our business has grown in size and complexity, the growth has placed, and will continue to place, significant demands on our internal information technology systems. To effectively manage this growth, we must commit significant financial and personnel resources to maintain and enhance existing systems and develop or acquire new systems to keep pace with continuing changes in our business and information processing technology as well as evolving industry, regulatory and accounting standards. If the information we rely upon to run our businesses is determined to be inaccurate or unreliable, if we fail to properly maintain or enhance our internal information technology systems, we could have operational disruptions, have customer disputes, lose our ability to produce timely and accurate financial reports, have significant deficiencies or material weaknesses in our internal controls, have increases in operating and administrative expenses, or suffer other adverse consequences.

If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements could be impaired, which could result in a loss of investor confidence in our financial reports, significant expenses to

remediate any internal control deficiencies, and ultimately have an adverse effect on the market price of our common stock.

As a publicly-traded company, we are subject to compliance with, among other regulations, Section 404 of the Sarbanes-Oxley Act of 2002, or SOX, which requires that we test our internal control over financial reporting and disclosure controls and procedures. Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. Our compliance with SOX requires that we incur substantial expense and expend significant management time on compliance-related issues. If we fail to achieve and maintain an effective internal control environment, we could suffer material misstatements in our financial statements and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial information. This could harm our operating results and lead to a decline in our stock price. Additionally, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to

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potential delisting from the New York Stock Exchange, regulatory investigations, civil or criminal sanctions, and class action litigation.

As a third-party technology service provider of mission-critical products and services to many financial institutions that are regulated by one or more member agencies of the Federal Financial Institutions Examination Council, or FFIEC, we are subject to an IT examination by the member agencies of the FFIEC. As a result, the FFIEC conducts recurring IT Examinations in order to identify existing or potential risks associated with our operations that could adversely affect the financial institutions to whom we provide products and services, evaluate our risk management systems, and controls and determine our compliance with applicable laws that affect the products and services we provide to financial institutions. In addition to examining areas such as our management of technology, data integrity, information confidentiality, and service availability, the reviews also assess our financial stability. In June 2014, the FDIC, a member agency of the FFIEC, completed its IT examination, and found that, while the services we provide to our client banks are satisfactory, several matters required further attention, some of which were repeat findings and recommendations from the FDIC's 2012 examination. Although management has developed a plan for addressing these matters, we cannot be assured that the plan will satisfy the FDIC or applicable law. A sufficiently unfavorable review from the FFIEC in the future could have a material adverse effect on our business and financial condition.

If one or more U.S. states or local jurisdictions successfully assert that we should have collected or in the future should collect additional sales or use taxes on our fees, we could be subject to additional liability with respect to past or future sales, and the results of our operations could be adversely affected.

We do not collect state and local sales and use taxes on all sales in all jurisdictions in which our customers are located, based on our belief that such taxes are not applicable. Sales and use tax laws and rates vary by jurisdiction and such laws are subject to interpretation. Jurisdictions in which we do not collect sales and use taxes may assert that such taxes are applicable, which could result in the assessment of such taxes, interest, and penalties, and we could be required to collect such taxes in the future. This additional sales and use tax liability could adversely affect the results of our operations.

Our business is subject to the risks of earthquakes, fires, floods, and other natural catastrophic events and to interruption by man-made problems such as terrorism.

Our systems and operations are vulnerable to damage or interruption from earthquakes, fires, floods, power losses, telecommunications failures, terrorist attacks, acts of war, and similar events. For example, a significant natural disaster, such as an earthquake, fire or flood, could have a material adverse impact on our business, operating results and financial condition, and our insurance coverage may be insufficient to compensate us for losses that may occur. Our corporate offices and one of the facilities we lease to house our computer and telecommunications equipment are located in the San Francisco Bay Area, a region known for seismic activity. In addition, acts of terrorism, which may be targeted at metropolitan areas with higher population density than rural areas, could cause disruptions in our or our customers' businesses or the economy as a whole. We may not have sufficient protection or recovery plans in certain circumstances, such as natural disasters affecting the San Francisco Bay Area, and our business interruption insurance may be insufficient to compensate us for losses that may occur.

Our stock price is volatile and purchasers of our common stock could incur substantial losses.

The trading price of our common stock may be subject to wide fluctuations in response to various factors, some of which are beyond our control. In addition to the factors discussed in this "Risk Factors" section and elsewhere in our filings with the SEC, these factors include:

- our operating performance and the operating performance of similar companies;
- the overall performance of the equity markets;
- the number of shares our common stock publicly owned and available for trading;
- threatened or actual litigation;
- changes in laws or regulations relating to our solutions;
- any major change in our board of directors or management;
- publication of research reports about us or our industry or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- large volumes of sales of our shares of common stock by existing stockholders; and

general political and economic conditions.

In addition, the stock market in general has experienced extreme price and volume fluctuations. Securities class action litigation has often been instituted against companies following periods of volatility in the overall market and in the market price of a company's securities. This litigation, if instituted against us, could result in very substantial costs, divert our management's attention and resources and harm our business.

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Our stock repurchase program may be suspended or terminated at any time, which may result in a decrease in the trading price of our common stock.

Our board of directors previously approved a stock repurchase program under which we are authorized to repurchase up to \$75.0 million of our common stock over a 36-month period ending in May 2017, \$43.5 million of which remains available as of June 30, 2016. Such stock repurchases may be limited, suspended, or terminated at any time without prior notice. There can be no assurance that we will repurchase additional shares of our common stock under our stock repurchase program or that any future repurchases will have a positive impact on the trading price of our common stock or earnings per share. Important factors that could cause us to limit, suspend or terminate our stock repurchase program include, among others, unfavorable market conditions, the trading price of our common stock, the nature of other investment or strategic opportunities presented to us from time to time, the rate of dilution of our equity compensation programs, the availability of adequate funds, and our ability to make appropriate, timely, and beneficial decisions as to when, how, and whether to purchase shares under the stock repurchase program. If we limit, suspend or terminate our stock repurchase program, our stock price may be negatively affected.

If securities or industry analysts discontinue publishing research or publish inaccurate or unfavorable research about our business, our stock price could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our stock or publish inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, demand for our stock could decrease, which might cause our stock price to decline.

Certain provisions in our charter documents and Delaware law could discourage takeover attempts and lead to management entrenchment.

Our amended and restated certificate of incorporation and amended and restated bylaws contain provisions that could have the effect of delaying or preventing changes in control or changes in 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 determine to issue shares of preferred stock and to determine the price and other terms of those shares, including preferences and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;
- the requirement that a special meeting of stockholders may be called only by the chairman of the board of directors, the chief executive officer, the president 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 acquirer from conducting a solicitation of proxies to elect the acquirer'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.





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

The table below sets forth the information with respect to purchases made by or on behalf of the Company or any “affiliated purchaser” (as the term is defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended) of our common stock during the three months ended June 30, 2016:

## ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced or Programs	Approximate Dollar Value or Shares that May Yet be Purchased Under the Plans or Programs (1)
April 1, 2016 to April 30, 2016	—	\$	—	\$43,469,986
May 1, 2016 to May 31, 2016	—	\$	—	\$43,469,986
June 1, 2016 to June 30, 2016	—	\$	—	\$43,469,986

(1) In May 2014, our board of directors approved a stock repurchase program under which we are authorized to repurchase up to \$75.0 million of our common stock, which expires in May 2017. Shares under the program are retired upon the repurchase. Amount remaining to be purchased are exclusive of commissions.

## ITEM 3—DEFAULTS UPON SENIOR SECURITIES

Not applicable.

## ITEM 4—MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 5—OTHER INFORMATION

Not applicable.

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ITEM 6—EXHIBITS

Exhibit Number	Description of Document
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10.1(1)# Non-Employee Director Equity Compensation Policy.

10.2(2)# Executive Incentive Plan

31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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32.1*	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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32.2*	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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101.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

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(1) Previously filed as exhibit 10.1 to the Registrant’s Current Report on Form 8-K, filed on June 6, 2016, and incorporated herein by reference.

(2) Previously filed as Appendix A to the Registrant’s Definitive Proxy Materials on Form DEF14A, filed on April 7, 2016, and incorporated herein by reference.

Exhibits 32.1 and 32.2 are being furnished and shall not be deemed to be “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall such exhibits be deemed to be incorporated by reference in any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as otherwise specifically stated in such filing.

#Indicated management contract or compensatory plan.

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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.

ELLIE MAE, INC.

Date: July 29, 2016 By: /s/ Edgar A. Luce

Edgar A. Luce

Executive Vice President, Finance and Administration and

Chief Financial Officer

(Principal Financial and Accounting Officer and duly authorized signatory)