

**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, 2019

OR

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

For the transition period from _____ to _____
Commission File Number 000-24435

MICROSTRATEGY INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

51-0323571

(I.R.S. Employer
Identification Number)

1850 Towers Crescent Plaza, Tysons Corner, VA
(Address of Principal Executive Offices)

22182

(Zip Code)

(703) 848-8600

(Registrant's telephone number, including area code)

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

| Title of Each Class | Trading Symbol | Name of Each Exchange on which Registered |
|---|----------------|---|
| Class A common stock, par value \$0.001 per share | MSTR | The Nasdaq Global Select Market |

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

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

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

| | | | |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |
| | | Emerging growth company | <input type="checkbox"/> |

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

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

As of July 16, 2019, the registrant had 8,204,395 and 2,035,184 shares of class A common stock and class B common stock outstanding, respectively.

MICROSTRATEGY INCORPORATED

FORM 10-Q

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

MICROSTRATEGY INCORPORATED
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

| | June 30, 2019 <small>(unaudited)</small> | December 31, 2018 |
|--|--|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 261,497 | \$ 109,924 |
| Restricted cash | 1,039 | 862 |
| Short-term investments | 313,349 | 466,186 |
| Accounts receivable, net | 129,144 | 171,359 |
| Prepaid expenses and other current assets | 22,259 | 30,068 |
| Total current assets | 727,288 | 778,399 |
| Property and equipment, net | 54,285 | 51,919 |
| Right-of-use assets | 89,631 | 0 |
| Deposits and other assets | 7,981 | 8,134 |
| Deferred tax assets, net | 20,535 | 17,316 |
| Total assets | \$ 899,720 | \$ 855,768 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable, accrued expenses, and operating lease liabilities | \$ 32,300 | \$ 33,684 |
| Accrued compensation and employee benefits | 41,561 | 48,045 |
| Deferred revenue and advance payments | 176,786 | 176,540 |
| Total current liabilities | 250,647 | 258,269 |
| Deferred revenue and advance payments | 4,175 | 6,469 |
| Operating lease liabilities | 108,183 | 0 |
| Other long-term liabilities | 33,990 | 61,262 |
| Deferred tax liabilities | 36 | 37 |
| Total liabilities | 397,031 | 326,037 |
| Commitments and Contingencies | | |
| Stockholders' Equity | | |
| Preferred stock undesignated, \$0.001 par value; 5,000 shares authorized; no shares issued or outstanding | 0 | 0 |
| Class A common stock, \$0.001 par value; 330,000 shares authorized; 15,853 shares issued and 8,205 shares outstanding, and 15,837 shares issued and 8,552 shares outstanding, respectively | 16 | 16 |
| Class B convertible common stock, \$0.001 par value; 165,000 shares authorized; 2,035 shares issued and outstanding, and 2,035 shares issued and outstanding, respectively | 2 | 2 |
| Additional paid-in capital | 584,764 | 576,957 |
| Treasury stock, at cost; 7,648 shares and 7,285 shares, respectively | (634,405) | (586,161) |
| Accumulated other comprehensive loss | (9,310) | (10,217) |
| Retained earnings | 561,622 | 549,134 |
| Total stockholders' equity | 502,689 | 529,731 |
| Total liabilities and stockholders' equity | \$ 899,720 | \$ 855,768 |

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

| | Three Months Ended June 30, | |
|--|--------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) |
| Revenues: | | |
| Product licenses | \$ 20,121 | \$ 19,292 |
| Subscription services | 7,104 | 7,584 |
| Total product licenses and subscription services | 27,225 | 26,876 |
| Product support | 72,978 | 73,676 |
| Other services | 17,534 | 20,050 |
| Total revenues | 117,737 | 120,602 |
| Cost of revenues: | | |
| Product licenses | 552 | 1,667 |
| Subscription services | 3,489 | 3,445 |
| Total product licenses and subscription services | 4,041 | 5,112 |
| Product support | 7,721 | 4,810 |
| Other services | 13,588 | 15,118 |
| Total cost of revenues | 25,350 | 25,040 |
| Gross profit | 92,387 | 95,562 |
| Operating expenses: | | |
| Sales and marketing | 48,273 | 50,978 |
| Research and development | 27,764 | 25,082 |
| General and administrative | 21,180 | 21,299 |
| Total operating expenses | 97,217 | 97,359 |
| Loss from operations | (4,830) | (1,797) |
| Interest income, net | 3,013 | 3,223 |
| Other income, net | 29,431 | 4,461 |
| Income before income taxes | 27,614 | 5,887 |
| Provision for income taxes | 7,220 | 1,059 |
| Net income | 20,394 | 4,828 |
| Basic earnings per share (1) | \$ 1.99 | \$ 0.42 |
| Weighted average shares outstanding used in computing basic earnings per share | 10,240 | 11,459 |
| Diluted earnings per share (1) | \$ 1.98 | \$ 0.42 |
| Weighted average shares outstanding used in computing diluted earnings per share | 10,310 | 11,493 |

(1) Basic and fully diluted earnings per share for class A and class B common stock are the same.

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

| | Six Months Ended June 30, | |
|--|------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) |
| Revenues: | | |
| Product licenses | \$ 38,412 | \$ 36,593 |
| Subscription services | 14,248 | 15,246 |
| Total product licenses and subscription services | 52,660 | 51,839 |
| Product support | 144,428 | 148,091 |
| Other services | 36,015 | 43,639 |
| Total revenues | 233,103 | 243,569 |
| Cost of revenues: | | |
| Product licenses | 1,071 | 3,878 |
| Subscription services | 7,087 | 6,694 |
| Total product licenses and subscription services | 8,158 | 10,572 |
| Product support | 14,788 | 9,606 |
| Other services | 28,577 | 30,047 |
| Total cost of revenues | 51,523 | 50,225 |
| Gross profit | 181,580 | 193,344 |
| Operating expenses: | | |
| Sales and marketing | 97,033 | 102,313 |
| Research and development | 55,979 | 48,642 |
| General and administrative | 43,784 | 43,471 |
| Total operating expenses | 196,796 | 194,426 |
| Loss from operations | (15,216) | (1,082) |
| Interest income, net | 5,579 | 5,257 |
| Other income, net | 28,835 | 2,867 |
| Income before income taxes | 19,198 | 7,042 |
| Provision for income taxes | 6,710 | 541 |
| Net income | 12,488 | 6,501 |
| Basic earnings per share (1) | \$ 1.21 | \$ 0.57 |
| Weighted average shares outstanding used in computing basic earnings per share | 10,283 | 11,453 |
| Diluted earnings per share (1) | \$ 1.21 | \$ 0.57 |
| Weighted average shares outstanding used in computing diluted earnings per share | 10,350 | 11,488 |

(1) Basic and fully diluted earnings per share for class A and class B common stock are the same.

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)

| | Three Months Ended | |
|---|--------------------|-------------|
| | June 30, | |
| | 2019 | 2018 |
| | (unaudited) | (unaudited) |
| Net income | \$ 20,394 | \$ 4,828 |
| Other comprehensive income (loss), net of applicable taxes: | | |
| Foreign currency translation adjustment | 422 | (3,892) |
| Unrealized gain on short-term investments | 232 | 0 |
| Total other comprehensive income (loss) | 654 | (3,892) |
| Comprehensive income | \$ 21,048 | \$ 936 |

| | Six Months Ended | |
|---|------------------|-------------|
| | June 30, | |
| | 2019 | 2018 |
| | (unaudited) | (unaudited) |
| Net income | \$ 12,488 | \$ 6,501 |
| Other comprehensive income (loss), net of applicable taxes: | | |
| Foreign currency translation adjustment | 260 | (2,452) |
| Unrealized gain on short-term investments | 647 | 0 |
| Total other comprehensive income (loss) | 907 | (2,452) |
| Comprehensive income | \$ 13,395 | \$ 4,049 |

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, unaudited)

| | Total | Class A | | Class B | | Additional Paid-in Capital | Treasury Stock | | Accumulated Other Comprehensive Income (Loss) | Retained Earnings |
|--|-------------------|---------------|--------------|-----------------------------|-------------|----------------------------------|----------------|---------------------|--|----------------------|
| | | Common Stock | | Convertible Common Stock | | | Shares | Amount | | |
| | | Shares | Amount | Shares | Amount | | | | | |
| Balance at January 1, 2018 | <u>\$ 605,726</u> | <u>15,817</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 559,918</u> | <u>(6,405)</u> | <u>\$ (475,184)</u> | <u>\$ (5,659)</u> | <u>\$ 528,633</u> |
| Net income | 1,673 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,673 |
| Other comprehensive income | 1,440 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,440 | 0 |
| Share-based compensation expense | 4,743 | 0 | 0 | 0 | 0 | 4,743 | 0 | 0 | 0 | 0 |
| Balance at March 31, 2018 | <u>\$ 613,582</u> | <u>15,817</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 564,661</u> | <u>(6,405)</u> | <u>\$ (475,184)</u> | <u>\$ (4,219)</u> | <u>\$ 528,306</u> |
| Net income | 4,828 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 4,828 |
| Other comprehensive loss | (3,892) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (3,892) | 0 |
| Issuance of class A common stock under stock option plans | 2,471 | 20 | 0 | 0 | 0 | 2,471 | 0 | 0 | 0 | 0 |
| Share-based compensation expense | 3,370 | 0 | 0 | 0 | 0 | 3,370 | 0 | 0 | 0 | 0 |
| Balance at June 30, 2018 | <u>\$ 620,359</u> | <u>15,837</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 570,502</u> | <u>(6,405)</u> | <u>\$ (475,184)</u> | <u>\$ (8,111)</u> | <u>\$ 533,134</u> |
| Net income | 12,699 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 12,699 |
| Other comprehensive loss | (607) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (607) | 0 |
| Share-based compensation expense | 2,972 | 0 | 0 | 0 | 0 | 2,972 | 0 | 0 | 0 | 0 |
| Balance at September 30, 2018 | <u>\$ 635,423</u> | <u>15,837</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 573,474</u> | <u>(6,405)</u> | <u>\$ (475,184)</u> | <u>\$ (8,718)</u> | <u>\$ 545,833</u> |
| Net income | 3,301 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 3,301 |
| Other comprehensive loss | (1,499) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (1,499) | 0 |
| Purchases of treasury stock | (110,977) | 0 | 0 | 0 | 0 | 0 | (880) | (110,977) | 0 | 0 |
| Share-based compensation expense | 3,483 | 0 | 0 | 0 | 0 | 3,483 | 0 | 0 | 0 | 0 |
| Balance at December 31, 2018 | <u>\$ 529,731</u> | <u>15,837</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 576,957</u> | <u>(7,285)</u> | <u>\$ (586,161)</u> | <u>\$ (10,217)</u> | <u>\$ 549,134</u> |
| Net loss | (7,906) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (7,906) |
| Other comprehensive income | 253 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 253 | 0 |
| Issuance of class A common stock under stock option plans | 1,507 | 13 | 0 | 0 | 0 | 1,507 | 0 | 0 | 0 | 0 |
| Purchases of treasury stock | (48,244) | 0 | 0 | 0 | 0 | 0 | (363) | (48,244) | 0 | 0 |
| Share-based compensation expense | 2,965 | 0 | 0 | 0 | 0 | 2,965 | 0 | 0 | 0 | 0 |
| Balance at March 31, 2019 | <u>\$ 478,306</u> | <u>15,850</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 581,429</u> | <u>(7,648)</u> | <u>\$ (634,405)</u> | <u>\$ (9,964)</u> | <u>\$ 541,228</u> |
| Net income | 20,394 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 20,394 |
| Other comprehensive income | 654 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 654 | 0 |
| Issuance of class A common stock under stock option plans | 329 | 3 | 0 | 0 | 0 | 329 | 0 | 0 | 0 | 0 |
| Share-based compensation expense | 3,006 | 0 | 0 | 0 | 0 | 3,006 | 0 | 0 | 0 | 0 |
| Balance at June 30, 2019 | <u>\$ 502,689</u> | <u>15,853</u> | <u>\$ 16</u> | <u>2,035</u> | <u>\$ 2</u> | <u>\$ 584,764</u> | <u>(7,648)</u> | <u>\$ (634,405)</u> | <u>\$ (9,310)</u> | <u>\$ 561,622</u> |

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | Six Months Ended June 30, | |
|---|------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) |
| Operating activities: | | |
| Net income | \$ 12,488 | \$ 6,501 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 7,687 | 3,870 |
| Write-offs and sales allowances | 796 | 948 |
| Net realized loss on short-term investments | 41 | 0 |
| Deferred taxes | (3,219) | (5,758) |
| Share-based compensation expense | 6,053 | 8,121 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 5,985 | 5,044 |
| Prepaid expenses and other current assets | 7,089 | 453 |
| Deposits and other assets | 96 | (344) |
| Accounts payable and accrued expenses | (8,396) | (7,775) |
| Accrued compensation and employee benefits | (8,082) | (3,015) |
| Deferred revenue and advance payments | 33,489 | 10,502 |
| Operating lease liabilities | (4,316) | 0 |
| Other long-term liabilities | (509) | 4,780 |
| Net cash provided by operating activities | 49,202 | 23,327 |
| Investing activities: | | |
| Proceeds from redemption of short-term investments | 369,603 | 245,680 |
| Purchases of property and equipment | (8,432) | (2,644) |
| Purchases of short-term investments | (212,248) | (596,376) |
| Net cash provided by (used in) investing activities | 148,923 | (353,340) |
| Financing activities: | | |
| Proceeds from sale of class A common stock under exercise of employee stock options | 1,836 | 2,471 |
| Purchases of treasury stock | (48,244) | 0 |
| Payments on capital lease obligations and other financing arrangements prior to the adoption of ASU 2016-02 | 0 | (9) |
| Net cash (used in) provided by financing activities | (46,408) | 2,462 |
| Effect of foreign exchange rate changes on cash, cash equivalents, and restricted cash | 33 | (2,240) |
| Net increase (decrease) in cash, cash equivalents, and restricted cash | 151,750 | (329,791) |
| Cash, cash equivalents and restricted cash, beginning of period | 110,786 | 421,182 |
| Cash, cash equivalents and restricted cash, end of period | \$ 262,536 | \$ 91,391 |

The accompanying notes are an integral part of these Consolidated Financial Statements.

MICROSTRATEGY INCORPORATED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

(1) Summary of Significant Accounting Policies

(a) Basis of Presentation

The accompanying Consolidated Financial Statements of MicroStrategy Incorporated (“MicroStrategy” or the “Company”) are unaudited. In the opinion of management, all adjustments necessary for a fair statement of financial position and results of operations have been included. All such adjustments are of a normal recurring nature, unless otherwise disclosed. Interim results are not necessarily indicative of results for a full year.

As discussed in Note 2, Recent Accounting Standards, to the Consolidated Financial Statements, the Company adopted Accounting Standards Update No. 2016-02, *Leases (Topic 842)*, and its subsequent amendments (“ASU 2016-02”) effective January 1, 2019. Comparative prior period Consolidated Financial Statements have not been restated and are not directly comparable to the current period Consolidated Financial Statements.

The Consolidated Financial Statements and Notes to Consolidated Financial Statements are presented as required by the United States Securities and Exchange Commission (“SEC”) and do not contain certain information included in the Company’s annual financial statements and notes. These financial statements should be read in conjunction with the Company’s audited financial statements and the notes thereto filed with the SEC in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018. There have been no significant changes in the Company’s accounting policies since December 31, 2018, except as discussed below with respect to the Company’s adoption of ASU 2016-02.

The accompanying Consolidated Financial Statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. The Company is not aware of any subsequent event that would require recognition or disclosure.

(b) Leases

ASU 2016-02 defines a lease as a contract, or part of a contract, that conveys the right to both (i) obtain economic benefits from and (ii) direct the use of an identified asset for a period of time in exchange for consideration. Under ASU 2016-02, the Company evaluates its contracts to determine if they contain a lease and classifies any lease components identified as an operating or finance lease. For each lease component, the Company recognizes a right-of-use (“ROU”) asset and a lease liability. ROU assets and lease liabilities are presented separately for operating and finance leases; however, the Company currently has no material finance leases. The Company’s operating leases are primarily related to office space in the United States and foreign locations.

In a contract that contains a lease, a component is an item or activity that transfers a good or service to the lessee. Such contracts may be comprised of lease components, non-lease components, and elements that are not components. Each lease component represents a lessee’s right to use an underlying asset in the contract if the lessee can benefit from the right of use of the asset either on its own or together with other readily available resources and if the right of use is neither highly dependent nor highly interrelated with other rights of use. Non-lease components include items such as common area maintenance and utilities provided by the lessor. The Company has elected the practical expedient provided in ASU 2016-02 to not separate lease components from non-lease components for office space, which is the Company’s only material underlying asset class. For each lease within this asset class, the non-lease components and related lease components are accounted for as a single lease component. Items or activities that do not transfer goods or services to the lessee, such as administrative tasks to set up the contract and reimbursement or payment of lessor costs, are not components of the contract and therefore no contract consideration is allocated to such items or activities.

Consideration in the contract is comprised of any fixed payments and variable payments that depend on an index or rate. Payments in the Company’s operating lease arrangements are typically comprised of base office rent and parking fees. Costs related to the Company’s non-lease components, as described above, are generally variable and do not depend on an index or rate and are therefore excluded from the contract consideration allocated to the lease components. The Company’s operating lease arrangements generally do not contain any payments related to items or activities that are not components.

MICROSTRATEGY INCORPORATED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

Operating lease liabilities are initially and subsequently measured at the present value of unpaid lease payments, discounted at the discount rate of the lease. Operating lease ROU assets are initially measured as the sum of the initial lease liability, any initial direct costs incurred, and any prepaid lease payments, less any lease incentives received. The ROU asset is amortized over the term of the lease. A single lease expense is recorded within operating expenses in the consolidated statements of operations on a straight-line basis over the lease term. Variable lease payments that are not included in the measurement of the lease liability are recognized in the period when the obligations for those payments are incurred. In the Company's lease agreements, these variable payments typically include certain taxes, utilities, and maintenance costs, and other fees.

The Company uses its incremental borrowing rate as the discount rate for all of its leases, as the rate implicit in the lease is not readily determinable in any of its lease contracts. In determining the incremental borrowing rate, the Company considers its credit risk profile, the currency of the contract, the economic environment in which the lease exists, and the term of the lease.

The Company does not recognize lease liabilities or ROU assets for any short-term leases with a non-cancellable lease term of 12 months or less. Instead the lease payments for these short-term leases are expensed on a straight-line basis over the lease term, and any variable payments are recognized in the period when the obligations for those payments are incurred. The Company believes that, using this methodology, expense reasonably reflects the Company's short-term lease commitments.

(2) Recent Accounting Standards

Lease accounting

The Company adopted ASU 2016-02 effective as of January 1, 2019 and elected the transition option to apply the new lease requirements as of the adoption date without restating comparative periods presented in its financial statements. Additionally, the Company elected the package of practical expedients described in ASU 2016-02, which includes not reassessing the following: (i) lease classification of existing leases, (ii) whether expired or existing contracts contain leases, and (iii) initial direct costs for existing leases.

Upon adoption of ASU 2016-02, the Company recognized additional ROU assets of \$88.8 million, additional total lease liabilities of \$116.9 million, reductions in total deferred rent of \$28.5 million, and reductions in prepaid expenses of \$0.4 million in its 2019 beginning balances. All adjustments relate to the Company's operating leases; the Company does not have any material leases that are classified as finance leases. There was no cumulative effect adjustment to the Company's 2019 beginning retained earnings balance, as the Company did not have material unamortized initial direct costs. Beginning in 2019, the Company presents the amortization of its operating ROU assets and the change in its operating lease liabilities within the operating activities section of its consolidated statements of cash flows. The adoption of ASU 2016-02 did not have a material impact on the Company's consolidated results of operations.

Cloud computing arrangements

In August 2018, the FASB issued Accounting Standards Update No. 2018-15, *Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract* ("ASU 2018-15"). ASU 2018-15 requires customers in a hosting arrangement that is a service contract to follow existing internal-use software guidance to determine which implementation costs to capitalize and which costs to expense. Under this model, customers would need to determine the nature of the implementation costs and the project stage in which they are incurred to determine which costs to capitalize or expense. Customers would be required to amortize the capitalized implementation costs over the term of the hosting arrangement, which might extend beyond the noncancelable period if there are options to extend or terminate. ASU 2018-15 specifies the financial statement presentation of capitalized implementation costs and related amortization in addition to required disclosures for material capitalized implementation costs related to hosting arrangements that are service contracts. The standard is effective for interim and annual periods beginning January 1, 2020. Early adoption is permitted. Entities can choose to adopt this guidance prospectively to eligible costs incurred on or after the date the guidance is first applied, or to adopt the guidance retrospectively. The Company is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

MICROSTRATEGY INCORPORATED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

Credit losses

In June 2016, the FASB issued Accounting Standards Update No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which requires the application of a current expected credit loss (“CECL”) impairment model to financial assets measured at amortized cost (including trade accounts receivable), net investments in leases, and certain off-balance-sheet credit exposures. Under the CECL model, lifetime expected credit losses on such financial assets are measured and recognized at each reporting date based on historical, current, and forecasted information. ASU 2016-13 also changes the impairment accounting for available-for-sale debt securities, requiring credit losses to be recorded through an allowance for credit losses. The standard is effective for interim and annual periods beginning January 1, 2020. Early adoption is permitted. A modified retrospective adoption method is required, with a cumulative-effect adjustment to the opening retained earnings balance in the period of adoption. The Company is currently evaluating the impact of this guidance on its consolidated financial position, results of operations, cash flows, and disclosures.

(3) Short-term Investments

The Company periodically invests a portion of its excess cash in short-term investment instruments. All of the Company’s short-term investments are in U.S. Treasury securities and all short-term investments have stated maturity dates between three months and one year from the purchase date. All short-term investments are included within “Short-term investments” on the accompanying Consolidated Balance Sheets. The fair value of the Company’s short-term investments is determined based on quoted market prices in active markets for identical securities (Level 1 inputs). As of June 30, 2019 and December 31, 2018, all short-term investments were classified as available-for-sale and reported at fair value.

The amortized cost and fair value of available-for-sale investments at June 30, 2019 were \$313.1 million and \$313.3 million, respectively. The amortized cost and fair value of available-for-sale investments at December 31, 2018 were \$466.6 million and \$466.2 million, respectively. The total gross unrecognized holding losses accumulated in other comprehensive loss were not material as of June 30, 2019 and December 31, 2018. The total gross unrecognized holding gains accumulated in other comprehensive loss were not material as of June 30, 2019 and December 31, 2018. No other-than-temporary impairments related to these investments have been recognized as of June 30, 2019 and December 31, 2018.

(4) Contract Balances

The Company invoices its customers in accordance with billing schedules established in each contract. The Company’s rights to consideration from customers are presented separately in the Company’s Consolidated Balance Sheets depending on whether those rights are conditional or unconditional.

The Company presents unconditional rights to consideration from customers within “Accounts receivable, net” in its Consolidated Balance Sheets. All of the Company’s contracts are generally non-cancellable and/or non-refundable and therefore an unconditional right generally exists when the customer is billed or amounts are billable per the contract.

Accounts receivable (in thousands) consisted of the following, as of:

| | June 30, 2019 | December 31, 2018 |
|---------------------------------------|-------------------|----------------------|
| Billed and billable | \$ 133,443 | \$ 176,848 |
| Less: allowance for doubtful accounts | (4,299) | (5,489) |
| Accounts receivable, net | <u>\$ 129,144</u> | <u>\$ 171,359</u> |

The Company maintains an allowance for doubtful accounts, which represents its best estimate of probable losses and sales allowances. The Company evaluates the adequacy of its allowance for doubtful accounts by considering the aging of receivable balances, historical experience, and other currently available information. The Company’s write-offs and sales allowances were not material for the three months ended June 30, 2019. For the six months ended June 30, 2019, the Company’s write-offs and sales allowances totaled \$0.8 million. For the three and six months ended June 30, 2018, the Company’s write-offs and sales allowances totaled \$0.8 million and \$0.9 million, respectively.

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In contrast, rights to consideration that are subject to a condition other than the passage of time are considered contract assets and presented within “Prepaid expenses and other current assets” in the Consolidated Balance Sheets since the rights to consideration are expected to become unconditional and transfer to accounts receivable within one year. Contract assets generally consist of accrued sales and usage-based royalty revenue. In these arrangements, consideration is not billed or billable until the royalty reporting is received, generally in the subsequent quarter, at which time the contract asset transfers to accounts receivable and a true-up adjustment is recorded to revenue. During the three and six months ended June 30, 2019 and 2018, there were no significant impairments to the Company’s contract assets, nor were there any significant changes in the timing of the Company’s contract assets being reclassified to accounts receivable. Contract assets included in “Prepaid expenses and other current assets” in the Consolidated Balance Sheets consisted of \$0.8 million and \$0.8 million in accrued sales and usage-based royalty revenue as of June 30, 2019 and December 31, 2018, respectively.

Contract liabilities are amounts received or due from customers in advance of the Company transferring the products or services to the customer. Revenue is subsequently recognized in the period(s) in which control of the products or services is transferred to the customer. The Company’s contract liabilities are presented as either current or non-current “Deferred revenue and advance payments” in the Consolidated Balance Sheets, depending on whether the products or services are expected to be transferred to the customer within the next year.

Deferred revenue and advance payments (in thousands) from customers consisted of the following, as of:

| | June 30, 2019 | December 31, 2018 |
|---|-------------------|----------------------|
| Current: | | |
| Deferred product licenses revenue | \$ 633 | \$ 1,768 |
| Deferred subscription services revenue | 15,393 | 13,508 |
| Deferred product support revenue | 152,866 | 152,501 |
| Deferred other services revenue | 7,894 | 8,763 |
| Total current deferred revenue and advance payments | <u>\$ 176,786</u> | <u>\$ 176,540</u> |
| Non-current: | | |
| Deferred product licenses revenue | \$ 405 | \$ 542 |
| Deferred subscription services revenue | 116 | 2,384 |
| Deferred product support revenue | 3,083 | 3,091 |
| Deferred other services revenue | 571 | 452 |
| Total non-current deferred revenue and advance payments | <u>\$ 4,175</u> | <u>\$ 6,469</u> |

During the three and six months ended June 30, 2019, the Company recognized revenues of \$51.0 million and \$118.0 million, respectively, from amounts included in the total deferred revenue and advance payments balances at the beginning of 2019. During the three and six months ended June 30, 2018, the Company recognized revenues of \$56.8 million and \$131.3 million, respectively, from amounts included in the total deferred revenue and advance payments balances at the beginning of 2018. For the three and six months ended June 30, 2019 and 2018, there were no significant changes in the timing of revenue recognition on the Company’s deferred balances.

As of June 30, 2019, the Company had an aggregate transaction price of \$181.0 million allocated to unsatisfied performance obligations related to product support, subscription services, other services, and product licenses contracts. The Company expects to recognize \$176.8 million within the next 12 months and \$4.2 million thereafter.

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(5) Leases

The Company leases office space in the United States and foreign locations under operating lease agreements. Office space is the Company's only material underlying asset class under operating lease agreements. The Company has no material finance leases.

Under the Company's office space lease agreements, fixed payments and variable payments that depend on an index or rate are typically comprised of base rent and parking fees. Additionally, under these agreements the Company is generally responsible for certain variable payments that typically include certain taxes, utilities and maintenance costs, and other fees. These variable lease payments are generally based on the Company's occupation or usage percentages and are subject to adjustments by the lessor.

As of June 30, 2019, the Company's ROU asset and total lease liability balances were comprised of \$73.2 million and \$100.2 million, respectively, for leases in the United States and \$16.4 million and \$17.2 million, respectively, for foreign leases. The Company's most significant lease is for its corporate headquarters, in which it leases approximately 214,000 square feet of office space at a location in Northern Virginia. The ROU asset and total lease liability balances related to the Company's corporate headquarters lease were \$68.6 million and \$95.6 million, respectively, as of June 30, 2019. The lease agreement for the Company's corporate headquarters location is set to expire in December 2030, with an option for the Company to extend the term for an additional five or 10 consecutive years. The Company is currently not reasonably certain it will exercise this renewal option and therefore has not included the renewal option in the lease term. Several of the Company's remaining leases also contain options for renewal or options to terminate all or a portion of the leased space. The Company continually assesses the likelihood of exercising these options and recognizes an option as part of its ROU assets and lease liabilities if and when it is reasonably certain that it will exercise the option.

The following table presents the Company's total lease cost and other lease details for the three and six months ended June 30, 2019 (in thousands, except years and discount rate):

| | June 30, 2019 | |
|--|--------------------|------------------|
| | Three Months Ended | Six Months Ended |
| <i>Lease cost:</i> | | |
| Operating lease cost | \$ 3,838 | \$ 7,607 |
| Short-term lease cost | 401 | 1,215 |
| Variable lease cost | 284 | 595 |
| Total lease cost | \$ 4,523 | \$ 9,417 |
| <i>Other information:</i> | | |
| Cash paid for amounts included in the measurement of operating lease liabilities | \$ 4,028 | \$ 7,889 |
| ROU assets obtained in exchange for new operating lease liabilities | \$ 3,999 | \$ 5,016 |
| Weighted-average remaining lease term in years – operating leases | 10.4 | 10.4 |
| Weighted-average discount rate – operating leases | 6.0% | 6.0% |

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The following table presents the maturities of the Company's operating lease liabilities as of June 30, 2019 (in thousands):

| For the period ended June 30, | |
|---|-------------------|
| 2020 | \$ 15,953 |
| 2021 | 16,039 |
| 2022 | 15,288 |
| 2023 | 15,482 |
| 2024 | 14,104 |
| Thereafter | 82,518 |
| Total lease payments | <u>159,384</u> |
| Less: imputed interest | <u>(41,937)</u> |
| Total | <u>\$ 117,447</u> |
| Reported as: | |
| Current operating lease liabilities | \$ 9,264 |
| Non-current operating lease liabilities | 108,183 |
| Total | <u>\$ 117,447</u> |

The following table shows future minimum payments under noncancellable operating leases and purchase agreements with initial terms of greater than one year, based on the expected due dates of the various installments as of December 31, 2018 (in thousands), as previously reported in the Company's Annual Report on Form 10-K for the year ended December 31, 2018, prior to the adoption of ASU 2016-02:

| Year | Operating Leases Amount |
|-------------|------------------------------------|
| 2019 | \$ 27,768 |
| 2020 | 25,583 |
| 2021 | 18,573 |
| 2022 | 15,694 |
| 2023 | 15,607 |
| Thereafter | 92,347 |
| | <u>\$ 195,572</u> |

(6) Commitments and Contingencies

(a) Commitments

From time to time, the Company enters into certain types of contracts that require it to indemnify parties against third-party claims. These contracts primarily relate to agreements under which the Company assumes indemnity obligations for intellectual property infringement, as well as other obligations from time to time depending on arrangements negotiated with customers and other third parties. The conditions of these obligations vary. Thus, the overall maximum amount of the Company's indemnification obligations cannot be reasonably estimated. Historically, the Company has not been obligated to make significant payments for these obligations and does not currently expect to incur any material obligations in the future. Accordingly, the Company has not recorded an indemnification liability on its balance sheets as of June 30, 2019 or December 31, 2018.

See Note 5, Leases, to the Consolidated Financial Statements for information regarding the Company's commitments that are related to lease agreements.

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As a result of the U.S. government-enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”), the Company recorded a final tax expense of \$37.2 million related to the mandatory deemed repatriation transition tax (“Transition Tax”), of which \$8.3 million was paid in 2018. At June 30, 2019, \$28.9 million of the Transition Tax was unpaid, of which \$28.0 million was included in “Other long-term liabilities” and \$0.9 million was included in “Accounts payable, accrued expenses, and operating lease liabilities” in the Company’s Consolidated Balance Sheets. See Note 8, Income Taxes, to the Consolidated Financial Statements for further information.

(b) Contingencies

Following an internal review, the Company believes that its Brazilian subsidiary failed or likely failed to comply with local procurement regulations in conducting business with certain Brazilian government entities. While the Company believes that it is probable that the resolution of this matter will result in a loss, the amount or range of loss is not reasonably estimable at this time. Given the stage of the matter, no assurance can be given that the outcome will not result in a material impact on the Company’s earnings and financial results for the period in which any such liability is accrued. However, the Company believes that the outcome of this matter will not have a material effect on the Company’s financial position.

The Company is also involved in various legal proceedings arising in the normal course of business. Although the outcomes of these legal proceedings are inherently difficult to predict, management does not expect the resolution of these legal proceedings to have a material adverse effect on the Company’s financial position, results of operations, or cash flows.

The Company has contingent liabilities that, in management’s judgment, are not probable of assertion. If such unasserted contingent liabilities were to be asserted, or become probable of assertion, the Company may be required to record significant expenses and liabilities in the period in which these liabilities are asserted or become probable of assertion.

(7) Treasury Stock

The Board of Directors previously authorized the Company’s repurchase of up to an aggregate of \$800.0 million of its class A common stock from time to time on the open market through April 29, 2023 (the “Share Repurchase Program”), although the program may be suspended or discontinued by the Company at any time. The timing and amount of any shares repurchased will be determined by the Company’s management based on its evaluation of market conditions and other factors. The Share Repurchase Program may be funded using the Company’s working capital, as well as proceeds from any other funding arrangements that the Company may enter into in the future. During the three months ended June 30, 2019, the Company did not repurchase any shares of its class A common stock pursuant to the Share Repurchase Program. During the six months ended June 30, 2019, the Company repurchased an aggregate of 362,148 shares of its class A common stock at an average price per share of \$133.21 and an aggregate cost of \$48.2 million pursuant to the Share Repurchase Program. As of June 30, 2019, the Company had repurchased an aggregate of 5,069,762 shares of its class A common stock at an average price per share of \$99.51 and an aggregate cost of \$504.5 million pursuant to the Share Repurchase Program. The average price per share and aggregate cost amounts disclosed above include broker commissions. During the three and six months ended June 30, 2018, the Company did not repurchase any shares of its class A common stock pursuant to the Share Repurchase Program.

(8) Income Taxes

The Company and its subsidiaries conduct business in the United States and various foreign countries and are subject to taxation in numerous domestic and foreign jurisdictions. As a result of its business activities, the Company files tax returns that are subject to examination by various U.S. federal, state, and local, and foreign tax authorities. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or foreign income tax examination by tax authorities for years before 2014. However, due to the Company’s use of state net operating loss (“NOL”) and federal tax credit carryovers in the United States, U.S. tax authorities may attempt to reduce or fully offset the amount of state NOL or federal tax credit carryovers from tax years ended 2007 and forward that the Company used in later tax years. The Company’s major foreign tax jurisdictions and tax years that remain subject to potential examination are Italy for tax years 2013 and forward, Poland for tax years 2014 and forward, Spain for tax years 2015 and forward, and Germany and the United Kingdom for tax years 2016 and forward. To date there have been no material audit assessments related to audits in any of the applicable foreign jurisdictions.

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As of June 30, 2019, the Company had unrecognized tax benefits of \$5.1 million, which are recorded in “Other long-term liabilities” in the Company’s Consolidated Balance Sheets. If recognized, \$4.5 million of these unrecognized tax benefits would impact the Company’s effective tax rate. The Company recognizes estimated accrued interest related to unrecognized income tax benefits in the provision for income tax accounts. Penalties relating to income taxes, if incurred, would also be recognized as a component of the Company’s provision for income taxes. Over the next 12 months, the amount of the Company’s liability for unrecognized tax benefits is expected to decrease by \$2.2 million due to expiration of the applicable statute of limitations. As of June 30, 2019, the amount of cumulative accrued interest expense on unrecognized income tax benefits was approximately \$0.8 million.

The following table summarizes the Company’s deferred tax assets, net of deferred tax liabilities and valuation allowance (in thousands), as of:

| | June 30, 2019 | December 31, 2018 |
|--|--------------------------|------------------------------|
| Deferred tax assets, net of deferred tax liabilities | \$ 22,006 | \$ 18,786 |
| Valuation allowance | (1,507) | (1,507) |
| Deferred tax assets, net of deferred tax liabilities and valuation allowance | <u>\$ 20,499</u> | <u>\$ 17,279</u> |

The valuation allowance as of June 30, 2019 and December 31, 2018 related to certain foreign tax credit carryforwards that, in the Company’s present estimation, more likely than not will not be realized.

The Company has estimated its annual effective tax rate for the full fiscal year 2019 and applied that rate to its income before income taxes in determining its provision for income taxes for the six months ended June 30, 2019. The Company also records discrete items in each respective period as appropriate. The estimated effective tax rate is subject to fluctuation based on the level and mix of earnings and losses by tax jurisdiction, foreign tax rate differentials, and the relative impact of permanent book to tax differences (e.g., non-deductible expenses). Each quarter, a cumulative adjustment is recorded for any fluctuations in the estimated annual effective tax rate as compared to the prior quarter. As a result of these factors, and due to potential changes in the Company’s period-to-period results, fluctuations in the Company’s effective tax rate and respective tax provisions or benefits may occur.

For the six months ended June 30, 2019, the Company recorded a provision for income taxes of \$6.7 million that resulted in an effective tax rate of 35.0%, as compared to a provision for income taxes of \$0.5 million that resulted in an effective tax rate of 7.7% for the six months ended June 30, 2018. The change in the effective tax rate in 2019 is mainly due to certain discrete items and the change in the expected proportion of U.S. versus foreign income. The most significant discrete item was a tax provision of \$8.1 million on the \$29.8 million gain from the sale of the Voice.com domain name in May 2019, as discussed in Note 12, Sale of Domain Name, to the Consolidated Financial Statements.

In the United States, the Tax Act reduced the U.S. corporate tax rate from 35% to 21%, effective January 1, 2018. Additionally, the Tax Act requires certain Global Intangible Low Taxed Income (“GILTI”) earned by controlled foreign corporations (“CFCs”) to be included in the gross income of the CFCs’ U.S. shareholder. The Company has elected the “period cost method” and treats taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred. The Tax Act allows a U.S. corporation a deduction equal to a certain percentage of its foreign-derived intangible income (“FDII”). The Company estimated the impact of the GILTI tax and FDII deduction in determining its 2019 annual effective tax rate that is reflected in its provision for income taxes for the six months ended June 30, 2019.

The Tax Act also imposed a Transition Tax on previously untaxed accumulated and current earnings and profits of certain foreign subsidiaries of the Company. The Company recorded a final tax expense of \$37.2 million related to the Transition Tax, of which \$8.3 million was paid in 2018. As of June 30, 2019, \$28.9 million of the Transition Tax was unpaid, of which \$28.0 million was recorded in “Other long-term liabilities” and \$0.9 million was recorded in “Accounts payable, accrued expenses, and operating lease liabilities” in the Company’s Consolidated Balance Sheets. The Transition Tax will be paid in full by 2025.

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The Company earns a significant amount of its revenues outside the United States and, as of December 31, 2018, the Company's accumulated foreign earnings and profits were \$397.4 million. As of June 30, 2019 and December 31, 2018, the amount of cash and cash equivalents and short-term investments held by the Company's U.S. entities was \$294.0 million and \$173.6 million, respectively, and by the Company's non-U.S. entities was \$280.8 million and \$402.5 million, respectively. As of June 30, 2019, the Company intends to indefinitely reinvest \$197.4 million of its undistributed foreign earnings. This amount takes into consideration repatriations the Company made during the three months ended June 30, 2019. After taking into account the Transition Tax described above, the Company expects such repatriation generated only an immaterial U.S. tax expense related to U.S. state income taxes.

In the United Kingdom, recently enacted legislation related to offshore receipts in respect of intangible property imposes a 20% tax on payments made by multinational companies that hold intangible property in low tax jurisdictions where the income derived from such intangible property results from sales within the United Kingdom. Based on currently available information, the Company believes that this tax does not apply to its operations in the United Kingdom.

In determining the Company's provision for income taxes, net deferred tax assets, liabilities, and valuation allowances, management is required to make judgments and estimates related to projections of domestic and foreign profitability, the timing and extent of the utilization of NOL carryforwards, applicable tax rates, transfer pricing methods, and prudent and feasible tax planning strategies. As a multinational company, the Company is required to calculate and provide for estimated income tax liabilities for each of the tax jurisdictions in which it operates. This process involves estimating current tax obligations and exposures in each jurisdiction, as well as making judgments regarding the future recoverability of deferred tax assets. Changes in the estimated level of annual pre-tax income, changes in tax laws, particularly changes related to the utilization of NOLs in various jurisdictions, and changes resulting from tax audits can all affect the overall effective income tax rate, which, in turn, impacts the overall level of income tax expense or benefit and net income.

Judgments and estimates related to the Company's projections and assumptions are inherently uncertain. Therefore, actual results could differ materially from projections. Currently, the Company expects to use its deferred tax assets, subject to Internal Revenue Code limitations, within the carryforward periods. Valuation allowances have been established where the Company has concluded that it is more likely than not that such deferred tax assets are not realizable. If the Company is unable to regain or increase profitability from its normal business operations in future periods, it may be required to increase the valuation allowance against the deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred.

(9) Share-based Compensation

The Company's 2013 Stock Incentive Plan (as amended, the "2013 Equity Plan") authorizes the issuance of various types of share-based awards to the Company's employees, officers, directors, and other eligible participants. As of June 30, 2019, a total of 2,300,000 shares of the Company's class A common stock were authorized for issuance under the 2013 Equity Plan. As of June 30, 2019, there were 572,500 shares of class A common stock reserved and available for future issuance under the 2013 Equity Plan.

Stock option awards

During the three months ended June 30, 2019, stock options to purchase an aggregate of 22,500 shares of class A common stock were granted pursuant to the 2013 Equity Plan. As of June 30, 2019, there were options to purchase 1,458,733 shares of class A common stock outstanding under the 2013 Equity Plan.

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The following table summarizes the Company's stock option activity (in thousands, except per share data and years) for the three months ended June 30, 2019:

| | Stock Options Outstanding | | | |
|--------------------------------------|----------------------------------|--|--|--|
| | Shares | Weighted Average Exercise Price Per Share | Aggregate Intrinsic Value | Weighted Average Remaining Contractual Term (Years) |
| Balance as of April 1, 2019 | 1,460 | \$ 137.38 | | |
| Granted | 23 | \$ 133.62 | | |
| Exercised | (3) | \$ 131.53 | \$ 38 | |
| Forfeited/Expired | (21) | \$ 156.14 | | |
| Balance as of June 30, 2019 | <u>1,459</u> | <u>\$ 137.05</u> | | |
| Exercisable as of June 30, 2019 | 842 | \$ 136.98 | \$ 12,676 | 5.8 |
| Expected to vest as of June 30, 2019 | 617 | \$ 137.15 | \$ 6,823 | 8.7 |
| Total | <u>1,459</u> | <u>\$ 137.05</u> | <u>\$ 19,499</u> | 7.0 |

Stock options outstanding as of June 30, 2019 are comprised of the following range of exercise prices per share (in thousands, except per share data and years):

| Range of Exercise Prices per Share | Stock Options Outstanding at June 30, 2019 | | |
|---|---|--|--|
| | Shares | Weighted Average Exercise Price Per Share | Weighted Average Remaining Contractual Term (Years) |
| \$119.02 - \$140.00 | 1,161 | \$ 126.51 | 7.1 |
| \$140.01 - \$160.00 | 30 | \$ 145.41 | 9.7 |
| \$160.01 - \$180.00 | 113 | \$ 167.75 | 5.7 |
| \$180.01 - \$201.25 | 155 | \$ 191.97 | 7.2 |
| Total | <u>1,459</u> | <u>\$ 137.05</u> | 7.0 |

An aggregate of 40,625 stock options with an aggregate fair value of \$2.4 million vested during the three months ended June 30, 2019. The weighted average grant date fair value of stock option awards using the Black-Scholes pricing model was \$48.84 and \$50.76 for each share subject to a stock option granted during the three months ended June 30, 2019 and 2018, respectively, based on the following assumptions:

| | Three months ended June 30, | |
|-----------------------------------|--|---------------|
| | 2019 | 2018 |
| Expected term of options in years | 6.3 | 6.3 |
| Expected volatility | 33.2% - 33.3% | 34.6% - 34.9% |
| Risk-free interest rate | 2.0% - 2.3% | 2.7% - 2.8% |
| Expected dividend yield | 0.0% | 0.0% |

For the three and six months ended June 30, 2019, the Company recognized approximately \$3.0 million and \$6.0 million, respectively, in share-based compensation expense from stock options granted under the 2013 Equity Plan. For the three and six months ended June 30, 2018, the Company recognized approximately \$3.4 million and \$8.1 million, respectively, in share-based compensation expense from stock options granted under the 2013 Equity Plan. As of June 30, 2019, there was approximately \$28.4 million of total unrecognized share-based compensation expense related to unvested stock options. The Company expects to recognize this remaining share-based compensation expense over a weighted average vesting period of approximately 2.7 years. Included in this amount is approximately \$4.2 million of total unrecognized share-based compensation expense related to unvested stock options that have been or will be forfeited in connection with the departures of two executive officers in July 2019. Prior to their departures, such amount was expected to be recognized over a remaining service period of approximately 2.8 years.

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Other stock-based awards

During the three months ended June 30, 2019, the Company did not grant any “other stock-based awards” under the 2013 Equity Plan. For each of the three and six months ended June 30, 2019 and 2018, the Company did not recognize a material amount in share-based compensation expense from other stock-based awards. As of June 30, 2019, there was approximately \$0.4 million of total unrecognized share-based compensation expense related to other stock-based awards. The Company expects to recognize this remaining share-based compensation expense over a weighted average vesting period of approximately 2.9 years, subject to additional fair value adjustments through the earlier of settlement or expiration.

(10) Common Equity and Earnings per Share

The Company has two classes of common stock: class A common stock and class B common stock. Holders of class A common stock generally have the same rights, including rights to dividends, as holders of class B common stock, except that holders of class A common stock have one vote per share while holders of class B common stock have 10 votes per share. Each share of class B common stock is convertible at any time, at the option of the holder, into one share of class A common stock. As such, basic and fully diluted earnings per share for class A common stock and for class B common stock are the same. The Company has never declared or paid any cash dividends on either class A or class B common stock. As of June 30, 2019 and December 31, 2018, there were no shares of preferred stock issued or outstanding.

Potential shares of common stock are included in the diluted earnings per share calculation when dilutive. Potential shares of common stock, consisting of common stock issuable upon exercise of outstanding stock options, are calculated using the treasury stock method.

For the three and six months ended June 30, 2019, stock options issued under the 2013 Equity Plan to purchase a weighted average of approximately 947,000 and 955,000 shares of class A common stock, respectively, were excluded from the diluted earnings per share calculation because their impact would have been anti-dilutive. For the three and six months ended June 30, 2018, stock options issued under the 2013 Equity Plan to purchase a weighted average of approximately 938,000 and 830,000 shares of class A common stock, respectively, were excluded from the diluted earnings per share calculation because their impact would have been anti-dilutive.

(11) Segment Information

The Company manages its business in one reportable operating segment. The Company’s one reportable operating segment is engaged in the design, development, marketing, and sales of its software platform through licensing arrangements and cloud-based subscriptions and related services. The following table presents total revenues, gross profit, and long-lived assets, excluding long-term deferred tax assets, (in thousands) according to geographic region:

| Geographic regions: | Domestic | EMEA | Other Regions | Consolidated |
|---|-----------------|-------------|----------------------|---------------------|
| Three months ended June 30, 2019 | | | | |
| Total revenues | \$ 67,338 | \$ 38,957 | \$ 11,442 | \$ 117,737 |
| Gross profit | \$ 52,994 | \$ 30,679 | \$ 8,714 | \$ 92,387 |
| Three months ended June 30, 2018 | | | | |
| Total revenues | \$ 68,025 | \$ 38,008 | \$ 14,569 | \$ 120,602 |
| Gross profit | \$ 53,239 | \$ 30,246 | \$ 12,077 | \$ 95,562 |
| Six months ended June 30, 2019 | | | | |
| Total revenues | \$ 132,219 | \$ 76,632 | \$ 24,252 | \$ 233,103 |
| Gross profit | \$ 102,528 | \$ 60,207 | \$ 18,845 | \$ 181,580 |
| Six months ended June 30, 2018 | | | | |
| Total revenues | \$ 140,104 | \$ 76,206 | \$ 27,259 | \$ 243,569 |
| Gross profit | \$ 110,290 | \$ 60,761 | \$ 22,293 | \$ 193,344 |
| As of June 30, 2019 | | | | |
| Long-lived assets | \$ 123,696 | \$ 14,371 | \$ 13,830 | \$ 151,897 |
| As of December 31, 2018 | | | | |
| Long-lived assets | \$ 49,611 | \$ 5,931 | \$ 4,511 | \$ 60,053 |

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(unaudited)

The domestic region consists of the United States and Canada. The EMEA region includes operations in Europe, the Middle East, and Africa. The other regions include all other foreign countries, generally comprising Latin America and the Asia Pacific region. For the three and six months ended June 30, 2019 and 2018, no individual foreign country accounted for 10% or more of total consolidated revenues.

For the three and six months ended June 30, 2019 and 2018, no individual customer accounted for 10% or more of total consolidated revenues.

As of June 30, 2019 and December 31, 2018, no individual foreign country accounted for 10% or more of total consolidated assets.

(12) Sale of Domain Name

On May 30, 2019, the Company completed the sale of its Voice.com domain name for consideration of \$ 30.0 million in cash (the “Domain Name Sale”). As of the date of the Domain Name Sale, the Company had no unamortized costs associated with the Voice.com domain name asset. The Company did not incur any material costs related to the Domain Name Sale. The Domain Name Sale resulted in a gain of \$29.8 million, which was recorded as “Other income, net” in the Consolidated Statements of Operations. The Company also recorded a discrete \$8.1 million tax provision related to the Domain Name Sale.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING INFORMATION

This Quarterly Report on Form 10-Q (this "Quarterly Report") contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). For this purpose, any statements contained herein that are not statements of historical fact, including without limitation, certain statements regarding industry prospects and our results of operations or financial position, may be deemed to be forward-looking statements. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects," and similar expressions are intended to identify forward-looking statements. The important factors discussed under "Part II. Item 1A. Risk Factors," among others, could cause actual results to differ materially from those indicated by forward-looking statements made herein and presented elsewhere by management from time to time. Such forward-looking statements represent management's current expectations and are inherently uncertain. Investors are warned that actual results may differ from management's expectations.

Overview

MicroStrategy® is a leading worldwide provider of enterprise analytics and mobility software. We are one of the largest independent, publicly-traded analytics vendors as measured by annual revenue. Our customers include leading companies from a wide range of industries, including retail, consulting, technology, manufacturing, finance, banking, insurance, healthcare, education, and telecommunications, as well as the public sector.

The analytics market is highly competitive and subject to rapidly-changing technology paradigms. Our success depends on our ability to compete with and differentiate our products from those offered by other analytics vendors, including large software vendors that provide one or more products that directly compete with our products and other vendors that offer competing self-service analytics tools. We believe a key differentiator of MicroStrategy is our offering of a single, comprehensive enterprise platform that uniquely features Federated Analytics, Transformational Mobility, and HyperIntelligence™, which can be deployed on-premises or on multiple private and public cloud platforms.

We continue to innovate our platform by focusing on making it more usable, powerful, scalable, flexible, and secure. In the three months ended June 30, 2019, these innovations included:

- a new HyperIntelligence for Office product that enriches emails within the Microsoft Outlook application for Windows PC and Mac by enabling users to find relevant, contextual insights with zero-clicks within their emails and Outlook-based workflows through HyperIntelligence cards;
- HyperIntelligence for Mobile, a native mobile app now available for iOS and Android that brings contextual insights to more users on the go;
- powerful enhancements to the connectors that promote Federated Analytics – MicroStrategy for Tableau, MicroStrategy for Power BI, and MicroStrategy for Qlik – to support greater data volumes by connecting to MicroStrategy's Enterprise Semantic Graph™;
- advanced administration and automation features within the MicroStrategy Cloud™ platform that make it easier to deploy and manage applications via Amazon Web Services ("AWS") and Microsoft Azure; and
- over 400 customer-reported enhancements and fixes that make our platform faster and more stable and secure.

The following table sets forth certain operating highlights (in thousands) for the three and six months ended June 30, 2019 and 2018:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-------------------|------------------------------|-------------------|
| | 2019 | 2018 | 2019 | 2018 |
| Revenues | | | | |
| Product licenses | \$ 20,121 | \$ 19,292 | \$ 38,412 | \$ 36,593 |
| Subscription services | 7,104 | 7,584 | 14,248 | 15,246 |
| Total product licenses and subscription services | 27,225 | 26,876 | 52,660 | 51,839 |
| Product support | 72,978 | 73,676 | 144,428 | 148,091 |
| Other services | 17,534 | 20,050 | 36,015 | 43,639 |
| Total revenues | 117,737 | 120,602 | 233,103 | 243,569 |
| Cost of revenues | | | | |
| Product licenses | 552 | 1,667 | 1,071 | 3,878 |
| Subscription services | 3,489 | 3,445 | 7,087 | 6,694 |
| Total product licenses and subscription services | 4,041 | 5,112 | 8,158 | 10,572 |
| Product support | 7,721 | 4,810 | 14,788 | 9,606 |
| Other services | 13,588 | 15,118 | 28,577 | 30,047 |
| Total cost of revenues | 25,350 | 25,040 | 51,523 | 50,225 |
| Gross profit | 92,387 | 95,562 | 181,580 | 193,344 |
| Operating expenses | | | | |
| Sales and marketing | 48,273 | 50,978 | 97,033 | 102,313 |
| Research and development | 27,764 | 25,082 | 55,979 | 48,642 |
| General and administrative | 21,180 | 21,299 | 43,784 | 43,471 |
| Total operating expenses | 97,217 | 97,359 | 196,796 | 194,426 |
| Loss from operations | \$ (4,830) | \$ (1,797) | \$ (15,216) | \$ (1,082) |

On May 30, 2019, we completed the Domain Name Sale, resulting in a one-time gain of \$29.8 million and an associated discrete tax provision of \$8.1 million.

As of June 30, 2019, we had a total of 2,477 employees, of whom 1,146 were based in the United States and 1,331 were based internationally. Of our 2,477 total employees, 637 were engaged in sales and marketing, 764 in research and development, 740 in subscription services, product support, consulting, and education, and 336 in finance, administration, and corporate operations. The following table summarizes employee headcount as of the dates indicated:

| | June 30, 2019 | December 31, 2018 | June 30, 2018 |
|----------------------------|------------------|----------------------|------------------|
| Subscription services | 62 | 56 | 54 |
| Product support | 234 | 202 | 184 |
| Consulting | 404 | 452 | 443 |
| Education | 40 | 47 | 39 |
| Sales and marketing | 637 | 707 | 687 |
| Research and development | 764 | 716 | 651 |
| General and administrative | 336 | 348 | 322 |
| Total headcount | 2,477 | 2,528 | 2,380 |

As discussed in Note 9, Share-based Compensation, to the Consolidated Financial Statements, we have outstanding stock options to purchase shares of our class A common stock and certain other stock-based awards under our 2013 Equity Plan. Share-based compensation expense (in thousands) from these awards was recognized in the following operating expense line items in our Consolidated Statements of Operations for the periods indicated:

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|----------|------------------|----------|
| | June 30, | | June 30, | |
| | 2019 | 2018 | 2019 | 2018 |
| Cost of product support revenues | \$ 81 | \$ 81 | \$ 162 | \$ 128 |
| Cost of consulting revenues | 46 | 17 | 98 | 26 |
| Cost of education revenues | (28) | 49 | 20 | 77 |
| Sales and marketing | 1,055 | 658 | 1,958 | 1,722 |
| Research and development | 585 | 789 | 1,264 | 1,424 |
| General and administrative | 1,297 | 1,784 | 2,551 | 4,744 |
| Total share-based compensation expense | \$ 3,036 | \$ 3,378 | \$ 6,053 | \$ 8,121 |

As of June 30, 2019, we estimated that approximately \$28.8 million of additional share-based compensation expense for awards granted under the 2013 Equity Plan will be recognized over a remaining weighted average period of 2.7 years. Included in this amount is approximately \$4.2 million of total unrecognized share-based compensation expense related to unvested stock options that have been or will be forfeited in connection with the departures of two executive officers in July 2019. Prior to their departures, such amount was expected to be recognized over a remaining service period of approximately 2.8 years.

We base our internal operating expense forecasts on expected revenue trends and strategic objectives. Many of our expenses, such as office leases and certain personnel costs, are relatively fixed. Accordingly, any shortfall in revenue may cause significant variation in our operating results. We therefore believe that quarter-to-quarter comparisons of our operating results may not be a good indication of our future performance.

Non-GAAP Financial Measures

We are providing supplemental financial measures for (i) (loss) income from operations that excludes the impact of our share-based compensation arrangements, (ii) net (loss) income and diluted (loss) earnings per share that exclude the impact from the Domain Name Sale, and (iii) certain revenues, cost of revenues, and operating expenses that exclude foreign currency exchange rate fluctuations. These supplemental financial measures are not measurements of financial performance under generally accepted accounting principles in the United States (“GAAP”) and, as a result, these supplemental financial measures may not be comparable to similarly titled measures of other companies. Management uses these non-GAAP financial measures internally to help understand, manage, and evaluate our business performance and to help make operating decisions.

We believe that these non-GAAP financial measures are also useful to investors and analysts in comparing our performance across reporting periods on a consistent basis. The first supplemental financial measure excludes a significant non-cash expense that we believe is not reflective of our general business performance, and for which the accounting requires significant management judgment and the resulting share-based compensation expense could vary significantly in comparison to other companies. The second category of supplemental financial measures excludes the impact from the Domain Name Sale, which is outside of our normal business operations. The third category of supplemental financial measures excludes changes resulting from fluctuations in foreign currency exchange rates so that results may be compared to the same period in the prior year on a “constant currency” basis. We believe the use of these non-GAAP financial measures can also facilitate comparison of our operating results to those of our competitors.

Non-GAAP financial measures are subject to material limitations as they are not in accordance with, or a substitute for, measurements prepared in accordance with GAAP. For example, we expect that share-based compensation expense, which is excluded from the first non-GAAP financial measure, will continue to be a significant recurring expense over the coming years and is an important part of the compensation provided to certain employees, officers, and directors. Our non-GAAP financial measures are not meant to be considered in isolation and should be read only in conjunction with our Consolidated Financial Statements, which have been prepared in accordance with GAAP. We rely primarily on such Consolidated Financial Statements to understand, manage, and evaluate our business performance and use the non-GAAP financial measures only supplementally.

The following is a reconciliation of our non-GAAP (loss) income from operations excluding the impact of our share-based compensation arrangements to its most directly comparable GAAP measure (in thousands) for the periods indicated:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-----------------|------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Reconciliation of non-GAAP (loss) income from operations: | | | | |
| Loss from operations | \$ (4,830) | \$ (1,797) | \$ (15,216) | \$ (1,082) |
| Share-based compensation expense | 3,036 | 3,378 | 6,053 | 8,121 |
| Non-GAAP (loss) income from operations | <u>\$ (1,794)</u> | <u>\$ 1,581</u> | <u>\$ (9,163)</u> | <u>\$ 7,039</u> |

The following are reconciliations of our non-GAAP net (loss) income and non-GAAP diluted (loss) earnings per share, in each case excluding the impact of the Domain Name Sale, to their most directly comparable GAAP measures (in thousands, except per share data) for the periods indicated:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-----------------|------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Reconciliation of non-GAAP net (loss) income: | | | | |
| Net income | \$ 20,394 | \$ 4,828 | \$ 12,488 | \$ 6,501 |
| Gain from Domain Name Sale, net of tax | (21,778) | 0 | (21,778) | 0 |
| Non-GAAP net (loss) income | <u>\$ (1,384)</u> | <u>\$ 4,828</u> | <u>\$ (9,290)</u> | <u>\$ 6,501</u> |
| Reconciliation of non-GAAP diluted (loss) earnings per share: | | | | |
| Diluted earnings per share | \$ 1.98 | \$ 0.42 | \$ 1.21 | \$ 0.57 |
| Gain from Domain Name Sale, net of tax (per diluted share) | (2.12) | 0.00 | (2.11) | 0.00 |
| Non-GAAP diluted (loss) earnings per share | <u>\$ (0.14)</u> | <u>\$ 0.42</u> | <u>\$ (0.90)</u> | <u>\$ 0.57</u> |

The following are reconciliations of our non-GAAP “constant currency” revenues, cost of revenues, and operating expenses to their most directly comparable GAAP measures (in thousands) for the periods indicated. We adopted Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, and its subsequent amendments (“ASU 2014-09”) effective January 1, 2018. Where applicable, prior year information within the following reconciliations has been adjusted to reflect the full retrospective adoption of ASU 2014-09.

**Three Months Ended
June 30,**

| | <u>GAAP</u> | <u>Foreign Currency Exchange Rate Impact (1)</u> | <u>Non-GAAP Constant Currency (2)</u> | <u>GAAP</u> | <u>GAAP % Change</u> | <u>Non-GAAP Constant Currency % Change (3)</u> |
|-------------------------------------|-------------|--|---|-------------|--------------------------|--|
| | <u>2019</u> | <u>2019</u> | <u>2019</u> | <u>2018</u> | <u>2019</u> | <u>2019</u> |
| Product licenses revenues | \$ 20,121 | \$ (616) | \$ 20,737 | \$ 19,292 | 4.3% | 7.5% |
| Subscription services revenues | 7,104 | (93) | 7,197 | 7,584 | -6.3% | -5.1% |
| Product support revenues | 72,978 | (2,091) | 75,069 | 73,676 | -0.9% | 1.9% |
| Other services revenues | 17,534 | (603) | 18,137 | 20,050 | -12.5% | -9.5% |
| Cost of product support revenues | 7,721 | (163) | 7,884 | 4,810 | 60.5% | 63.9% |
| Cost of other services revenues | 13,588 | (499) | 14,087 | 15,118 | -10.1% | -6.8% |
| Sales and marketing expenses | 48,273 | (1,382) | 49,655 | 50,978 | -5.3% | -2.6% |
| Research and development expenses | 27,764 | (409) | 28,173 | 25,082 | 10.7% | 12.3% |
| General and administrative expenses | 21,180 | (309) | 21,489 | 21,299 | -0.6% | 0.9% |

| | <u>2018</u> | <u>2018</u> | <u>2018</u> | <u>2017</u> | <u>2018</u> | <u>2018</u> |
|-------------------------------------|-------------|-------------|-------------|---------------|-------------|-------------|
| | | | | (as adjusted) | | |
| Product licenses revenues | \$ 19,292 | \$ 200 | \$ 19,092 | \$ 17,728 | 8.8% | 7.7% |
| Subscription services revenues | 7,584 | 99 | 7,485 | 8,346 | -9.1% | -10.3% |
| Product support revenues | 73,676 | 1,194 | 72,482 | 70,766 | 4.1% | 2.4% |
| Other services revenues | 20,050 | 399 | 19,651 | 22,380 | -10.4% | -12.2% |
| Cost of product support revenues | 4,810 | 59 | 4,751 | 4,542 | 5.9% | 4.6% |
| Cost of other services revenues | 15,118 | 358 | 14,760 | 14,686 | 2.9% | 0.5% |
| Sales and marketing expenses | 50,978 | 628 | 50,350 | 41,626 | 22.5% | 21.0% |
| Research and development expenses | 25,082 | 361 | 24,721 | 19,561 | 28.2% | 26.4% |
| General and administrative expenses | 21,299 | 158 | 21,141 | 19,582 | 8.8% | 8.0% |

Six Months Ended
June 30,

| | GAAP | Foreign Currency Exchange Rate Impact (1) | Non-GAAP Constant Currency (2) | GAAP | GAAP % Change | Non-GAAP Constant Currency % Change (3) |
|-------------------------------------|-----------|---|--------------------------------------|-----------|------------------|--|
| | 2019 | 2019 | 2019 | 2018 | 2019 | 2019 |
| Product licenses revenues | \$ 38,412 | \$ (1,940) | \$ 40,352 | \$ 36,593 | 5.0% | 10.3% |
| Subscription services revenues | 14,248 | (206) | 14,454 | 15,246 | -6.5% | -5.2% |
| Product support revenues | 144,428 | (4,786) | 149,214 | 148,091 | -2.5% | 0.8% |
| Other services revenues | 36,015 | (1,415) | 37,430 | 43,639 | -17.5% | -14.2% |
| Cost of product support revenues | 14,788 | (351) | 15,139 | 9,606 | 53.9% | 57.6% |
| Cost of other services revenues | 28,577 | (1,296) | 29,873 | 30,047 | -4.9% | -0.6% |
| Sales and marketing expenses | 97,033 | (3,066) | 100,099 | 102,313 | -5.2% | -2.2% |
| Research and development expenses | 55,979 | (819) | 56,798 | 48,642 | 15.1% | 16.8% |
| General and administrative expenses | 43,784 | (707) | 44,491 | 43,471 | 0.7% | 2.3% |

| | 2018 | 2018 | 2018 | 2017 (as adjusted) | 2018 | 2018 |
|-------------------------------------|---------------------------|-----------|---------|-----------------------|-----------|-------|
| | Product licenses revenues | \$ 36,593 | \$ 664 | \$ 35,929 | \$ 40,374 | -9.4% |
| Subscription services revenues | 15,246 | 272 | 14,974 | 16,118 | -5.4% | -7.1% |
| Product support revenues | 148,091 | 4,108 | 143,983 | 141,278 | 4.8% | 1.9% |
| Other services revenues | 43,639 | 1,593 | 42,046 | 43,682 | -0.1% | -3.7% |
| Cost of product support revenues | 9,606 | 199 | 9,407 | 8,876 | 8.2% | 6.0% |
| Cost of other services revenues | 30,047 | 1,259 | 28,788 | 28,773 | 4.4% | 0.1% |
| Sales and marketing expenses | 102,313 | 1,961 | 100,352 | 81,208 | 26.0% | 23.6% |
| Research and development expenses | 48,642 | 759 | 47,883 | 37,987 | 28.0% | 26.1% |
| General and administrative expenses | 43,471 | 511 | 42,960 | 39,839 | 9.1% | 7.8% |

- (1) The “Foreign Currency Exchange Rate Impact” reflects the estimated impact from fluctuations in foreign currency exchange rates on international components of our Consolidated Statements of Operations. It shows the increase (decrease) in international revenues or expenses, as applicable, from the same period in the prior year, based on comparisons to the prior year quarterly average foreign currency exchange rates. The term “international” refers to operations outside of the United States and Canada.
- (2) The “Non-GAAP Constant Currency” reflects the current period GAAP amount, less the Foreign Currency Exchange Rate Impact.
- (3) The “Non-GAAP Constant Currency % Change” reflects the percentage change between the current period Non-GAAP Constant Currency amount and the GAAP amount for the same period in the prior year.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based on our Consolidated Financial Statements, which have been prepared in accordance with GAAP.

The preparation of our Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, and equity, the 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. These estimates, particularly estimates relating to revenue recognition, have a material impact on our financial statements. In some cases, changes in accounting estimates are reasonably likely to occur from period to period. Actual results and outcomes could differ from these estimates and assumptions.

The section “Critical Accounting Policies” included in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2018 provides a more detailed explanation of the judgments made and a discussion of our accounting estimates and policies. There have been no significant changes in such estimates and policies since December 31, 2018.

Results of Operations

Comparison of the three and six months ended June 30, 2019 and 2018

Revenues

Except as otherwise indicated herein, the term “domestic” refers to operations in the United States and Canada and the term “international” refers to operations outside of the United States and Canada.

Product licenses and subscription services revenues. The following table sets forth product licenses and subscription services revenues (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended June 30, | | | % | Six Months Ended June 30, | | | % |
|---|--------------------------------|------------------|--------|------------------|------------------------------|-------|--------|---|
| | 2019 | 2018 | Change | | 2019 | 2018 | Change | |
| Product Licenses and Subscription Services Revenues: | | | | | | | | |
| Product Licenses | | | | | | | | |
| Domestic | \$ 11,525 | \$ 7,953 | 44.9% | \$ 20,719 | \$ 19,149 | 8.2% | | |
| International | 8,596 | 11,339 | -24.2% | 17,693 | 17,444 | 1.4% | | |
| Total product licenses revenues | <u>20,121</u> | <u>19,292</u> | 4.3% | <u>38,412</u> | <u>36,593</u> | 5.0% | | |
| Subscription Services | | | | | | | | |
| Domestic | 5,379 | 5,889 | -8.7% | 10,842 | 11,966 | -9.4% | | |
| International | 1,725 | 1,695 | 1.8% | 3,406 | 3,280 | 3.8% | | |
| Total subscription services revenues | <u>7,104</u> | <u>7,584</u> | -6.3% | <u>14,248</u> | <u>15,246</u> | -6.5% | | |
| Total product licenses and subscription services revenues | <u>\$ 27,225</u> | <u>\$ 26,876</u> | 1.3% | <u>\$ 52,660</u> | <u>\$ 51,839</u> | 1.6% | | |

The following table sets forth a summary, grouped by size, of the number of recognized product licenses transactions for the periods indicated:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|----------|------------------------------|-----------|
| | 2019 | 2018 | 2019 | 2018 |
| Product Licenses Transactions with Recognized Licenses Revenue in the Applicable Period: | | | | |
| More than \$1.0 million in licenses revenue recognized | 5 | 3 | 7 | 4 |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 1 | 3 | 4 | 7 |
| Total | <u>6</u> | <u>6</u> | <u>11</u> | <u>11</u> |
| Domestic: | | | | |
| More than \$1.0 million in licenses revenue recognized | 4 | 1 | 5 | 2 |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 1 | 1 | 2 | 4 |
| Total | <u>5</u> | <u>2</u> | <u>7</u> | <u>6</u> |
| International: | | | | |
| More than \$1.0 million in licenses revenue recognized | 1 | 2 | 2 | 2 |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 0 | 2 | 2 | 3 |
| Total | <u>1</u> | <u>4</u> | <u>4</u> | <u>5</u> |

The following table sets forth the recognized revenue (in thousands) attributable to product licenses transactions, grouped by size, and related percentage changes for the periods indicated:

| | Three Months Ended June 30, | | | % | Six Months Ended June 30, | | | % |
|--|--------------------------------|------------------|---------------|------------------|------------------------------|-------------|--------|---|
| | 2019 | 2018 | Change | | 2019 | 2018 | Change | |
| Product Licenses Revenue Recognized in the Applicable Period: | | | | | | | | |
| More than \$1.0 million in licenses revenue recognized | \$ 7,579 | \$ 3,901 | 94.3% | \$ 9,981 | \$ 4,956 | 101.4% | | |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 993 | 2,175 | -54.3% | 3,054 | 4,742 | -35.6% | | |
| Less than \$0.5 million in licenses revenue recognized | 11,549 | 13,216 | -12.6% | 25,377 | 26,895 | -5.6% | | |
| Total | 20,121 | 19,292 | 4.3% | 38,412 | 36,593 | 5.0% | | |
| <i>Domestic:</i> | | | | | | | | |
| More than \$1.0 million in licenses revenue recognized | 5,219 | 1,794 | 190.9% | 6,347 | 2,849 | 122.8% | | |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 993 | 610 | 62.8% | 1,542 | 2,620 | -41.1% | | |
| Less than \$0.5 million in licenses revenue recognized | 5,313 | 5,549 | -4.3% | 12,830 | 13,680 | -6.2% | | |
| Total | 11,525 | 7,953 | 44.9% | 20,719 | 19,149 | 8.2% | | |
| <i>International:</i> | | | | | | | | |
| More than \$1.0 million in licenses revenue recognized | 2,360 | 2,107 | 12.0% | 3,634 | 2,107 | 72.5% | | |
| Between \$0.5 million and \$1.0 million in licenses revenue recognized | 0 | 1,565 | -100.0% | 1,512 | 2,122 | -28.7% | | |
| Less than \$0.5 million in licenses revenue recognized | 6,236 | 7,667 | -18.7% | 12,547 | 13,215 | -5.1% | | |
| Total | \$ 8,596 | \$ 11,339 | -24.2% | \$ 17,693 | \$ 17,444 | 1.4% | | |

Product licenses revenues increased \$0.8 million and \$1.8 million for the three and six months ended June 30, 2019, respectively, as compared to the same periods in the prior year. For the three months ended June 30, 2019 and 2018, product licenses transactions with more than \$0.5 million in recognized revenue represented 42.6% and 31.5%, respectively, of our product licenses revenues. For the six months ended June 30, 2019, our top three product licenses transactions totaled \$5.4 million in recognized revenue, or 14.0% of total product licenses revenues, compared to \$3.9 million, or 10.8% of total product licenses revenues, for the six months ended June 30, 2018.

Domestic product licenses revenues. Domestic product licenses revenues increased \$3.6 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to an increase in the number of transactions with greater than \$1.0 million in recognized revenue and an increase in the average deal size of transactions with recognized revenue between \$0.5 million and \$1.0 million, partially offset by a decrease in the average deal size of transactions with less than \$0.5 million in recognized revenue.

Domestic product licenses revenues increased \$1.6 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to an increase in the number of transactions with greater than \$1.0 million in recognized revenue, partially offset by a decrease in the number of transactions with recognized revenue between \$0.5 million and \$1.0 million and a decrease in the average deal size of transactions with less than \$0.5 million in recognized revenue.

International product licenses revenues. International product licenses revenues decreased \$2.7 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a decrease in the number of transactions with recognized revenue between \$0.5 million and \$1.0 million and a \$0.6 million unfavorable foreign currency exchange impact.

International product licenses revenues increased \$0.2 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to an increase in the average deal size of transactions with revenue greater than \$1.0 million in recognized revenue, partially offset by a \$1.9 million unfavorable foreign currency exchange impact and a decrease in the number of transactions with recognized revenue between \$0.5 million and \$1.0 million.

Subscription services revenues. Subscription services revenues are derived primarily from our cloud services offerings that are recognized on a subscription basis over the service period of the contract. Subscription services revenues decreased \$0.5 million and \$1.0 million for the three and six months ended June 30, 2019, respectively, as compared to the same periods in the prior year, primarily due to a decrease in the use of subscription services by existing customers.

Product support revenues. The following table sets forth product support revenues (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended | | | Six Months Ended | | |
|--------------------------------|--------------------|------------------|-------------|-------------------|-------------------|-------------|
| | June 30, | | % Change | June 30, | | % Change |
| | 2019 | 2018 | | 2019 | 2018 | |
| Product Support Revenues: | | | | | | |
| Domestic | \$ 43,184 | \$ 43,681 | -1.1% | \$ 85,186 | \$ 86,825 | -1.9% |
| International | 29,794 | 29,995 | -0.7% | 59,242 | 61,266 | -3.3% |
| Total product support revenues | <u>\$ 72,978</u> | <u>\$ 73,676</u> | -0.9% | <u>\$ 144,428</u> | <u>\$ 148,091</u> | -2.5% |

Product support revenues are derived from providing technical software support and software updates and upgrades to customers. Product support revenues are recognized ratably over the term of the contract, which is generally one year. Product support revenues decreased \$0.7 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.1 million unfavorable foreign currency exchange impact, partially offset by an increase in new product support contracts. Product support revenues decreased \$3.7 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$4.8 million unfavorable foreign currency exchange impact, partially offset by an increase in new product support contracts.

Other services revenues. The following table sets forth other services revenues (in thousands) and related percentage changes in these revenues for the periods indicated:

| | Three Months Ended | | | Six Months Ended | | |
|-------------------------------|--------------------|------------------|-------------|------------------|------------------|-------------|
| | June 30, | | % Change | June 30, | | % Change |
| | 2019 | 2018 | | 2019 | 2018 | |
| Other Services Revenues: | | | | | | |
| Consulting | | | | | | |
| Domestic | \$ 6,254 | \$ 8,986 | -30.4% | \$ 13,300 | \$ 19,291 | -31.1% |
| International | 9,240 | 8,724 | 5.9% | 18,797 | 19,706 | -4.6% |
| Total consulting revenues | <u>15,494</u> | <u>17,710</u> | -12.5% | <u>32,097</u> | <u>38,997</u> | -17.7% |
| Education | 2,040 | 2,340 | -12.8% | 3,918 | 4,642 | -15.6% |
| Total other services revenues | <u>\$ 17,534</u> | <u>\$ 20,050</u> | -12.5% | <u>\$ 36,015</u> | <u>\$ 43,639</u> | -17.5% |

Consulting revenues. Consulting revenues are derived from helping customers plan and execute the deployment of our software. Consulting revenues decreased \$2.2 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a decrease in billable hours worldwide and a \$0.5 million unfavorable foreign currency exchange impact. Consulting revenues decreased \$6.9 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a decrease in billable hours worldwide and a \$1.3 million unfavorable foreign currency exchange impact.

Education revenues. Education revenues are derived from the education and training that we provide to our customers to enhance their ability to fully utilize the features and functionality of our software. These offerings include self-tutorials, custom course development, joint training with customers' internal staff, and standard course offerings, with pricing dependent on the specific offering delivered. Education revenues decreased \$0.3 million and \$0.7 million for the three and six months ended June 30, 2019, respectively, as compared to the same periods in the prior year, primarily due to a decrease in overall contract values.

Costs and Expenses

Cost of revenues. The following table sets forth cost of revenues (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended June 30, | | % | Six Months Ended June 30, | | % |
|--|--------------------------------|-----------|--------|------------------------------|-----------|--------|
| | 2019 | 2018 | | 2019 | 2018 | |
| Cost of Revenues: | | | | | | |
| Product licenses and subscription services: | | | | | | |
| Product licenses | \$ 552 | \$ 1,667 | -66.9% | \$ 1,071 | \$ 3,878 | -72.4% |
| Subscription services | 3,489 | 3,445 | 1.3% | 7,087 | 6,694 | 5.9% |
| Total product licenses and subscription services | 4,041 | 5,112 | -21.0% | 8,158 | 10,572 | -22.8% |
| Product support | 7,721 | 4,810 | 60.5% | 14,788 | 9,606 | 53.9% |
| Other services: | | | | | | |
| Consulting | 11,909 | 13,542 | -12.1% | 24,894 | 26,863 | -7.3% |
| Education | 1,679 | 1,576 | 6.5% | 3,683 | 3,184 | 15.7% |
| Total other services | 13,588 | 15,118 | -10.1% | 28,577 | 30,047 | -4.9% |
| Total cost of revenues | \$ 25,350 | \$ 25,040 | 1.2% | \$ 51,523 | \$ 50,225 | 2.6% |

Cost of product licenses revenues. Cost of product licenses revenues consists of amortization of capitalized software development costs, referral fees paid to channel partners, the costs of product manuals and media, and royalties paid to third-party software vendors. Capitalized software development costs are generally amortized over a useful life of three years.

Cost of product licenses revenues decreased \$1.1 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$1.0 million decrease in amortization of capitalized software development costs related to MicroStrategy 10™, which became fully amortized in May 2018. Cost of product licenses revenues decreased \$2.8 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.5 million decrease in amortization of capitalized software development costs related to MicroStrategy 10, which became fully amortized in May 2018, and a \$0.3 million decrease in referral fees related to channel partners. As of June 30, 2019, all previously capitalized software development costs have been fully amortized.

Cost of subscription services revenues. Cost of subscription services revenues consists of equipment, facility and other related support costs, and personnel and related overhead costs. Cost of subscription services revenues did not materially change for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$0.5 million increase in third-party hosting service provider fees, partially offset by a \$0.2 million decrease in compensation and related costs and a \$0.2 million decrease in equipment, facility, and other related support costs. Subscription services headcount increased 14.8% to 62 at June 30, 2019 from 54 at June 30, 2018.

Cost of subscription services revenues increased \$0.4 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$1.0 million increase in third-party hosting service provider fees, partially offset by a \$0.3 million decrease in compensation and related costs due to a decrease in average staffing levels and a \$0.2 million decrease in equipment, facility, and other related support costs.

Cost of product support revenues. Cost of product support revenues consists of personnel and related overhead costs. Cost of product support revenues increased \$2.9 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.7 million increase in compensation and related costs due to an increase in services provided by our consulting personnel under our Enterprise Support program and an increase in product support staffing levels. Our Enterprise Support program utilizes consulting personnel to provide product support to our customers. Compensation related to personnel providing Enterprise Support services is reported as cost of product support revenues. Product support headcount increased 27.2% to 234 at June 30, 2019 from 184 at June 30, 2018.

As a result of the grant of awards under the 2013 Equity Plan, we expect that share-based compensation expense, a portion of which is recognized as cost of product support revenues, will continue to be a recurring expense. As of June 30, 2019, we estimated that approximately \$0.9 million of additional share-based compensation expense will be recognized as cost of product support revenues over a remaining weighted average period of 2.6 years.

Cost of product support revenues increased \$5.2 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$4.7 million increase in compensation and related costs due to an increase in services provided by our consulting personnel under our Enterprise Support program and an increase in product support staffing levels, and a \$0.2 million increase in facility and other related support costs.

Cost of consulting revenues. Cost of consulting revenues consists of personnel and related overhead costs. Cost of consulting revenues decreased \$1.6 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$1.9 million decrease in compensation and related costs due to an increase in services provided by our consulting personnel under our Enterprise Support program and a decrease in consulting staffing levels, partially offset by a \$0.4 million increase in travel and entertainment expenditures and a \$0.2 million increase in facilities and other related support costs. Included in cost of consulting revenues for the three months ended June 30, 2019 is an aggregate \$0.5 million favorable foreign currency exchange impact. Consulting headcount decreased 8.8% to 404 at June 30, 2019 from 443 at June 30, 2018.

As a result of the grant of awards under the 2013 Equity Plan, we expect that share-based compensation expense, a portion of which is recognized as cost of consulting revenues, will continue to be a recurring expense. As of June 30, 2019, we estimated that approximately \$0.6 million of additional share-based compensation expense will be recognized as cost of consulting revenues over a remaining weighted average period of 3.4 years.

Cost of consulting revenues decreased \$2.0 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.6 million decrease in compensation and related costs due to an increase in services provided by our consulting personnel under our Enterprise Support program and a decrease in consulting staffing levels, a \$0.2 million decrease in subcontractor costs, and a \$0.2 million decrease in recruiting costs, partially offset by a \$0.7 million increase in travel and entertainment expenditures and a \$0.3 million increase in facilities and other related support costs. Included in cost of consulting revenues for the six months ended June 30, 2019 is an aggregate \$1.2 million favorable foreign currency exchange impact.

Cost of education revenues. Cost of education revenues consists of personnel and related overhead costs. Cost of education revenues did not materially change for the three months ended June 30, 2019, as compared to the same period in the prior year. Education headcount increased 2.6% to 40 at June 30, 2019 from 39 at June 30, 2018.

Cost of education revenues increased \$0.5 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$0.3 million increase in compensation and related costs due to an increase in staffing levels and a \$0.2 million increase in subcontractor costs.

Sales and marketing expenses. Sales and marketing expenses consist of personnel costs, commissions, office facilities, travel, advertising, public relations programs, and promotional events, such as trade shows, seminars, and technical conferences. The following table sets forth sales and marketing expenses (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended June 30, | | % | Six Months Ended June 30, | | % |
|------------------------------|--------------------------------|-----------|-------|------------------------------|------------|-------|
| | 2019 | 2018 | | 2019 | 2018 | |
| Sales and marketing expenses | \$ 48,273 | \$ 50,978 | -5.3% | \$ 97,033 | \$ 102,313 | -5.2% |

Sales and marketing expenses decreased \$2.7 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.4 million decrease in marketing and advertising costs, a \$0.8 million decrease in travel and entertainment expenditures, a \$0.5 million decrease in recruiting costs, and a \$0.5 million decrease in compensation and related costs due to a decrease in staffing levels, partially offset by a \$0.5 million increase in facility and other related support costs, a \$0.4 million net increase in share-based compensation expense, a \$0.3 million increase in the amortization of capitalized variable compensation, and a \$0.2 million increase in subcontractor costs. The \$0.4 million net increase in share-based compensation expense is primarily due to the grant of additional awards under the 2013 Equity Plan. Included in sales and marketing expenses for the three months ended June 30, 2019 is an aggregate \$1.4 million favorable foreign currency exchange impact. Sales and marketing headcount decreased 7.3% to 637 at June 30, 2019 from 687 at June 30, 2018.

As a result of the grant of awards under the 2013 Equity Plan, we expect that share-based compensation expense, a significant portion of which is recognized as sales and marketing expense, will continue to be a significant recurring expense. As of June 30, 2019, we estimated that approximately \$12.0 million of additional share-based compensation expense will be recognized as sales and marketing expense over a remaining weighted average period of 2.9 years. Included in this amount is approximately \$4.2 million of total unrecognized share-based compensation expense related to unvested stock options that have been or will be forfeited in connection with the departures of two executive officers in July 2019. Prior to their departures, such amount was expected to be recognized over a remaining service period of approximately 2.8 years.

Sales and marketing expenses decreased \$5.3 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$5.6 million decrease in marketing and advertising costs, a \$1.8 million decrease in travel and entertainment expenditures, and a \$0.8 million decrease in recruiting costs, partially offset by a \$1.2 million increase in facility and other related support costs, a \$0.7 million increase in subcontractor costs, a \$0.6 million increase in the amortization of capitalized variable compensation, a \$0.2 million net increase in share-based compensation expense, and a \$0.2 million increase in compensation and related costs. The \$0.2 million net increase in share-based compensation expense is primarily due to the grant of additional awards under the 2013 Equity Plan, partially offset by the effect of forfeitures of certain stock options and certain awards becoming fully vested since the second quarter of 2018. Included in sales and marketing expenses for the six months ended June 30, 2019 is an aggregate \$3.1 million favorable foreign currency exchange impact.

Research and development expenses. Research and development expenses consist of the personnel costs for our software engineering personnel, depreciation of equipment, and other related costs. The following table summarizes research and development expenses and amortization of capitalized software development costs (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended | | | Six Months Ended | | |
|--|--------------------|-----------|-------------|------------------|-----------|-------------|
| | June 30, | | % Change | June 30, | | % Change |
| | 2019 | 2018 | | 2019 | 2018 | |
| Research and development expenses | \$ 27,764 | \$ 25,082 | 10.7% | \$ 55,979 | \$ 48,642 | 15.1% |
| Amortization of capitalized software development costs included in cost of product licenses revenues | \$ 0 | \$ 1,000 | -100.0% | \$ 0 | \$ 2,499 | -100.0% |

Research and development expenses increased \$2.7 million for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$3.0 million increase in compensation and related costs due to an increase in staffing levels, a \$0.3 million increase in facility and other related support costs, and a \$0.2 million increase in consulting and advisory costs, partially offset by a \$0.5 million decrease in recruiting costs and a \$0.2 million net decrease in share-based compensation expense. The increase in research and development expenses reflects our previously announced strategy to seek to take greater advantage of the opportunities in the market by increasing our research and development expenditures as we invest in our technology products and personnel. The \$0.2 million net decrease in share-based compensation expense is primarily due to certain awards becoming fully vested since the second quarter of 2018. Research and development headcount increased 17.4% to 764 at June 30, 2019 from 651 at June 30, 2018. We expect research and development expenses to continue at the current pace in future periods. We have significantly accelerated the pace of our software development efforts and increased the frequency of our software releases subsequent to the release of MicroStrategy 10 in 2015, which has resulted in our software development costs in recent periods being expensed as incurred. We do not expect to capitalize material software development costs in the near term.

As a result of the grant of awards under the 2013 Equity Plan, we expect that share-based compensation expense, a significant portion of which is recognized as research and development expense, will continue to be a significant recurring expense. As of June 30, 2019, we estimated that approximately \$4.7 million of additional share-based compensation expense will be recognized as research and development expense over a remaining weighted average period of 2.4 years.

Research and development expenses increased \$7.3 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$6.8 million increase in compensation and related costs due to an increase in staffing levels, a \$0.9 million increase in facility and other related support costs, and a \$0.3 million increase in employee relations expenses, partially offset by \$0.6 million decrease in recruiting costs and a \$0.2 million net decrease in share-based compensation expense. The \$0.2 million net decrease in share-based compensation expense is primarily due to certain awards becoming fully vested since the second quarter of 2018, partially offset by the grant of additional awards under the 2013 Equity Plan.

General and administrative expenses. General and administrative expenses consist of personnel and related overhead costs, and other costs of our executive, finance, human resources, information systems, and administrative departments, as well as third-party consulting, legal, and other professional fees. The following table sets forth general and administrative expenses (in thousands) and related percentage changes for the periods indicated:

| | Three Months Ended | | | Six Months Ended | | |
|-------------------------------------|--------------------|-----------|-------------|------------------|-----------|-------------|
| | June 30, | | % Change | June 30, | | % Change |
| | 2019 | 2018 | | 2019 | 2018 | |
| General and administrative expenses | \$ 21,180 | \$ 21,299 | -0.6% | \$ 43,784 | \$ 43,471 | 0.7% |

General and administrative expenses did not materially change for the three months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$0.6 million decrease in legal, consulting, and other advisory costs, \$0.5 million net decrease in share-based compensation expense, and a \$0.4 million decrease in travel and entertainment expenditures, substantially offset by a \$0.8 million increase in compensation and related costs due to an increase in staffing levels and a \$0.6 million increase in facility and other related support costs. The \$0.5 million net decrease in share-based compensation expense is primarily due to certain awards becoming fully vested since the second quarter of 2018, partially offset by the effect of forfeitures of certain stock options. General and administrative headcount increased 4.3% to 336 at June 30, 2019 from 322 at June 30, 2018.

As a result of the grant of awards under the 2013 Equity Plan, we expect that share-based compensation expense, a significant portion of which is recognized as general and administrative expense, will continue to be a significant recurring expense. As of June 30, 2019, we estimated that approximately \$10.6 million of additional share-based compensation expense will be recognized as general and administrative expense over a remaining weighted average period of 2.6 years.

General and administrative expenses increased \$0.3 million for the six months ended June 30, 2019, as compared to the same period in the prior year, primarily due to a \$2.0 million increase in compensation and related costs due to an increase in staffing levels, a \$1.3 million increase in facility and other related support costs, and a \$0.9 million increase in write-offs to accounts receivable, partially offset by a \$2.2 million net decrease in share-based compensation expense, a \$0.8 million decrease in legal, consulting, and other advisory costs, a \$0.6 million decrease in travel and entertainment expenditures, a \$0.3 million decrease in recruiting costs, and a \$0.2 million decrease in employee relations expenses. The \$2.2 million net decrease in share-based compensation expense is primarily due to certain awards becoming fully vested since the second quarter of 2018, partially offset by the grant of additional awards under the 2013 Equity Plan.

Other Income, Net

Other income, net is comprised primarily of proceeds from the Domain Name Sale and foreign currency transaction gains and losses. For the three and six months ended June 30, 2019, other income, net, of \$29.4 and \$28.8 million, respectively, were comprised primarily of a \$29.8 million gain from the Domain Name Sale in the second quarter of 2019, partially offset by foreign currency transaction net losses arising mainly from the revaluation of U.S. dollar-denominated cash balances held at international locations in addition to outstanding balances denominated in the British Pound, which has declined in value as compared to the U.S. dollar. For the three and six months ended June 30, 2018, other income, net, of \$4.5 million and \$2.9 million, respectively, were comprised primarily of foreign currency transaction net gains arising mainly from the revaluation of U.S. dollar-denominated cash balances held at international locations.

Provision for Income Taxes

We have estimated an annual effective tax rate for the full fiscal year 2019 and applied that rate to the income before income taxes in determining the provision for income taxes for the six months ended June 30, 2019. We also record discrete items in each respective period as appropriate. The estimated effective tax rate is subject to fluctuation based on the level and mix of earnings and losses by tax jurisdiction, foreign tax rate differentials, and the relative impact of permanent book to tax differences (e.g., non-deductible expenses). Each quarter, a cumulative adjustment is recorded for any fluctuations in the estimated annual effective tax rate as compared to the prior quarter. As a result of these factors, and due to potential changes in our period-to-period results, fluctuations in our effective tax rate and respective tax provisions or benefits may occur.

For the six months ended June 30, 2019, we recorded a provision for income taxes of \$6.7 million that resulted in an effective tax rate of 35.0%, as compared to a provision for income taxes of \$0.5 million that resulted in an effective tax rate of 7.7% for the six months ended June 30, 2018. The change in the effective tax rate in 2019 is mainly due to certain discrete items and the change in the expected proportion of U.S. versus foreign income. The most significant discrete item was a tax provision of \$8.1 million on the \$29.8 million gain from the Domain Name Sale.

As of June 30, 2019, we had no U.S. federal NOL carryforwards and estimated that we had \$3.6 million of foreign NOL carryforwards. As of June 30, 2019, we estimated that we had foreign NOL carryforwards, other temporary differences and carryforwards, and credits that resulted in deferred tax assets, net of valuation allowances and deferred tax liabilities, of \$20.5 million. As of June 30, 2019, we had a valuation allowance of \$1.5 million related to certain foreign tax credit carryforwards that, in our present estimation, more likely than not will not be realized.

If we are unable to regain or increase profitability from our normal business operations in future periods, we may be required to increase the valuation allowance against our deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred. We will continue to regularly assess the realizability of deferred tax assets.

Deferred Revenue and Advance Payments

Deferred revenue and advance payments represent amounts received or due from our customers in advance of our transferring our products or services to the customer. Revenue is subsequently recognized in the period(s) in which control of the products or services are transferred to the customer.

The following table summarizes deferred revenue and advance payments (in thousands), as of:

| | June 30, 2019 | December 31, 2018 | June 30, 2018 |
|---|-------------------|----------------------|-------------------|
| Current: | | | |
| Deferred product licenses revenue | \$ 633 | \$ 1,768 | \$ 1,819 |
| Deferred subscription services revenue | 15,393 | 13,508 | 13,847 |
| Deferred product support revenue | 152,866 | 152,501 | 151,909 |
| Deferred other services revenue | 7,894 | 8,763 | 7,783 |
| Total current deferred revenue and advance payments | <u>\$ 176,786</u> | <u>\$ 176,540</u> | <u>\$ 175,358</u> |
| Non-current: | | | |
| Deferred product licenses revenue | \$ 405 | \$ 542 | \$ 794 |
| Deferred subscription services revenue | 116 | 2,384 | 9 |
| Deferred product support revenue | 3,083 | 3,091 | 3,950 |
| Deferred other services revenue | 571 | 452 | 1,063 |
| Total non-current deferred revenue and advance payments | <u>\$ 4,175</u> | <u>\$ 6,469</u> | <u>\$ 5,816</u> |
| Total current and non-current: | | | |
| Deferred product licenses revenue | \$ 1,038 | \$ 2,310 | \$ 2,613 |
| Deferred subscription services revenue | 15,509 | 15,892 | 13,856 |
| Deferred product support revenue | 155,949 | 155,592 | 155,859 |
| Deferred other services revenue | 8,465 | 9,215 | 8,846 |
| Total current and non-current deferred revenue and advance payments | <u>\$ 180,961</u> | <u>\$ 183,009</u> | <u>\$ 181,174</u> |

Total deferred revenue and advance payments decreased \$2.0 million as of June 30, 2019, as compared to December 31, 2018, primarily due to the recognition of previously deferred product licenses, other services, and subscription services revenues, partially offset by an increase in deferred revenue from new product support contracts. Total deferred revenue and advance payments decreased \$0.2 million as of June 30, 2019, as compared to June 30, 2018, primarily due to the decrease in our international deferred product support revenue balances from the general strengthening of the U.S. dollar and the recognition of previously deferred product licenses and other services revenues, partially offset by an increase in deferred revenue from new product support and subscription services contracts.

We expect to recognize approximately \$176.8 million of deferred revenue and advance payments over the next 12 months. However, the timing and ultimate recognition of our deferred revenue and advance payments depend on our satisfaction of various performance obligations, and the amount of deferred revenue and advance payments at any date should not be considered indicative of revenues for any succeeding period.

Liquidity and Capital Resources

Liquidity. Our principal sources of liquidity are cash and cash equivalents and on-going collection of our accounts receivable. Cash and cash equivalents may include holdings in bank demand deposits, money market instruments, certificates of deposit, and U.S. Treasury securities. We also periodically invest a portion of our excess cash in short-term investments with stated maturity dates between three months and one year from the purchase date.

As of June 30, 2019 and December 31, 2018, the amount of cash and cash equivalents and short-term investments held by our U.S. entities was \$294.0 million and \$173.6 million, respectively, and by our non-U.S. entities was \$280.8 million and \$402.5 million, respectively. We earn a significant amount of our revenues outside the United States and our accumulated foreign earnings and profits as of December 31, 2018 were \$397.4 million. As of June 30, 2019, we intend to indefinitely reinvest \$197.4 million of our undistributed foreign earnings. This amount takes into consideration repatriations we made during the three months ended June 30, 2019. After taking into account the Transition Tax, we expect such repatriation generated only an immaterial U.S. tax expense related to U.S. state income taxes. We do not anticipate needing to repatriate additional cash or cash equivalents held by non-U.S. entities to the United States to finance our U.S. operations.

We believe that existing cash and cash equivalents and short-term investments held by us and cash and cash equivalents anticipated to be generated by us are sufficient to meet working capital requirements, anticipated capital expenditures, and contractual obligations for at least the next 12 months.

The following table sets forth a summary of our cash flows (in thousands) and related percentage changes for the periods indicated:

| | Six Months Ended June 30, | | % |
|---|------------------------------|--------------|-----------|
| | 2019 | 2018 | |
| Net cash provided by operating activities | \$ 49,202 | \$ 23,327 | 110.9% |
| Net cash provided by (used in) investing activities | \$ 148,923 | \$ (353,340) | -142.1% |
| Net cash (used in) provided by financing activities | \$ (46,408) | \$ 2,462 | -1,985.0% |

Net cash provided by operating activities. The primary source of our cash provided by operating activities is cash collections of our accounts receivable from customers following the sales and renewals of our software licenses, technical software support, software updates and upgrades, as well as consulting, education, and subscription services. Our primary uses of cash in operating activities are for personnel-related expenditures for software development, personnel-related expenditures for providing consulting, education, and subscription services, and for sales and marketing costs, general and administrative costs, and income taxes.

Net cash provided by operating activities was \$49.2 million and \$23.3 million for the six months ended June 30, 2019 and 2018, respectively. The increase in net cash provided by operating activities during the six months ended June 30, 2019, as compared to the same period in the prior year, was due to a \$15.7 million increase from changes in operating assets and liabilities, a \$6.0 million increase in net income, and a \$4.2 million increase from changes in non-cash items. Non-cash items consist primarily of depreciation and amortization, write-offs and sales allowances, deferred taxes, and share-based compensation expense.

Net cash provided by (used in) investing activities. The changes in net cash provided by (used in) investing activities relate to purchases and redemptions of short-term investments and expenditures on property and equipment. Net cash provided by investing activities was \$148.9 million and net cash used in investing activities was \$353.3 million for the six months ended June 30, 2019 and 2018, respectively. The increase in net cash provided by investing activities for the six months ended June 30, 2019, as compared to the same period in the prior year, was due to a \$384.1 million decrease in purchases of short-term investments and a \$123.9 million increase in proceeds from the redemption of short-term investments, offset by a \$5.8 million increase in purchases of property and equipment.

Net cash (used in) provided by financing activities. The changes in net cash (used in) provided by financing activities primarily relate to the purchase of treasury stock and the exercise of stock options under the 2013 Equity Plan. Net cash used in financing activities was \$46.4 million and net cash provided by financing activities was \$2.5 million for the six months ended June 30, 2019 and 2018, respectively. The increase in net cash used in financing activities for the six months ended June 30, 2019, as compared to the same period in the prior year, was due to a \$48.2 million increase in purchases of treasury stock and a \$0.6 million decrease in proceeds from the exercise of stock options under the 2013 Equity Plan.

Contractual obligations.

The following table shows future minimum payments under noncancellable operating leases and purchase agreements with initial terms of greater than one year and anticipated payments related to the Transition Tax resulting from the Tax Act, based on the expected due dates of the various installments as of June 30, 2019 (in thousands):

| | Payments due by period ended June 30, | | | | |
|---------------------------------|---------------------------------------|------------------|------------------|------------------|------------------|
| | Total | 2020 | 2021-2022 | 2023-2024 | Thereafter |
| Contractual Obligations: | | | | | |
| Operating leases | \$ 168,411 | \$ 16,614 | \$ 33,298 | \$ 31,193 | \$ 87,306 |
| Purchase obligations | 23,968 | 9,694 | 11,193 | 1,351 | 1,730 |
| Transition Tax | 28,935 | 896 | 5,903 | 12,913 | 9,223 |
| Total | \$ 221,314 | \$ 27,204 | \$ 50,394 | \$ 45,457 | \$ 98,259 |

Unrecognized tax benefits. As of June 30, 2019, we had \$5.1 million of total gross unrecognized tax benefits, including penalty and interest accrued, recorded in other long-term liabilities. The timing of any payments that could result from these unrecognized tax benefits will depend on a number of factors, and accordingly the amount and period of any future payments cannot be estimated. We do not expect any significant tax payment related to these obligations during 2019.

Off-balance sheet arrangements. As of June 30, 2019, we did not have any off-balance sheet arrangements that had a material impact on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

Recent Accounting Standards

See Note 2, Recent Accounting Standards, to the Consolidated Financial Statements for further information.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The following discussion about our market risk exposures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements.

We are exposed to the impact of both interest rate changes and foreign currency fluctuations.

Interest Rate Risk. We face exposure to changes in interest rates primarily relating to our investments. We generally invest our excess cash in short-term, highly-rated, fixed-rate financial instruments. These fixed-rate instruments are subject to interest rate risk and may fall in value if interest rates increase. We do not hold or invest in these fixed-rate instruments for trading purposes or speculation. As of June 30, 2019, we held approximately \$313.3 million of investments in U.S. Treasury securities with stated maturity dates between three months and one year from the purchase date.

Foreign Currency Risk. We conduct a significant portion of our business in currencies other than the U.S. dollar, the currency in which we report our Consolidated Financial Statements. International revenues accounted for 42.8% and 43.6% of our total revenues for the three months ended June 30, 2019 and 2018, respectively, and 43.3% and 42.5% of our total revenues for the six months ended June 30, 2019 and 2018, respectively. We anticipate that international revenues will continue to account for a significant portion of our total revenues. The functional currency of each of our foreign subsidiaries is generally the local currency.

Assets and liabilities of our foreign subsidiaries are translated into U.S. dollars at exchange rates in effect as of the applicable balance sheet date and any resulting translation adjustments are included as an adjustment to stockholders' equity. Revenues and expenses generated from these subsidiaries are translated at average monthly exchange rates during the quarter in which the transactions occur. Gains and losses from transactions in local currencies are included in net income.

As a result of transacting in multiple currencies and reporting our financial statements in U.S. dollars, our operating results may be adversely impacted by currency exchange rate fluctuations in the future. The impact of foreign currency exchange rate fluctuations on current and comparable periods is described in the "Non-GAAP Financial Measures" section under "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations."

We cannot predict the effect of exchange rate fluctuations upon our future results. We attempt to minimize our foreign currency risk by converting our excess foreign currency held in foreign jurisdictions to U.S. dollar-denominated cash and investment accounts.

As of June 30, 2019 and December 31, 2018, a 10% adverse change in foreign currency exchange rates versus the U.S. dollar would have decreased our aggregate reported cash and cash equivalents and short-term investments by 0.4% and 0.3%, respectively. If average exchange rates during the six months ended June 30, 2019 had changed unfavorably by 10%, our revenues for the six months ended June 30, 2019 would have decreased by 3.9%. During the six months ended June 30, 2019, our revenues were lower by 3.5% as a result of a 6.8% unfavorable change in weighted average exchange rates, as compared to the same period in the prior year.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report. 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. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their control objectives. Based on the evaluation of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were not effective at the reasonable assurance level due to the material weaknesses in our internal controls disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018.

Material Weaknesses and Status of Remediation

As described in Part II, Item 9A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, we have been implementing a remediation plan to address the material weaknesses disclosed in such Annual Report. These material weaknesses will not be considered fully remediated until the applicable controls operate for a sufficient period of time and management concludes, through testing, that these controls are operating effectively. We expect to complete the remediation of these material weaknesses prior to the end of the fiscal year ending December 31, 2019.

Changes in Internal Controls. During the six months ended June 30, 2019, we implemented new internal controls to facilitate our adoption of ASU 2016-02 and help ensure the proper identification, accounting, and reporting of material lease arrangements. Other than as disclosed above under “Material Weaknesses and Status of Remediation” and the new internal controls related to our adoption of ASU 2016-02, there have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the six months ended June 30, 2019 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting. During the six months ended June 30, 2019, we implemented a new human resources management system. We continue to assess the impact of this new system on our internal control over financial reporting, but do not currently expect to make significant changes to our existing internal controls.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in various legal proceedings arising in the normal course of business. Although the outcomes of these legal proceedings are inherently difficult to predict, we do not expect the resolution of these legal proceedings to have a material adverse effect on our financial position, results of operations, or cash flows.

Item 1A. Risk Factors

You should carefully consider the risks described below before making an investment decision. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations.

If any of the following risks occurs, our business, financial condition, or results of operations could be materially adversely affected. In such case, the market price of our class A common stock could decline, and you may lose all or part of your investment.

Our quarterly operating results, revenues, and expenses may fluctuate significantly, which could have an adverse effect on the market price of our stock

For many reasons, including those described below, our operating results, revenues, and expenses have varied in the past and may vary significantly in the future from quarter to quarter. These fluctuations could have an adverse effect on the market price of our class A common stock.

Fluctuations in Quarterly Operating Results. Our quarterly operating results may fluctuate, in part, as a result of:

- the size, timing, volume, and execution of significant orders and shipments;
- the mix of products and services ordered by customers, including product licenses and subscription offerings, which can affect the extent to which revenue is recognized immediately or over future quarterly periods;
- the timing of the release or delivery of new or enhanced offerings, which may affect the period in which we can recognize revenue;
- the timing of announcements of new offerings by us or our competitors;
- changes in our pricing policies or those of our competitors;
- market acceptance of new and enhanced versions of our products and services;
- the length of our sales cycles;
- seasonal or other buying patterns of our customers;
- changes in our operating expenses;
- planned major maintenance activities related to our corporate aircraft;
- the timing of research and development projects and the capitalization of software development costs;
- personnel changes;
- our use of channel partners;
- utilization of our consulting and education services, which can be affected by delays or deferrals of customer implementation of our software products;
- changes in foreign currency exchange rates;
- our profitability and expectations for future profitability and their effect on our deferred tax assets and net income for the period in which any adjustment to our net deferred tax asset valuation allowance may be made;
- increases or decreases in our liability for unrecognized tax benefits; and
- changes in customer decision-making processes or customer budgets.

Limited Ability to Adjust Expenses. We base our operating expense budgets on expected revenue trends and strategic objectives. Many of our expenses, such as office leases and certain personnel costs, are relatively fixed. We may be unable to adjust spending quickly enough to offset any unexpected revenue shortfall. Accordingly, any shortfall in revenue may cause significant variation in operating results in any quarter. For example, if our revenues in the future are not sufficient to offset our operating expenses, or we are unable to adjust our operating expenses in a timely manner in response to any shortfall in anticipated revenue, we may incur operating losses.

Based on the above factors, we believe that quarter-to-quarter comparisons of our operating results are not a good indication of our future performance. It is possible that in one or more future quarters, our operating results may be below the expectations of public market analysts and investors. In that event, the market price of our class A common stock may fall.

The market price of our class A common stock has been and may continue to be volatile

The market price of our class A common stock historically has been volatile and may continue to be volatile. The market price of our class A common stock may fluctuate widely in response to various factors, some of which are beyond our control. These factors include, but are not limited to:

- quarterly variations in our results of operations or those of our competitors;
- announcements about our earnings that are not in line with analyst expectations, the likelihood of which may be enhanced because it is our policy not to give guidance relating to our anticipated financial performance in future periods;
- announcements by us or our competitors of acquisitions, dispositions, new offerings, significant contracts, commercial relationships, or capital commitments;
- the emergence of new sales channels in which we are unable to compete effectively;
- our ability to develop, market, and deliver new and enhanced offerings on a timely basis;
- commencement of, or our involvement in, litigation;
- any major change in our Board of Directors, management, or governing documents;
- changes in government regulations or in the status of our regulatory approvals;
- recommendations by securities analysts or changes in earnings estimates and our ability to meet those estimates;
- investor perception of our Company;
- announcements by our competitors of their earnings that are not in line with analyst expectations;
- the volume of shares of our class A common stock available for public sale;
- sales or purchases of stock by us or by our stockholders, and issuances of awards under our stock incentive plan;
- short sales, hedging, and other derivative transactions involving shares of our class A common stock; and
- general economic conditions and slow or negative growth of related markets.

In addition, the stock market in general, and the market for technology companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of companies in those markets. These broad market and industry factors may seriously harm the market price of our class A common stock, regardless of our actual operating performance.

We may not be able to regain or increase profitability from our normal business operations in the future

We generated net income for the six months ended June 30, 2019. However, excluding a one-time gain of \$21.8 million, net of tax, from the Domain Name Sale in the second quarter of 2019, we would have generated a net loss of \$9.3 million for the six months ended June 30, 2019. We may not be able to regain or increase profitability from our normal business operations on a quarterly or annual basis in the future. If our revenues are not sufficient to offset our operating expenses, or we are unable to adjust our operating expenses in a timely manner in response to any shortfall in anticipated revenue, we may incur operating losses in future periods. As a result, our business, results of operations, and financial condition may be materially adversely affected.

As of June 30, 2019, we had \$20.5 million of deferred tax assets, net of a \$1.5 million valuation allowance. If we are unable to regain or increase profitability from our normal business operations in the future, we may be required to increase the valuation allowance against these deferred tax assets, which could result in a charge that would materially adversely affect net income in the period in which the charge is incurred.

Economic uncertainty and increased competition for our customers, particularly in the retail industry, could materially adversely affect our business and results of operations

The U.S. and other significant markets have experienced cyclical downturns, and worldwide economic conditions remain uncertain. Economic uncertainty and associated macroeconomic conditions make it extremely difficult for our customers and us to accurately forecast and plan future business activities and could cause our customers to slow spending on our products and services, which could delay and lengthen sales cycles. Furthermore, during uncertain economic times, our customers may face issues gaining timely access to sufficient credit, which could result in an impairment of their ability to make timely payments to us. If that were to occur, we may be required to increase our allowance for doubtful accounts and our results would be negatively impacted.

Furthermore, we have a significant number of customers in the retail industry, which has experienced intense competition and structural changes. A significant downturn or the intensification of competition in this industry may cause organizations to reduce their capital expenditures in general or specifically reduce their spending on information technology (“IT”). In addition, customers in this industry may delay or cancel IT projects or seek to lower their costs by renegotiating vendor contracts. Customers with excess IT resources may choose to develop in-house software solutions rather than obtain those solutions from us. Consumers have increasingly migrated toward large e-commerce platforms and other online applications. As a result, the retail industry has experienced consolidation and other ownership changes. In the future, retailers may further consolidate, undergo restructurings or reorganizations, or realign their affiliations, any of which could decrease the number of competitors within the retail industry, reducing the number of potential customers for our offerings. Moreover, our competitors may respond to challenging market conditions by lowering prices and attempting to lure away our customers.

We cannot predict the timing, strength, or duration of any economic slowdown, or any subsequent recovery generally, or competitive and structural changes in the retail industry. If the conditions in the general economy and the markets in which we operate worsen from present levels, our business, financial condition, and results of operations could be materially adversely affected.

We may have exposure to greater than anticipated tax liabilities

We are subject to income taxes and non-income taxes in a variety of domestic and foreign jurisdictions. Our future income taxes could be materially adversely affected by earnings that are lower than anticipated in jurisdictions where we have lower statutory rates, earnings that are higher than anticipated in jurisdictions where we have higher statutory rates, changes in the valuation of our deferred tax assets and liabilities, changes in the amount of unrecognized tax benefits, or changes in tax laws, regulations, accounting principles, or interpretations thereof.

In the United States, the Tax Act was enacted in December 2017, bringing about broad changes in the existing corporate tax system. Over time, the Tax Act may result in material impacts to our results of operations and may affect customer behavior and our ability to forecast our effective tax rate. Many aspects of the Tax Act are unclear at this time and remain subject to pending regulatory and accounting guidance. As a result, we have not yet been able to determine the full impact of the Tax Act on our business, operating results, and financial condition. As additional regulatory guidance is issued by the Internal Revenue Service, accounting treatment is clarified, and we perform additional analysis on the application of the Tax Act, our tax obligations and effective tax rate could be materially affected.

In the United Kingdom, legislation imposing a tax related to offshore receipts in respect of intangible property held in low tax jurisdictions became effective in April 2019. Certain aspects of this legislation and its implementation remain unclear at this time, and, as a result, we have not yet been able to determine the full impact of the legislation on our business, operating results, or financial condition. We expect that additional regulations or guidance may be issued and the accounting treatment of the new tax may be clarified. This legislation may materially increase our tax obligations with respect to the applicable receipts, which could have a material adverse effect on our results of operations.

Further changes in the tax laws of foreign jurisdictions could arise, including as a result of the project undertaken by the Organisation for Economic Co-operation and Development (“OECD”) to combat base erosion and profit shifting (“BEPS”). The OECD, which represents a coalition of member countries, has issued recommendations that, in some cases, make substantial changes to numerous long-standing tax positions and principles. These changes, many of which have been adopted or are under active consideration by OECD members and/or other countries, could increase tax uncertainty and may adversely affect our provision for income taxes.

Our determination of our tax liability is subject to review by applicable domestic and foreign tax authorities. Any adverse outcome of such reviews could have an adverse effect on our operating results and financial condition. The determination of our worldwide provision for income taxes and other tax liabilities requires significant judgment and, in the ordinary course of business, there are many transactions and calculations where the ultimate tax determination is uncertain. Moreover, as a multinational business, we have subsidiaries that engage in many intercompany transactions in a variety of tax jurisdictions where the ultimate tax determination is uncertain.

We also have contingent tax liabilities that, in management's judgment, are not probable of assertion. If such unasserted contingent liabilities were to be asserted, or become probable of assertion, we may be required to record significant expenses and liabilities in the period in which these liabilities are asserted or become probable of assertion.

As a result of these and other factors, the ultimate amount of tax obligations owed may differ from the amounts recorded in our financial statements and any such difference may materially affect our financial results in future periods in which we change our estimates of our tax obligations or in which the ultimate tax outcome is determined.

If the market for analytics products fails to grow as we expect or if businesses fail to adopt our offerings, our business, operating results, and financial condition could be materially adversely affected

Nearly all of our revenues to date have come from sales of analytics products and related technical support, consulting, and education services. We expect these sales to account for a large portion of our revenues for the foreseeable future. Although demand for analytics products has grown in recent years, the market for analytics offerings continues to evolve. Resistance from consumer and privacy groups to commercial collection, use, and sharing of data on spending patterns and other personal behavior (including individuals' online or offline activities, mobile data, sensor data, social data, web log data, Internet of Things data, and other personal data) has grown in recent years and our customers, potential customers or the public in general may perceive that use of our analytics products could violate individual privacy rights. In addition, increasing government restrictions on the collection, use, and transfer of personal data could impair the further growth of the market for analytics products. We cannot be sure that this market will continue to grow or, even if it does grow, that businesses will adopt our solutions.

We have spent, and intend to keep spending, considerable resources to educate potential customers about analytics offerings in general and our offerings in particular. However, we cannot be sure that these expenditures will help any of our offerings achieve any additional market acceptance. If the market fails to grow or grows more slowly than we currently expect or businesses fail to adopt our offerings, our business, operating results, and financial condition could be materially adversely affected.

Our products face intense competition, which may lead to lower prices for our products and services, reduced gross margins, loss of market share, and reduced revenue

The analytics market is highly competitive and subject to rapidly changing technology paradigms. Within the analytics space, we compete with many different types of vendors, including large software vendors, such as IBM, Microsoft, Oracle, and SAP, that provide one or more products that directly compete with our products. We also compete with other analytics software providers, such as Qlik, Tableau Software, and the SAS Institute. Our future success depends on the effectiveness with which we can differentiate our offerings and compete with these vendors and other potential competitors across analytics implementation projects of varying sizes. Our ability to compete successfully in our markets depends on a number of factors, both within and outside of our control. Some of these factors include product deployment options; analytical, mobility, data discovery, and visualization capabilities; performance and scalability; the quality and reliability of our customer service and support; licensing model; and brand recognition. Failure to compete successfully in any one of these or other areas may reduce the demand for our products, as well as materially adversely affect our revenue from both existing and prospective customers.

Some of our competitors have longer operating histories and significantly greater financial, technical, and marketing resources than we do. As a result, they may be able to respond more quickly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion, sale, and marketing of their offerings than we can, such as offering certain analytics products free of charge when bundled with other software offerings. In addition, many of our competitors have strong relationships with current and potential customers, extensive industry and specialized business knowledge, as well as corresponding proprietary technologies that they can leverage, such as multidimensional databases and enterprise resource planning repositories. As a result, they may be able to prevent us from penetrating new accounts or expanding within existing accounts.

Increased competition may lead to price cuts, reduced gross margins, and loss of market share. We may not be able to compete successfully against current and future competitors, and the failure to meet the competitive pressures we face may have a material adverse effect on our business, operating results, and financial condition.

Current and future competitors may also make strategic acquisitions or establish cooperative relationships among themselves or with others. By doing so, these competitors may increase their ability to meet the needs of our potential customers by their expanded offerings. Our current or prospective channel partners may establish cooperative relationships with our current or future competitors. These relationships may limit our ability to sell our analytics offerings through specific distribution channels. Accordingly, new competitors or alliances among current and future competitors may emerge and rapidly gain significant market share. These developments could limit our ability to obtain revenues from new customers and to sustain software maintenance revenues from our installed customer base. In addition, basic office productivity software suites, such as Microsoft Office, could evolve to offer advanced analysis and reporting capabilities that may reduce the demand for our analytics offerings.

We depend on revenue from a single suite of products and related services as well as revenue from our installed customer base

Our platform and related services account for a substantial portion of our revenue. Because of this revenue concentration, our business could be harmed by a decline in demand for, or in the adoption or prices of, these products and related services as a result of, among other factors, any change in our pricing or packaging model, increased competition, maturation in the markets for these products, or other risks described in this Quarterly Report.

We also depend on our installed customer base for a substantial portion of our revenue. We have contracts with our license customers for ongoing support and maintenance, as well as contracts for cloud-based subscription services that provide recurring revenues to us. In addition, our installed customer base has historically generated additional new license and services revenues for us. If our existing customers cancel or fail to renew their service contracts or fail to purchase additional products or services, our revenue could decrease and our operating results could be materially adversely affected.

If we are unable to develop and release product enhancements and new offerings to respond to rapid technological change in a timely and cost-effective manner, our business, operating results, and financial condition could be materially adversely affected

The market for our offerings is characterized by rapid technological change, frequent new product introductions and enhancements, changing customer demands, and evolving industry standards. The introduction of offerings embodying new technologies can quickly make existing offerings obsolete and unmarketable. We believe that our future success depends largely on our ability to:

- continue to support a number of popular operating systems and databases;
- maintain and improve our current offerings;
- rapidly develop new offerings and product enhancements that achieve market acceptance;
- maintain technological competitiveness; and
- meet an expanding range of customer requirements.

Analytics applications are inherently complex, and it can take a long time and require significant research and development expenditures to develop and test new offerings and product enhancements. In addition, customers may delay their purchasing decisions because they anticipate that new or enhanced versions of our offerings will soon become available. We cannot be sure that we will succeed in developing, marketing, and delivering, on a timely and cost-effective basis, new or enhanced offerings that respond to technological change or new customer requirements, nor can we be sure that any new or enhanced offerings will achieve market acceptance. Moreover, even if we introduce a new offering, we may experience a decline in revenues of our existing offerings that is not fully matched by the new offering's revenue. For example, customers may delay making purchases of a new offering to permit them to make a more thorough evaluation of the offering or until industry and marketplace reviews become widely available. Some customers may hesitate migrating to a new offering due to concerns regarding the complexity of migration or performance issues that may occur in product infancy. In addition, we may lose existing customers who choose a competitor's offering rather than migrate to our new offering. This could result in a temporary or permanent revenue shortfall and materially adversely affect our business.

A substantial customer shift in the deployment of MicroStrategy Analytics™ from a perpetual software license model to our cloud services subscription model could affect the timing of revenue recognition and materially adversely affect our operating results

We offer our analytics platform in the form of a perpetual software license and a cloud-based subscription. The payment streams and revenue recognition timing for our perpetual software licenses are different from those for our cloud-based subscriptions. For perpetual software licenses, customers typically pay us a lump sum soon after entering into a software license agreement and revenue is typically recognized upon delivery of the software to the customer. For cloud-based subscriptions, customers typically make periodic payments over the subscription period and revenue is typically recognized ratably over the subscription period. As a result, if a substantial number of current customers shift to subscribing, or new customers subscribe, to our cloud services offerings instead of purchasing perpetual software licenses for MicroStrategy Analytics, the resulting change in payment terms and revenue recognition may materially adversely affect our operating results and cash flows for the periods during which such a shift occurs.

Our investment in new business strategies and initiatives could disrupt the operations of our ongoing business and present risks that we have not adequately anticipated

We have invested, and in the future may invest, in new business strategies and initiatives. For example, in recent years we have introduced a number of innovative technologies designed to enable companies to capitalize on Big Data, mobile applications, cloud-based services, security, Internet of Things, and artificial intelligence trends in the marketplace. These endeavors may involve significant risks and uncertainties, including distraction of management from other business operations, the dedication of significant research and development, sales and marketing, and other resources to these new initiatives at the expense of our other business operations, generation of insufficient revenue to offset expenses associated with new initiatives, incompatibility of our new technologies with third-party platforms, inadequate return of capital, and other risks that we may not have adequately anticipated. Because new strategies and initiatives are inherently risky, these strategies and initiatives may not be successful and could materially adversely affect our financial condition and operating results.

Business disruptions, including interruptions, delays, or failures of our systems, third-party data center hosting facility or other third-party services, could materially adversely affect our operating results or result in a material weakness in our internal controls that could adversely affect the market price of our stock

A significant portion of our research and development activities or certain other critical business operations are concentrated in facilities in Northern Virginia, China, and Poland. In addition, we serve our customers and manage certain critical internal processes using a third-party data center hosting facility located in the United States and other third-party services, including AWS, Microsoft Azure, and other cloud services. We could experience a disruption or failure of our systems or the third-party hosting facility or other services that we use. Such disruptions or failures could include a natural disaster, fire, cyber-attack, act of terrorism, geopolitical conflict, or other catastrophic event, as well as power outages or telecommunications infrastructure outages, or a decision by one of our third-party service providers to close facilities that we use without adequate notice or to materially change the pricing or terms of their services, or other unanticipated problems with the third-party services that we use, including a failure to meet service standards.

We are a highly automated business and any such disruptions or failures could (i) result in the destruction or disruption of any of our critical business operations, controls or procedures, or IT systems, (ii) severely affect our ability to conduct normal business operations, including delaying completion of sales and provision of services, (iii) result in a material weakness in our internal control over financial reporting, (iv) cause our customers to terminate their subscriptions, (v) result in our issuing credits to customers or paying penalties or fines, (vi) harm our reputation, (vii) adversely affect our attrition rates or our ability to attract new customers, or (viii) cause our offerings to be perceived as not being secure, any of which could materially adversely affect our future operating results.

For example, as described in “Part I. Item 4. Controls and Procedures,” our internal control over financial reporting is not effective because of certain material weaknesses in our internal controls previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018. We are implementing remedial measures and, while there can be no assurance that our efforts will be successful, we expect to complete the remediation of these material weaknesses prior to the end of the fiscal year ending December 31, 2019. If we are unable to remediate these material weaknesses with respect to future periods or are otherwise unable to maintain effective internal control over financial reporting or disclosure controls and procedures, management may need to devote significant resources to improving internal controls, our ability to meet reporting obligations could be adversely affected, and investors’ confidence in our financial statements may be negatively affected, which could have a material adverse effect on our operating results and the market price of our stock.

We use channel partners and if we are unable to maintain successful relationships with them, our business, operating results, and financial condition could be materially adversely affected

In addition to our direct sales force, we use channel partners such as resellers, value-added resellers, system integrators, consulting firms, OEMs, and technology partners to license and support our products. For the six months ended June 30, 2019, transactions by channel partners for which we recognized revenues accounted for 26.3% of our total product licenses revenues. Our channel partners may offer customers the products and services of several different companies, including offerings that compete with ours. Because our channel partners generally do not have exclusive relationships with us, we cannot be certain that they will prioritize or devote adequate resources to selling our products. Moreover, divergence in strategy or contract defaults by any of these channel partners may materially adversely affect our ability to develop, market, sell, or support our offerings.

Although we believe that direct sales will continue to account for a majority of our product licenses revenues, we seek to maintain a significant level of sales activities through our channel partners. There can be no assurance that our channel partners will continue to cooperate with us. In addition, actions taken or not taken by such parties may materially adversely affect us. Our ability to achieve revenue growth in the future will depend in part on our ability to maintain successful relationships with our channel partners. If we are unable to maintain our relationships with these channel partners, our business, operating results, and financial condition could be materially adversely affected.

In addition, we rely on our channel partners to operate in accordance with the terms of their contractual agreements with us. For example, some of our agreements with our channel partners prescribe the terms and conditions pursuant to which they are authorized to resell or distribute our software and offer technical support and related services. If our channel partners do not comply with their contractual obligations to us, our business, operating results, and financial condition may be materially adversely affected. We also rely on our channel partners to operate in accordance with applicable laws and regulatory requirements. If they fail to do so, we may need to incur significant costs in responding to investigations or enforcement actions or paying penalties assessed by the applicable authorities.

Our recognition of deferred revenue and advance payments is subject to future performance obligations and may not be representative of revenues for succeeding periods

Our current and non-current deferred revenue and advance payments totaled \$181.0 million as of June 30, 2019. The timing and ultimate recognition of our deferred revenue and advance payments depend on various factors, including our performance of various service obligations.

Because of the possibility of customer changes or delays in customer development or implementation schedules or budgets, and the need for us to satisfactorily perform product support and other services, deferred revenue and advance payments at any particular date may not be representative of actual revenue for any succeeding period.

Our international operations are complex and expose us to risks that could have a material adverse effect on our business, operating results, and financial condition

We receive a significant portion of our total revenues from international sales and conduct our business activities in various foreign countries, including some emerging markets where we have limited experience, where the challenges of conducting our business can be significantly different from those we have faced in more developed markets, and where business practices may create internal control risks. International revenues accounted for 42.8% and 43.6% of our total revenues for the three months ended June 30, 2019 and 2018, respectively, and 43.3% and 42.5% of our total revenues for the six months ended June 30, 2019 and 2018, respectively. Our international operations require significant management attention and financial resources.

There are certain risks inherent in our international business activities, including:

- fluctuations in foreign currency exchange rates;
- new, or changes in, regulatory requirements;
- tariffs, export and import restrictions, restrictions on foreign investments, sanctions, laws and policies that favor local competitors (such as mandatory technology transfers), and other trade barriers or protection measures;
- costs of localizing offerings;
- lack of acceptance of localized offerings;
- difficulties in and costs of staffing, managing, and operating our international operations;
- tax issues, including restrictions on repatriating earnings;
- weaker intellectual property protection;
- economic weakness or currency related crises;
- the burden of complying with a wide variety of laws, including those relating to labor matters, antitrust, procurement and contracting, consumer and data protection, privacy, data localization, network security, and encryption;
- generally longer payment cycles and greater difficulty in collecting accounts receivable;
- our ability to adapt to sales practices and customer requirements in different cultures;

- corporate espionage; and
- political instability and security risks in the countries where we are doing business.

Disruptions to trade, weakening of economic conditions, economic and legal uncertainties, or changes in currency rates may adversely affect our business, financial condition, operating results, and cash flows. For example, we may face heightened risks in connection with our international operations as a result of the impending withdrawal of the United Kingdom from the European Union, commonly referred to as “Brexit.” The future effects of Brexit are uncertain and will depend on any agreements the United Kingdom makes to retain access to E.U. markets either during a transitional period or more permanently. Brexit could, among other outcomes, disrupt the free movement of goods, services, and people between the United Kingdom and the European Union and significantly disrupt trade between the United Kingdom and the European Union. Brexit could also lead to legal uncertainty and potentially divergent national laws and regulations, including tax laws and regulations, as the United Kingdom determines which E.U. laws to replace or replicate. In addition, the Trump administration has called for substantial changes to U.S. foreign trade policy, including the imposition of greater restrictions on international trade and significant increases in tariffs on goods imported into the United States, and has increased tariffs on certain goods imported into the United States from a number of foreign markets, following which retaliatory tariffs have been imposed on exports of certain U.S. goods to those markets. These tariffs and any further escalation of protectionist trade measures could adversely affect the markets in which we sell our products and services and, in turn, our business, financial condition, operating results and cash flows.

Changes to the U.S. taxation of our international income, or changes in foreign tax laws, could have a material effect on our future operating results. For example, the Tax Act brought about, among other items, corporate income tax rate changes, the modification or elimination of certain tax incentives, changes to the existing regime for taxing overseas earnings, and measures to prevent BEPS, and the United Kingdom adopted legislation imposing a tax related to offshore receipts in respect of intangible property held in low tax jurisdictions.

In addition, from time to time, we may undertake various potential intercompany transactions and legal entity restructurings that involve our international subsidiaries. We consider various factors in evaluating these potential transactions and restructurings, including the alignment of our corporate structure with our organizational objectives, the operational and tax efficiency of our corporate structure, and the long-term cash flows and cash needs of our business. Such transactions and restructurings could negatively impact our overall tax rate and result in additional tax liabilities.

Moreover, compliance with foreign and U.S. laws and regulations that are applicable to our international operations is complex and may increase our cost of doing business in international jurisdictions, and our international operations could expose us to fines and penalties if we fail to comply with these regulations. These laws and regulations include anti-bribery laws, such as the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, local laws prohibiting corrupt payments to government officials, and local laws relating to procurement, contracting, and antitrust. These laws and regulations also include import and export requirements and economic and trade sanctions administered by the Office of Foreign Assets Control and the U.S. Department of Commerce based on U.S. foreign policy and national security goals against targeted foreign states, organizations, and individuals. Although we have implemented policies and procedures designed to help ensure compliance with these laws, there can be no assurance that our employees, channel partners, and other persons with whom we do business will not take actions in violation of our policies or these laws. Any violations of these laws could subject us to civil or criminal penalties, including substantial fines or prohibitions on our ability to offer our products and services to one or more countries, and could also materially damage our reputation and our brand.

These factors may have a material adverse effect on our future sales and, consequently, on our business, operating results, and financial condition.

We may lose sales, or sales may be delayed, due to the long sales and implementation cycles of certain of our products and services, which could reduce our revenues

To date, our customers have typically invested substantial time, money, and other resources, and involved many people in the decision to license our software products and purchase our related services. As a result, we may wait nine months or more after the first contact with a customer for that customer to place an order while it seeks internal approval for the purchase of our products or services. During this long sales cycle, events may occur that affect the size and/or timing of the order or even cause it to be canceled. For example, our competitors may introduce new offerings, or the customer’s own budget and purchasing priorities may change.

Even after an order is placed, the time it takes to deploy our products and complete services engagements can vary widely. Implementing some of our offerings can take several months, depending on the customer’s needs, and may begin only with a pilot program. It may be difficult to deploy our products if the customer has complicated deployment requirements, such as deployments that involve integrating databases, hardware, and software from different vendors. If a customer hires a third party to deploy our products, we cannot be sure that our products will be deployed successfully.

Our results in any particular period may depend on the number and volume of large transactions in that period and these transactions may involve lengthier, more complex, and more unpredictable sales cycles than other transactions

As existing and potential customers seek to standardize on a single analytics vendor or require greater vendor capacity to meet their growing analytics needs, our business may experience larger transactions at the enterprise level and larger transactions may account for a greater proportion of our business. The presence or absence of one or more large transactions in a particular period may have a material positive or negative effect on our revenue and operating results for that period. For the six months ended June 30, 2019 and 2018, our top three product licenses transactions with recognized revenue totaled \$5.4 million and \$3.9 million, respectively, or 14.0% and 10.8% of total product licenses revenues, respectively. These transactions represent significant business and financial decisions for our customers, require considerable effort on the part of customers to assess alternative products, and often require additional levels of management approval. In addition, large transactions are often more complex than smaller transactions. These factors generally lengthen the typical sales cycle and increase the risk that customers may postpone or delay purchasing decisions from one period to a subsequent period or that customers will alter their purchasing requirements. We may also encounter greater competition and pricing pressure in larger transactions, and the sales effort and service delivery scope for larger transactions may require us to use additional resources to execute the transactions. These factors could result in lower than anticipated revenue and earnings for a particular period or lower estimated revenue and earnings in future periods.

We face a variety of risks in doing business with U.S. and foreign federal, state, and local governments and government agencies, including risks related to the procurement process, budget constraints and cycles, termination of contracts, and compliance with government contracting requirements

Our customers include the U.S. government and a number of state and local governments and government agencies. There are a variety of risks in doing business with government entities, including:

Procurement. Contracting with public sector customers is highly competitive and can be time-consuming and expensive, requiring us to incur significant up-front time and expense without any assurance that we will win a contract.

Budgetary Constraints and Cycles. Demand and payment for our products and services are impacted by public sector budgetary cycles and funding availability, with funding reductions or delays adversely impacting public sector demand for our products and services.

Termination of Contracts. Public sector customers often have contractual or other legal rights to terminate contracts for convenience or due to a default. If a contract is terminated for convenience, which can occur if the customer's needs change, we may only be able to collect fees for products or services delivered prior to termination and settlement expenses. If a contract is terminated due to a default, we may not recover even those amounts, and we may be liable for excess costs incurred by the customer for procuring alternative products or services.

Compliance with Government Contracting Requirements. Government contractors are required to comply with a variety of complex laws, regulations, and contractual provisions relating to the formation, administration, or performance of government contracts that give public sector customers substantial rights and remedies, many of which are not typically found in commercial contracts. These may include rights with respect to price protection, the accuracy of information provided to the government, contractor compliance with socio-economic policies, and other terms that are particular to government contracts. Federal, state, and local governments and government agencies routinely investigate and audit contractors for compliance with these requirements. If, as a result of an audit or review, it is determined that we have failed to comply with these requirements, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, costs associated with the triggering of price reduction clauses, fines, and suspensions or debarment from future government business and we may suffer harm to our reputation.

Our customers also include a number of foreign governments and government agencies. Similar procurement, budgetary, contract, and audit risks also apply to our doing business with these entities. In addition, compliance with complex regulations and contracting provisions in a variety of jurisdictions can be expensive and consume significant management resources. In certain jurisdictions, our ability to win business may be constrained by political and other factors unrelated to our competitive position in the market. Each of these difficulties could materially adversely affect our business and results of operations.

We depend on technology licensed to us by third parties, and the loss of this technology could impair our software, delay implementation of our offerings, or force us to pay higher license fees

We license third-party technologies that are incorporated into or utilized by our existing offerings. There can be no assurance that the licenses for such third-party technologies will not be terminated or that we will be able to license third-party software for future offerings. In addition, we may be unable to renegotiate acceptable third-party license terms, or we may be subject to infringement liability if third-party software that we license is found to infringe intellectual property rights of others. Changes in or the loss of third-party licenses could lead to a material increase in our costs or to our software offerings becoming inoperable or their performance being materially reduced. As a result, we may need to incur additional development costs to help ensure continued performance of our offerings, and we may experience a decreased demand for our offerings.

If we are unable to recruit or retain skilled personnel, or if we lose the services of our Chairman of the Board of Directors, President & Chief Executive Officer, our business, operating results, and financial condition could be materially adversely affected

Our future success depends on our continuing ability to attract, train, assimilate, and retain highly skilled personnel. Competition for these employees is intense, and competition may be amplified by evolving restrictions on immigration, travel, or availability of visas for skilled technology workers. We may not be able to retain our current key employees or attract, train, assimilate, and retain other highly skilled personnel in the future. Competition for qualified employees in the technology industry has historically been high, particularly for software engineers and other technical positions. Our future success also depends in large part on the continued service of Michael J. Saylor, our Chairman of the Board of Directors, President & Chief Executive Officer. If we lose the services of Mr. Saylor, or if we are unable to attract, train, assimilate, and retain the highly skilled personnel we need, our business, operating results, and financial condition could be materially adversely affected.

The emergence of new industry standards may materially adversely affect the demand for our existing offerings

The emergence of new industry standards in related fields may materially adversely affect the demand for our existing offerings. This could happen if new web standards and technologies or new standards in the field of operating system support emerge that are incompatible with customer deployments of our software offerings. For example, if we are unable to adapt our software offerings on a timely basis to new standards in database access technology, the ability of our software offerings to access customer databases could be impaired.

The nature of our software offerings makes them particularly susceptible to undetected errors, bugs, or security vulnerabilities, which could cause problems with how the offerings perform and, in turn, reduce demand for our offerings, reduce our revenue, and lead to litigation claims against us

Software as complex as ours may contain undetected errors, bugs, or security vulnerabilities. Although we test our software offerings extensively, we have in the past discovered software errors, bugs, or security vulnerabilities in our offerings after their introduction. Despite testing by us and our current and potential customers, errors, bugs, or security vulnerabilities may be found in new offerings or releases after commercial shipments begin. This could result in lost revenue, damage to our reputation, or delays in market acceptance, which could have a material adverse effect on our business, operating results, and financial condition. We may also need to expend resources and capital to correct these defects if they occur.

Our agreements with customers typically contain provisions designed to limit our exposure to product liability, warranty, and other claims. It is possible, however, that these provisions may not be effective under the laws of certain domestic or international jurisdictions and we may be exposed to product liability, warranty, and other claims. A successful product liability claim against us could have a material adverse effect on our business, operating results, and financial condition.

Changes in laws or regulations relating to privacy or the collection, processing, disclosure, storage, localization, or transmission of personal data, or any actual or perceived failure by us or our third-party service providers to comply with such laws and regulations, contractual obligations, or applicable privacy policies, could materially adversely affect our business

Aspects of our business, including our cloud services and digital identity offerings, involve collecting, processing, disclosing, storing, and transmitting personal data, which are subject to certain privacy policies, contractual obligations, and U.S. federal, U.S. state, and foreign laws, regulations, and directives relating to privacy and data protection. The amount of customer and employee data that we store through our cloud services offerings, networks, and other systems, including personal data, is increasing. In addition, the types of data subject to protection as personal data in the European Union, the United States, and elsewhere, including Asia and Latin America, have been expanding. In recent years, the collection and use of personal data by companies have come under increased regulatory and public scrutiny, especially in relation to the collection and processing of sensitive data, such as healthcare, biometric,

genetic, financial services, and government data, children's data, precise location data, and data regarding a person's race or ethnic origins, political opinions, religious or philosophical beliefs, trade union membership, or sex life or sexual orientation. For example, in the United States, protected health information is subject to the Health Insurance Portability and Accountability Act of 1996 ("HIPAA"). HIPAA has been supplemented by the Health Information Technology for Economic and Clinical Health Act with the result of increased civil and criminal penalties for noncompliance. Entities performing certain functions that engage in creating, receiving, maintaining, or transmitting protected health information provided by covered entities and other business associates are directly subject to enforcement under HIPAA. Our access to protected health information through our cloud services offerings triggers obligations to comply with certain privacy rules and data security requirements under HIPAA.

Any systems failure or security breach that results in the release of, or unauthorized access to, personal data, or any failure or perceived failure by us or our third-party service providers to comply with applicable privacy policies, contractual obligations, or any applicable laws or regulations relating to privacy or data protection, could result in proceedings against us by domestic or foreign government entities or others, including private plaintiffs in litigation. Such proceedings could result in the imposition of sanctions, fines, penalties, liabilities, government orders, and/or orders arising out of private proceedings, requiring that we change our data practices, any of which could have a material adverse effect on our business, operating results, reputation, and financial condition.

Various U.S. federal, U.S. state, and foreign legislative, regulatory, or other government bodies may enact new or additional laws or regulations, or issue rulings that invalidate prior laws or regulations, concerning privacy, data storage, data protection, and cross-border transfer of data that could materially adversely impact our business. For example, in April 2016, the European Parliament and the Council of the European Union formally adopted a comprehensive general data protection regulation ("GDPR"), which took effect in May 2018. GDPR governs data practices and privacy, establishes new requirements regarding the handling and security of personal data, requires disclosure of data breaches to individuals, customers, and data protection authorities in certain circumstances, requires companies to honor data subjects' requests relating to their personal data, permits regulators to impose fines of up to 4% of global annual revenue, and establishes a private right of action. Furthermore, a new ePrivacy Regulation, regulating electronic communications, was proposed in 2017 and is under consideration by the European Commission, the European Parliament, and the European Council.

In addition, we may be subject to a cybersecurity law that went into effect in China in June 2017 that has uncertain but broad application and imposes a number of new privacy and data security obligations, including a data localization requirement for certain types of data.

The state of California has also adopted a new comprehensive privacy law, the California Consumer Protection Act ("CCPA"), modeled largely on GDPR, that is scheduled to take effect on January 1, 2020 and become enforceable no later than July 1, 2020. The final scope of the CCPA remains unclear at this time since the California Attorney General is engaged in rulemaking proceedings pursuant to the CCPA and there are several bills pending in the California legislature to potentially amend the CCPA. While the final scope of the CCPA remains unclear, it is likely that we will be required to devote substantial resources to implement and maintain compliance with the CCPA, and noncompliance could carry the threat of regulatory investigations and fines or private litigation. In addition, several states are also now considering bills similar to the CCPA.

Furthermore, the U.S. Congress is considering comprehensive privacy legislation. At this time, it is unclear whether it will in fact pass such a law and if so, when and what it will require and prohibit. Moreover, it is not clear whether any such legislation would give the Federal Trade Commission ("FTC") any new authority to impose civil penalties for violations of the Federal Trade Commission Act in the first instance, or whether the U.S. Congress will grant the FTC rulemaking authority over privacy and information security.

Complying with these and other changing requirements could cause us or our customers to incur substantial costs or pay substantial fines or penalties, require us to change our business practices, require us to take on more onerous obligations in our contracts, or limit our ability to provide certain products and services in certain jurisdictions, any of which could materially adversely affect our business and operating results. In addition, mechanisms for lawfully transferring personal data from the European Union to the United States and certain other countries are being challenged in European courts, which could lead to uncertainty about the legality of such transfers, or burdensome or inconsistent legal requirements. New laws or regulations restricting or limiting the collection or use of mobile data could also reduce demand for certain of our services or require changes to our business practices, which could materially adversely affect our business and operating results.

If we or our third-party service providers experience a security breach and unauthorized parties obtain access to our customers', prospects', vendors', or channel partners' data, our data, or our cloud services offerings, networks, or other systems, our offerings may be perceived as not being secure, our reputation may be harmed, demand for our offerings may be reduced, our operations may be disrupted, we may incur significant legal and financial liabilities, and our business could be materially adversely affected

As part of our business, we process, store, and transmit our customers', prospects', vendors', and channel partners' information and data as well as our own, including in our cloud services offerings, networks, and other systems. There can be no assurance that any security measures that we or our third-party service providers have implemented will be effective against all current or future security threats. For example, security measures may be breached as a result of technological error, computer viruses, or third-party action, including intentional misconduct by computer hackers, physical break-ins, the actions of state actors, industrial espionage, fraudulent inducement of employees, customers, or channel partners to disclose sensitive information such as user names or passwords, and employee, customer, or channel partner error or malfeasance. We have experienced attempts by third parties to identify and exploit product and service vulnerabilities, penetrate or bypass our security measures, and gain unauthorized access to our or our customers' or service providers' cloud offerings, networks, and other systems.

A security breach could result in unauthorized access to or disclosure, modification, misuse, loss, or destruction of our customers', prospects', vendors', or channel partners' data, our data (including our proprietary information, intellectual property, or trade secrets), or our cloud services offerings, networks, or other systems. Because there are many different security breach techniques and such techniques continue to evolve, we may be unable to anticipate, detect, or mitigate attempted security breaches and implement adequate preventative measures. Third parties may also conduct attacks designed to prevent access to critical data or systems through ransomware or temporarily deny customers access to our cloud services.

Any security breach or successful denial of service attack could result in a loss of customer confidence in the security of our offerings and damage to our brand, reduce the demand for our offerings, disrupt our normal business operations, require us to spend material resources to investigate or correct the breach, require us to notify affected customers or individuals and/or applicable regulators and others, and provide identity theft protection services to individuals under applicable laws, expose us to legal liabilities, including litigation, regulatory enforcement, and indemnity obligations, and materially adversely affect our revenue and operating results. These risks will increase as we continue to grow the number and scale of our cloud-based offerings, and process, store, and transmit increasingly large amounts of our customers', prospects', vendors', channel partners', and our own information and data, which may include proprietary or confidential data or personal or identifying information. Moreover, if a high-profile security breach occurs with respect to an industry peer, our customers and potential customers may lose trust in the security of business intelligence or analytics platforms generally, which could adversely impact our ability to retain existing customers or attract new ones.

Our intellectual property is valuable, and any inability to protect it could reduce the value of our products, services, and brand

We rely on a combination of copyrights, patents, trademarks, trade secrets, confidentiality procedures, and contractual commitments to protect our intellectual property worldwide. Despite our efforts, these measures can only provide limited protection. Unauthorized third parties may try to copy or reverse engineer portions of our products or otherwise obtain and use our intellectual property. Any intellectual property owned by us may be invalidated, circumvented, or challenged. Any of our pending or future intellectual property applications, whether or not currently being challenged, may not be issued with the scope we seek, if at all. Moreover, amendments to and developing jurisprudence regarding U.S. and international law may affect our ability to protect our intellectual property and defend against claims of infringement. In addition, although we generally enter into confidentiality agreements with our employees and contractors, our former employees and contractors may seek employment with our business partners, customers, or competitors, and there can be no assurance that the confidential nature of our intellectual property will be maintained. Furthermore, the laws of some countries do not provide the same level of protection of our intellectual property as do the laws of the United States. If we cannot protect our intellectual property against unauthorized copying or use, we may not remain competitive.

Third parties may claim we infringe their intellectual property rights

We periodically receive notices from third parties claiming we are infringing their intellectual property rights, principally patent and trademark rights. We expect the number of such claims will increase as we continue to expand our offerings and branding, the number of offerings and level of competition in our industry segments grow, the functionality of offerings overlaps, and the volume of issued patents, patent applications, and trademark registrations continues to increase. Responding to any infringement claim, regardless of its validity, could:

- be time-consuming, costly, and/or result in litigation;
- divert management's time and attention from developing our business;

- require us to pay monetary damages or enter into royalty and licensing agreements that we would not normally find acceptable;
- require us to stop selling certain of our offerings;
- require us to redesign certain of our offerings using alternative non-infringing technology or practices, which could require significant effort and expense;
- require us to rename certain of our offerings or entities; or
- require us to satisfy indemnification obligations to our customers and channel partners.

Additionally, while we monitor our use of third-party software, including open source software, we cannot assure you that our processes for controlling such use in our products will be effective. If we inadvertently embed certain types of open source software into one or more of our products, fail to comply with the terms and conditions associated with the use of various open source software, or if third-party software that we license is found to infringe intellectual property rights of others, we could subject ourselves to infringement liability and be required to re-engineer our products, discontinue the sale of our products if re-engineering could not be accomplished on a timely or cost-effective basis, or make available to certain third parties or generally available, in source code form, our proprietary code, any of which could materially adversely affect our business, operating results, and financial condition.

If a successful infringement claim is made against us and we fail to develop or license a substitute technology or brand name, as applicable, our business, results of operations, financial condition, or cash flows could be materially adversely affected.

Because of the rights of our two classes of common stock and because we are controlled by Michael J. Saylor, who beneficially owns the majority of our class B common stock, Mr. Saylor could transfer control of MicroStrategy to a third party without the approval of our Board of Directors or our other stockholders, prevent a third party from acquiring us, or limit the ability of our other stockholders to influence corporate matters

We have two classes of common stock: class A common stock and class B common stock. Holders of our class A common stock generally have the same rights as holders of our class B common stock, except that holders of class A common stock have one vote per share while holders of class B common stock have ten votes per share. As of July 16, 2019, holders of our class B common stock owned 2,035,184 shares of class B common stock, or 71.3% of the total voting power. As of July 16, 2019, Mr. Saylor, our Chairman of the Board of Directors, President & Chief Executive Officer, beneficially owned 2,011,668 shares of class B common stock, or 70.4% of the total voting power. Accordingly, Mr. Saylor can control MicroStrategy through his ability to determine the outcome of elections of our directors, amend our certificate of incorporation and by-laws, and take other actions requiring the vote or consent of stockholders, including mergers, going-private transactions, and other extraordinary transactions and their terms.

Our certificate of incorporation allows holders of class B common stock to transfer shares of class B common stock, subject to the approval of stockholders holding a majority of the outstanding class B common stock. Mr. Saylor or a group of stockholders holding a majority of the outstanding class B common stock could, without the approval of our Board of Directors or our other stockholders, transfer voting control of MicroStrategy to a third party. Such a transfer of control could have a material adverse effect on our business, operating results, and financial condition. Mr. Saylor or a group of stockholders holding a majority of the outstanding class B common stock could also prevent a change of control of MicroStrategy, regardless of whether holders of class A common stock might otherwise receive a premium for their shares over the then current market price. In addition, this concentrated control limits stockholders' ability to influence corporate matters and, as a result, we may take actions that our non-controlling stockholders do not view as beneficial or that conflict with their interests. As a result, the market price of our class A common stock could be materially adversely affected.

Our status as a “controlled company” could make our class A common stock less attractive to some investors or otherwise materially adversely affect our stock price

Because we qualify as a “controlled company” under the corporate governance rules for Nasdaq-listed companies, we are not required to have independent directors comprise a majority of our Board of Directors. Additionally, our Board of Directors is not required to have an independent compensation or nominating committee, or to have the independent directors exercise the nominating function. We are also not required to have the compensation of our executive officers be determined by a compensation committee of independent directors. In addition, we are not required to empower our Compensation Committee with the authority to engage the services of any compensation consultants, legal counsel, or other advisors, or to have the Compensation Committee assess the independence of compensation consultants, legal counsel, and other advisors that it engages.

In light of our status as a controlled company, our Board of Directors has determined not to establish an independent nominating committee or have its independent directors exercise the nominating function and has elected instead to have the Board of Directors be directly responsible for nominating members of the Board. A majority of our Board of Directors is currently comprised of independent directors, and our Board of Directors has established a Compensation Committee comprised entirely of independent directors. The Compensation Committee determines the compensation of our Chief Executive Officer. However, our Board of Directors has authorized our Chief Executive Officer to determine the compensation of executive officers other than himself, rather than having such compensation determined by the Compensation Committee, except that certain performance-based executive officer compensation is determined by the Compensation Committee. Awards under our 2013 Equity Plan are also approved by the Compensation Committee. Additionally, while our Compensation Committee is empowered with the authority to retain and terminate outside counsel, compensation consultants, and other experts or consultants, it is not required to assess their independence.

Although currently a majority of our Board of Directors is comprised of independent directors and the Compensation Committee is comprised entirely of independent directors, we may elect in the future not to have independent directors constitute a majority of the Board of Directors or the Compensation Committee, our Chief Executive Officer's compensation determined by a compensation committee of independent directors, or a compensation committee of the Board of Directors at all.

Accordingly, should the interests of our controlling stockholder differ from those of other stockholders, the other stockholders may not have the same protections that are afforded to stockholders of companies that are required to follow all of the corporate governance rules for Nasdaq-listed companies. Our status as a controlled company could make our class A common stock less attractive to some investors or otherwise materially adversely affect our stock price.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the three months ended June 30, 2019, we did not repurchase any equity securities registered by us pursuant to Section 12 of the Exchange Act. See Note 7, Treasury Stock, to the Consolidated Financial Statements in "Part I. Item 1. Financial Statements" for further information regarding our Share Repurchase Program.

Item 5. Other Information

On July 30, 2019, we issued a press release announcing the Company's financial results for the quarter ended June 30, 2019. A copy of this press release is attached as Exhibit 99.1 to this Quarterly Report. The information in this Item 5 (including Exhibit 99.1) shall not be deemed "filed" for purposes of Section 18 of the Exchange Act or otherwise subject to the liabilities of that section, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933, as amended, or the Exchange Act, except as expressly set forth by specific reference in such a filing.

Item 6. Exhibits

INDEX TO EXHIBITS

| Exhibit Number | Description |
|-----------------------|---|
| 3.1 | <u>Second Restated Certificate of Incorporation of the registrant (incorporated herein by reference to Exhibit 3.1 to the registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2003 (File No. 000-24435)).</u> |
| 3.2 | <u>Amended and Restated By-Laws of the registrant (incorporated herein by reference to Exhibit 3.1 to the registrant's Current Report on Form 8-K filed with the SEC on January 30, 2015 (File No. 000-24435)).</u> |
| 4.1 | <u>Form of Certificate of Class A Common Stock of the registrant (incorporated herein by reference to Exhibit 4.1 to the registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2003 (File No. 000-24435)).</u> |
| 31.1 | <u>Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Chairman of the Board of Directors, President & Chief Executive Officer.</u> |
| 31.2 | <u>Certification pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Senior Executive Vice President, Chief Operating Officer & Chief Financial Officer.</u> |
| 32.1 | <u>Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> |
| 99.1 | <u>Press release, dated July 30, 2019, regarding the Company's financial results for the quarter ended June 30, 2019.</u> |
| 101.INS | XBRL Instance Document. The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document. |
| 101.SCH | XBRL Taxonomy Extension Schema. |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase. |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase. |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase. |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase. |

SIGNATURES

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

MICROSTRATEGY INCORPORATED

By: /s/ Michael J. Saylor
Michael J. Saylor
Chairman of the Board of Directors,
President & Chief Executive Officer

By: /s/ Phong Le
Phong Le
Senior Executive Vice President,
Chief Operating Officer & Chief Financial Officer

Date: July 30, 2019

CERTIFICATION

I, Michael J. Saylor, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of MicroStrategy Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: July 30, 2019

/s/ Michael J. Saylor
Michael J. Saylor
Chairman of the Board of Directors,
President & Chief Executive Officer

CERTIFICATION

I, Phong Le, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of MicroStrategy Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: July 30, 2019

/s/ Phong Le

Phong Le

Senior Executive Vice President,
Chief Operating Officer & Chief Financial Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of MicroStrategy Incorporated (the "Company") for the quarter ended June 30, 2019, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, the Chief Executive Officer of the Company and the Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge on the date hereof:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: July 30, 2019

/s/ Michael J. Saylor
Michael J. Saylor
Chairman of the Board of Directors,
President & Chief Executive Officer

Dated: July 30, 2019

/s/ Phong Le
Phong Le
Senior Executive Vice President,
Chief Operating Officer & Chief Financial Officer

Contact:

MicroStrategy Incorporated
Investor Relations
ir@microstrategy.com
(703) 848-8600

MicroStrategy Announces Second Quarter 2019 Financial Results

TYSONS CORNER, Va., July 30, 2019 - MicroStrategy® Incorporated (Nasdaq: MSTR), a leading worldwide provider of enterprise analytics and mobility software, today announced financial results for the three-month period ended June 30, 2019 (the second quarter of its 2019 fiscal year).

Second Quarter 2019 Financial Highlights

- **Revenues:** Total revenues for the second quarter of 2019 were \$117.7 million, a 2.4% decrease or a 0.4% increase on a non-GAAP constant currency basis compared to the second quarter of 2018. Product licenses and subscription services revenues for the second quarter of 2019 were \$27.2 million, a 1.3% increase or a 3.9% increase on a constant currency basis compared to the second quarter of 2018. Product support revenues for the second quarter of 2019 were \$73.0 million, a 0.9% decrease or a 1.9% increase on a constant currency basis compared to the second quarter of 2018. Other services revenues for the second quarter of 2019 were \$17.5 million, a 12.5% decrease or a 9.5% decrease on a constant currency basis compared to the second quarter of 2018.
- **Gross Profit:** Gross profit for the second quarter of 2019 was \$92.4 million, representing a 78.5% gross margin, compared to a gross margin of 79.2% in the second quarter of 2018.
- **Operating Expenses:** Operating expenses for the second quarter of 2019 were \$97.2 million versus \$97.4 million for the second quarter of 2018, essentially flat year over year.
- **Loss from Operations:** Loss from operations for the second quarter of 2019 was \$4.8 million versus \$1.8 million for the second quarter of 2018. Non-GAAP loss from operations, which excludes share-based compensation expense, was \$1.8 million for the second quarter of 2019 versus non-GAAP income from operations of \$1.6 million for the second quarter of 2018.
- **Net Income:** Net income for the second quarter of 2019 was \$20.4 million, or \$1.98 per share on a diluted basis, as compared to net income of \$4.8 million, or \$0.42 per share on a diluted basis, for the second quarter of 2018. In the second quarter of 2019, MicroStrategy completed the sale of its Voice.com domain name for a gain of \$21.8 million, net of tax (the "Domain Name Sale"). Excluding the impact of the Domain Name Sale, non-GAAP net loss for the second quarter of 2019 was \$1.4 million, or \$0.14 per share on a diluted basis.
- **Cash and Short-term Investments:** As of June 30, 2019, MicroStrategy had cash and cash equivalents and short-term investments of \$574.8 million, as compared to \$576.1 million as of December 31, 2018, a decrease of \$1.3 million.

The tables at the end of this press release include a reconciliation of GAAP to non-GAAP financial measures for the three and six months ended June 30, 2019 and 2018. An explanation of non-GAAP financial measures is also included under the heading "Non-GAAP Financial Measures" below.

MicroStrategy adopted Accounting Standards Update No. 2016-02, *Leases (Topic 842)*, and its subsequent amendments (“ASU 2016-02”), effective January 1, 2019. Comparative prior period consolidated financial statements have not been restated and are not directly comparable to the current period consolidated financial statements.

MicroStrategy uses its Intelligent Enterprise™ platform across the enterprise and has created an interactive dossier with quarterly financial performance data. Anyone can access [the MSTR Financials dossier](#) via a web browser, or by downloading the MicroStrategy Library™ app on an iOS or Android device. To download the native apps, visit [MicroStrategy Library for iPad](#), [MicroStrategy Library for iPhone](#), or [MicroStrategy Library for Android tablet and smartphone](#).

Recent Business Highlights

MicroStrategy has been successfully driving its growth and productivity initiatives throughout the first half of 2019, and its initiatives around the MicroStrategy 2019™ platform, cloud, and customer adoption have been gaining more traction.

“I am very pleased with our accomplishments in the second quarter of 2019,” said Michael J. Saylor, CEO, MicroStrategy Incorporated. “The MicroStrategy 2019 platform won multiple industry awards, we have seen increased demand for our innovative Cloud and HyperIntelligence™ offerings, and we have improved key operational metrics for our business at the same time. Considering these accomplishments, I believe there is now a tremendous opportunity for MicroStrategy to take advantage of the dislocations that Tableau is likely to experience as a result of its pending acquisition by Salesforce.”

The following are some key business highlights from the second quarter of 2019:

- MicroStrategy announced the general availability of MicroStrategy 2019 Update 2, adding powerful new capabilities and products to the industry’s first and only platform for Federated Analytics, Transformational Mobility, and HyperIntelligence. The latest update expands the platform’s suite of HyperIntelligence products to enrich web browsing, accelerate access to intuitive intelligence on iOS and Android devices, and add windows of contextual insights to email on Outlook. The new update also delivers powerful enhancements designed to augment user productivity on popular BI tools including [Tableau](#), [Power BI](#), and Qlik, putting trusted insights into the hands of a larger number of users within the enterprise. The HyperIntelligence for Mobile app can be easily downloaded and installed from the [Google Play store](#) and [Apple AppStore](#).
 - MicroStrategy 2019 was recognized by Gartner, Inc. with the highest product scores across four use cases in the “[Critical Capabilities for Analytics and Business Intelligence Platforms](#)” report.¹ According to Gartner’s findings, MicroStrategy ranks:
 - #1 in Agile, Centralized BI Provisioning Use Case, scoring 4.34 (out of 5)
 - #1 in Governed Data Discovery Use Case, scoring 4.24 (out of 5)
 - #1 in OEM or Embedded BI Use Case, scoring 4.64 (out of 5)
 - #1 in Extranet Deployment Use Case, scoring 4.38 (out of 5)
 - #2 in Decentralized Analytics Use Case, scoring 4.23 (out of 5)
 - MicroStrategy announced that the MicroStrategy Analytics Platform™ in the cloud is available on the Federal Risk and Authorization Management Program (FedRAMP) marketplace via IntelliCog Enterprise Cloud Analytics. With this first and only FedRAMP-ready enterprise analytics solution in the cloud, government agencies can rapidly adapt from old, insecure legacy IT to mission-enabling, secure, and cost-effective cloud-based IT.
-

- To promote adoption of its award-winning MicroStrategy 2019 platform within the existing installed base, MicroStrategy bundled expert services into its premium support offerings and issued complimentary upgrades to its largest customers. MicroStrategy also launched the MicroStrategy Elite Support program, which includes 400 hours of platform upgrade and advisory services annually.
- Following the announcements of the acquisitions of Tableau by Salesforce and Looker by Google, MicroStrategy reiterated its belief that its platform offering is a better long-term solution for organizations caught in the analytics industry upheaval. MicroStrategy's independence, longevity, focus, and innovation uniquely position MicroStrategy as a preferred partner for companies seeking a better, long-term alternative for their analytics and mobility needs.
- MicroStrategy sold the Voice.com domain name for \$30 million in cash in a transaction facilitated by GoDaddy. MicroStrategy holds more than a dozen evocative and powerful domain names. While MicroStrategy's focus continues to be on its core analytics and mobility business, it is open to leveraging these domain names in equity or other strategic transactions with well-funded parties. To learn more about these domain names, please visit www.microstrategy.com/domains.

[1] Gartner, Critical Capabilities for Analytics and Business Intelligence Platforms, James Richardson, Rita Sallam, Austin Kronz, 14 May 2019.

Gartner does not endorse any vendor, product or service depicted in its research publications, and does not advise technology users to select only those vendors with the highest ratings or other designation. Gartner research publications consist of the opinions of Gartner's research organization and should not be construed as statements of fact. Gartner disclaims all warranties, express or implied, with respect to this research, including any warranties of merchantability or fitness for a particular purpose.

Conference Call

MicroStrategy will be discussing its second quarter 2019 financial results on a conference call today beginning at approximately 5:00 p.m. EDT. To access the conference call, dial (844) 824-7425 (domestically) or (716) 220-9429 (internationally) and use conference ID 9389810. A live and archived webcast will be available under the "Events" section on MicroStrategy's investor relations website at <https://ir.microstrategy.com/events-presentations>. A replay of the conference call will be available beginning approximately two hours after the call concludes until August 6, 2019 at (855) 859-2056 (domestically) or (404) 537-3406 (internationally) using the passcode 9389810.

Non-GAAP Financial Measures

MicroStrategy is providing supplemental financial measures for (i) (loss) income from operations that excludes the impact of share-based compensation arrangements, (ii) net (loss) income and diluted (loss) earnings per share that exclude the impact from the Domain Name Sale, and (iii) revenues that exclude foreign currency exchange rate fluctuations. These supplemental financial measures are not measurements of financial performance under generally accepted accounting principles in the United States ("GAAP") and, as a result, these supplemental financial measures may not be comparable to similarly titled measures of other companies. Management uses these non-GAAP financial measures internally to help understand, manage, and evaluate business performance and to help make operating decisions.

MicroStrategy believes that these non-GAAP financial measures are also useful to investors and analysts in comparing its performance across reporting periods on a consistent basis. The first supplemental financial measure excludes a significant non-cash expense that MicroStrategy believes is not reflective of its general business performance, and for which the accounting requires significant management judgment and the resulting share-based compensation expense could vary significantly in comparison to other companies. The second category of supplemental financial measures excludes the impact from the Domain Name Sale, which is outside of MicroStrategy's normal business operations. The third category of supplemental financial measures excludes changes resulting from fluctuations in foreign currency exchange rates so that results may be compared to the same period in the prior year on a "constant currency" basis. MicroStrategy believes the use of these non-GAAP financial measures can also facilitate comparison of MicroStrategy's operating results to those of its competitors.

About MicroStrategy Incorporated

MicroStrategy (Nasdaq: MSTR) is a leading worldwide provider of enterprise analytics and mobility software and services. Our mission is to make every enterprise a more Intelligent Enterprise. MicroStrategy 2019 delivers modern analytics on an open, comprehensive enterprise platform designed to drive business results with Federated Analytics, Transformational Mobility, and HyperIntelligence. To learn more, visit [MicroStrategy](#) online, and follow us on [LinkedIn](#), [Twitter](#), and [Facebook](#).

MicroStrategy, Intelligent Enterprise, MicroStrategy Library, MicroStrategy 2019, HyperIntelligence, and MicroStrategy Analytics Platform are either trademarks or registered trademarks of MicroStrategy Incorporated in the United States and certain other countries. Other product and company names mentioned herein may be the trademarks of their respective owners.

This press release may include statements that may constitute “forward-looking statements,” including estimates of future business prospects or financial results and statements containing the words “believe,” “estimate,” “project,” “expect” or similar expressions. Forward-looking statements inherently involve risks and uncertainties that could cause actual results of MicroStrategy Incorporated and its subsidiaries (collectively, the “Company”) to differ materially from the forward-looking statements. Factors that could contribute to such differences include: the extent and timing of market acceptance of MicroStrategy’s new offerings, including MicroStrategy 2019; the Company’s ability to recognize revenue or deferred revenue through delivery of products or satisfactory performance of services; continued acceptance of the Company’s other products in the marketplace; fluctuations in tax benefits or provisions, including as a result of changes to U.S. federal tax laws; the timing of significant orders; delays in or the inability of the Company to develop or ship new products; competitive factors; general economic conditions; currency fluctuations; and other risks detailed in the Company’s registration statements and periodic reports filed with the Securities and Exchange Commission. The Company undertakes no obligation to update these forward-looking statements for revisions or changes after the date of this release.

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MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|-----------------|------------------|-----------------|
| | June 30, | | June 30, | |
| | 2019 | 2018 | 2019 | 2018 |
| | (unaudited) | (unaudited) | (unaudited) | (unaudited) |
| Revenues | | | | |
| Product licenses | \$ 20,121 | \$ 19,292 | \$ 38,412 | \$ 36,593 |
| Subscription services | 7,104 | 7,584 | 14,248 | 15,246 |
| Total product licenses and subscription services | 27,225 | 26,876 | 52,660 | 51,839 |
| Product support | 72,978 | 73,676 | 144,428 | 148,091 |
| Other services | 17,534 | 20,050 | 36,015 | 43,639 |
| Total revenues | 117,737 | 120,602 | 233,103 | 243,569 |
| Cost of revenues | | | | |
| Product licenses | 552 | 1,667 | 1,071 | 3,878 |
| Subscription services | 3,489 | 3,445 | 7,087 | 6,694 |
| Total product licenses and subscription services | 4,041 | 5,112 | 8,158 | 10,572 |
| Product support | 7,721 | 4,810 | 14,788 | 9,606 |
| Other services | 13,588 | 15,118 | 28,577 | 30,047 |
| Total cost of revenues | 25,350 | 25,040 | 51,523 | 50,225 |
| Gross profit | 92,387 | 95,562 | 181,580 | 193,344 |
| Operating expenses | | | | |
| Sales and marketing | 48,273 | 50,978 | 97,033 | 102,313 |
| Research and development | 27,764 | 25,082 | 55,979 | 48,642 |
| General and administrative | 21,180 | 21,299 | 43,784 | 43,471 |
| Total operating expenses | 97,217 | 97,359 | 196,796 | 194,426 |
| Loss from operations | (4,830) | (1,797) | (15,216) | (1,082) |
| Interest income, net | 3,013 | 3,223 | 5,579 | 5,257 |
| Other income, net | 29,431 | 4,461 | 28,835 | 2,867 |
| Income before income taxes | 27,614 | 5,887 | 19,198 | 7,042 |
| Provision for income taxes | 7,220 | 1,059 | 6,710 | 541 |
| Net income | \$ 20,394 | \$ 4,828 | \$ 12,488 | \$ 6,501 |
| Basic earnings per share (1): | \$ 1.99 | \$ 0.42 | \$ 1.21 | \$ 0.57 |
| Weighted average shares outstanding used in computing basic earnings per share | 10,240 | 11,459 | 10,283 | 11,453 |
| Diluted earnings per share (1): | \$ 1.98 | \$ 0.42 | \$ 1.21 | \$ 0.57 |
| Weighted average shares outstanding used in computing diluted earnings per share | 10,310 | 11,493 | 10,350 | 11,488 |

(1) Basic and fully diluted earnings per share for class A and class B common stock are the same.

MICROSTRATEGY INCORPORATED
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

| | June 30, 2019 (unaudited) | December 31, 2018* |
|--|---------------------------------|-----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 261,497 | \$ 109,924 |
| Restricted cash | 1,039 | 862 |
| Short-term investments | 313,349 | 466,186 |
| Accounts receivable, net | 129,144 | 171,359 |
| Prepaid expenses and other current assets | 22,259 | 30,068 |
| Total current assets | 727,288 | 778,399 |
| Property and equipment, net | 54,285 | 51,919 |
| Right-of-use assets | 89,631 | 0 |
| Deposits and other assets | 7,981 | 8,134 |
| Deferred tax assets, net | 20,535 | 17,316 |
| Total Assets | \$ 899,720 | \$ 855,768 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities | | |
| Accounts payable, accrued expenses, and operating lease liabilities | \$ 32,300 | \$ 33,684 |
| Accrued compensation and employee benefits | 41,561 | 48,045 |
| Deferred revenue and advance payments | 176,786 | 176,540 |
| Total current liabilities | 250,647 | 258,269 |
| Deferred revenue and advance payments | 4,175 | 6,469 |
| Operating lease liabilities | 108,183 | 0 |
| Other long-term liabilities | 33,990 | 61,262 |
| Deferred tax liabilities | 36 | 37 |
| Total Liabilities | 397,031 | 326,037 |
| Stockholders' Equity | | |
| Preferred stock undesignated, \$0.001 par value; 5,000 shares authorized; no shares issued or outstanding | 0 | 0 |
| Class A common stock, \$0.001 par value; 330,000 shares authorized; 15,853 shares issued and 8,205 shares outstanding, and 15,837 shares issued and 8,552 shares outstanding, respectively | 16 | 16 |
| Class B convertible common stock, \$0.001 par value; 165,000 shares authorized; 2,035 shares issued and outstanding, and 2,035 shares issued and outstanding, respectively | 2 | 2 |
| Additional paid-in capital | 584,764 | 576,957 |
| Treasury stock, at cost; 7,648 shares and 7,285 shares, respectively | (634,405) | (586,161) |
| Accumulated other comprehensive loss | (9,310) | (10,217) |
| Retained earnings | 561,622 | 549,134 |
| Total Stockholders' Equity | 502,689 | 529,731 |
| Total Liabilities and Stockholders' Equity | 899,720 | 855,768 |

* Derived from audited financial statements.

MICROSTRATEGY INCORPORATED
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | Six Months Ended June 30, | |
|---|------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) |
| Operating activities: | | |
| Net income | \$ 12,488 | \$ 6,501 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 7,687 | 3,870 |
| Write-offs and sales allowances | 796 | 948 |
| Net realized loss on short-term investments | 41 | 0 |
| Deferred taxes | (3,219) | (5,758) |
| Share-based compensation expense | 6,053 | 8,121 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 5,985 | 5,044 |
| Prepaid expenses and other current assets | 7,089 | 453 |
| Deposits and other assets | 96 | (344) |
| Accounts payable and accrued expenses | (8,396) | (7,775) |
| Accrued compensation and employee benefits | (8,082) | (3,015) |
| Deferred revenue and advance payments | 33,489 | 10,502 |
| Operating lease liabilities | (4,316) | 0 |
| Other long-term liabilities | (509) | 4,780 |
| Net cash provided by operating activities | <u>49,202</u> | <u>23,327</u> |
| Investing activities: | | |
| Proceeds from redemption of short-term investments | 369,603 | 245,680 |
| Purchases of property and equipment | (8,432) | (2,644) |
| Purchases of short-term investments | (212,248) | (596,376) |
| Net cash provided by (used in) investing activities | <u>148,923</u> | <u>(353,340)</u> |
| Financing activities: | | |
| Proceeds from sale of class A common stock under exercise of employee stock options | 1,836 | 2,471 |
| Purchases of treasury stock | (48,244) | 0 |
| Payments on capital lease obligations and other financing arrangements prior to the adoption of ASU 2016-02 | 0 | (9) |
| Net cash (used in) provided by financing activities | <u>(46,408)</u> | <u>2,462</u> |
| Effect of foreign exchange rate changes on cash, cash equivalents, and restricted cash | <u>33</u> | <u>(2,240)</u> |
| Net increase (decrease) in cash, cash equivalents, and restricted cash | <u>151,750</u> | <u>(329,791)</u> |
| Cash, cash equivalents, and restricted cash, beginning of period | <u>110,786</u> | <u>421,182</u> |
| Cash, cash equivalents, and restricted cash, end of period | <u>\$ 262,536</u> | <u>\$ 91,391</u> |

MICROSTRATEGY INCORPORATED
REVENUE AND COST OF REVENUE DETAIL
(in thousands)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-------------------------|------------------------------|--------------------------|
| | 2019 (unaudited) | 2018 (unaudited) | 2019 (unaudited) | 2018 (unaudited) |
| Revenues | | | | |
| Product licenses and subscription services: | | | | |
| Product licenses | \$ 20,121 | \$ 19,292 | \$ 38,412 | \$ 36,593 |
| Subscription services | 7,104 | 7,584 | 14,248 | 15,246 |
| Total product licenses and subscription services | <u>27,225</u> | <u>26,876</u> | <u>52,660</u> | <u>51,839</u> |
| Product support | 72,978 | 73,676 | 144,428 | 148,091 |
| Other services: | | | | |
| Consulting | 15,494 | 17,710 | 32,097 | 38,997 |
| Education | 2,040 | 2,340 | 3,918 | 4,642 |
| Total other services | <u>17,534</u> | <u>20,050</u> | <u>36,015</u> | <u>43,639</u> |
| Total revenues | <u>117,737</u> | <u>120,602</u> | <u>233,103</u> | <u>243,569</u> |
| Cost of revenues | | | | |
| Product licenses and subscription services: | | | | |
| Product licenses | 552 | 1,667 | 1,071 | 3,878 |
| Subscription services | 3,489 | 3,445 | 7,087 | 6,694 |
| Total product licenses and subscription services | <u>4,041</u> | <u>5,112</u> | <u>8,158</u> | <u>10,572</u> |
| Product support | 7,721 | 4,810 | 14,788 | 9,606 |
| Other services: | | | | |
| Consulting | 11,909 | 13,542 | 24,894 | 26,863 |
| Education | 1,679 | 1,576 | 3,683 | 3,184 |
| Total other services | <u>13,588</u> | <u>15,118</u> | <u>28,577</u> | <u>30,047</u> |
| Total cost of revenues | <u>25,350</u> | <u>25,040</u> | <u>51,523</u> | <u>50,225</u> |
| Gross profit | <u>\$ 92,387</u> | <u>\$ 95,562</u> | <u>\$ 181,580</u> | <u>\$ 193,344</u> |

MICROSTRATEGY INCORPORATED
DEFERRED REVENUE DETAIL
(in thousands)

| | June 30, 2019 <small>(unaudited)</small> | December 31, 2018* | June 30, 2018 <small>(unaudited)</small> |
|---|--|-----------------------|--|
| Current: | | | |
| Deferred product licenses revenue | \$ 633 | \$ 1,768 | \$ 1,819 |
| Deferred subscription services revenue | 15,393 | 13,508 | 13,847 |
| Deferred product support revenue | 152,866 | 152,501 | 151,909 |
| Deferred other services revenue | 7,894 | 8,763 | 7,783 |
| Total current deferred revenue and advance payments | <u>\$ 176,786</u> | <u>\$ 176,540</u> | <u>\$ 175,358</u> |
| Non-current: | | | |
| Deferred product licenses revenue | \$ 405 | \$ 542 | \$ 794 |
| Deferred subscription services revenue | 116 | 2,384 | 9 |
| Deferred product support revenue | 3,083 | 3,091 | 3,950 |
| Deferred other services revenue | 571 | 452 | 1,063 |
| Total non-current deferred revenue and advance payments | <u>\$ 4,175</u> | <u>\$ 6,469</u> | <u>\$ 5,816</u> |
| Total current and non-current: | | | |
| Deferred product licenses revenue | \$ 1,038 | \$ 2,310 | \$ 2,613 |
| Deferred subscription services revenue | 15,509 | 15,892 | 13,856 |
| Deferred product support revenue | 155,949 | 155,592 | 155,859 |
| Deferred other services revenue | 8,465 | 9,215 | 8,846 |
| Total current and non-current deferred revenue and advance payments | <u>\$ 180,961</u> | <u>\$ 183,009</u> | <u>\$ 181,174</u> |

* Derived from audited financial statements.

MICROSTRATEGY INCORPORATED
RECONCILIATION OF GAAP TO NON-GAAP MEASURES
EXCLUSION OF SHARE-BASED COMPENSATION EXPENSE
(in thousands)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|---------------------|------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) | 2019 (unaudited) | 2018 (unaudited) |
| Reconciliation of non-GAAP (loss) income from operations: | | | | |
| Loss from operations | \$ (4,830) | \$ (1,797) | \$ (15,216) | \$ (1,082) |
| Share-based compensation expense | 3,036 | 3,378 | 6,053 | 8,121 |
| Non-GAAP (loss) income from operations | <u>\$ (1,794)</u> | <u>\$ 1,581</u> | <u>\$ (9,163)</u> | <u>\$ 7,039</u> |

MICROSTRATEGY INCORPORATED
RECONCILIATION OF GAAP TO NON-GAAP MEASURES
EXCLUSION OF DOMAIN NAME SALE
(in thousands, except per share data)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|---------------------|------------------------------|---------------------|
| | 2019 (unaudited) | 2018 (unaudited) | 2019 (unaudited) | 2018 (unaudited) |
| Reconciliation of non-GAAP net (loss) income: | | | | |
| Net income | \$ 20,394 | \$ 4,828 | \$ 12,488 | \$ 6,501 |
| Gain from Domain Name Sale, net of tax | (21,778) | 0 | (21,778) | 0 |
| Non-GAAP net (loss) income | <u>\$ (1,384)</u> | <u>\$ 4,828</u> | <u>\$ (9,290)</u> | <u>\$ 6,501</u> |
| Reconciliation of non-GAAP diluted (loss) earnings per share: | | | | |
| Diluted earnings per share | \$ 1.98 | \$ 0.42 | \$ 1.21 | \$ 0.57 |
| Gain from Domain Name Sale, net of tax (per diluted share) | (2.12) | 0.00 | (2.11) | 0.00 |
| Non-GAAP diluted (loss) earnings per share | <u>\$ (0.14)</u> | <u>\$ 0.42</u> | <u>\$ (0.90)</u> | <u>\$ 0.57</u> |

MICROSTRATEGY INCORPORATED
RECONCILIATION OF GAAP TO NON-GAAP MEASURES
CONSTANT CURRENCY
(in thousands)

Three Months Ended
June 30,
(unaudited)

| | GAAP | Foreign Currency Exchange Rate Impact (1) | Non-GAAP Constant Currency (2) | GAAP | GAAP % Change | Non-GAAP Constant Currency % Change (3) |
|--|----------------|--|--------------------------------------|----------------|------------------|--|
| | 2019 | 2019 | 2019 | 2018 | 2019 | 2019 |
| Revenues | | | | | | |
| Product licenses | \$ 20,121 | \$ (616) | \$ 20,737 | \$ 19,292 | 4.3% | 7.5% |
| Subscription services | 7,104 | (93) | 7,197 | 7,584 | -6.3% | -5.1% |
| Total product licenses and subscription services | 27,225 | (709) | 27,934 | 26,876 | 1.3% | 3.9% |
| Product support | 72,978 | (2,091) | 75,069 | 73,676 | -0.9% | 1.9% |
| Other services | 17,534 | (603) | 18,137 | 20,050 | -12.5% | -9.5% |
| Total revenues | 117,737 | (3,403) | 121,140 | 120,602 | -2.4% | 0.4% |

- (1) The “Foreign Currency Exchange Rate Impact” reflects the estimated impact from fluctuations in foreign currency exchange rates on international revenues. It shows the increase (decrease) in international revenues from the same period in the prior year, based on comparisons to the prior year quarterly average foreign currency exchange rates. The term “international” refers to operations outside of the United States and Canada.
- (2) The “Non-GAAP Constant Currency” reflects the current period GAAP amount, less the Foreign Currency Exchange Rate Impact.
- (3) The “Non-GAAP Constant Currency % Change” reflects the percentage change between the current period Non-GAAP Constant Currency amount and the GAAP amount for the same period in the prior year.

MICROSTRATEGY INCORPORATED
WORLDWIDE EMPLOYEE HEADCOUNT

| | <u>June 30, 2019</u> | <u>March 31, 2019</u> | <u>December 31, 2018</u> | <u>September 30, 2018</u> | <u>June 30, 2018</u> |
|----------------------------|--------------------------|---------------------------|------------------------------|-------------------------------|--------------------------|
| Subscription services | 62 | 54 | 56 | 55 | 54 |
| Product support | 234 | 224 | 202 | 194 | 184 |
| Consulting | 404 | 429 | 452 | 458 | 443 |
| Education | 40 | 50 | 47 | 44 | 39 |
| Sales and marketing | 637 | 675 | 707 | 699 | 687 |
| Research and development | 764 | 733 | 716 | 688 | 651 |
| General and administrative | 336 | 329 | 348 | 326 | 322 |
| Total headcount | <u>2,477</u> | <u>2,494</u> | <u>2,528</u> | <u>2,464</u> | <u>2,380</u> |