

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 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, 2018

OR

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

For the transition period from _____ to _____

Commission File Number: 001-38107

ShotSpotter, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware
**(State or other jurisdiction of
incorporation or organization)**
7979 Gateway Blvd., Suite 210
Newark, California
(Address of principal executive offices)

47-0949915
**(I.R.S. Employer
Identification No.)**

94560
(Zip Code)

Registrant's telephone number, including area code: (510) 794-3100

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input type="checkbox"/>
Emerging growth company	<input checked="" 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 August 2, 2018, the registrant had 10,772,311 shares of common stock, \$0.005 par value per share, outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

ShotSpotter, Inc.
Condensed Consolidated Balance Sheets
(In thousands)

	June 30, 2018 <u>(Unaudited)</u>	December 31, 2017
Assets		
Current assets		
Cash and cash equivalents	\$ 14,811	\$ 19,567
Accounts receivable and unbilled revenue	6,359	3,928
Prepaid expenses and other current assets	1,704	839
Restricted cash	60	30
Total current assets	<u>22,934</u>	<u>24,364</u>
Property and equipment, net	15,134	11,596
Intangible assets, net	95	95
Other assets	1,662	143
Total assets	<u>\$ 39,825</u>	<u>\$ 36,198</u>
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 2,732	\$ 1,627
Deferred revenue, short-term	16,230	15,780
Accrued expenses and other current liabilities	3,127	3,815
Total current liabilities	<u>22,089</u>	<u>21,222</u>
Deferred revenue, long-term	1,212	2,710
Other liabilities	91	104
Total liabilities	<u>23,392</u>	<u>24,036</u>
Stockholders' equity:		
Common stock	53	48
Additional paid-in capital	112,639	109,708
Accumulated deficit	(96,156)	(97,595)
Accumulated other comprehensive income (loss)	(103)	1
Total stockholders' equity	<u>16,433</u>	<u>12,162</u>
Total liabilities and stockholders' equity	<u>\$ 39,825</u>	<u>\$ 36,198</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Operations
(In thousands, except share and per share data)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Revenues	\$ 8,927	\$ 5,836	\$ 15,834	\$ 10,398
Costs				
Cost of revenues	3,589	2,687	6,897	5,362
Impairment of property and equipment	361	—	361	—
Total costs	<u>3,950</u>	<u>2,687</u>	<u>7,258</u>	<u>5,362</u>
Gross profit	4,977	3,149	8,576	5,036
Operating expenses				
Sales and marketing	2,195	1,369	3,749	2,477
Research and development	1,255	928	2,491	1,962
General and administrative	1,824	971	3,852	1,901
Total operating expenses	<u>5,274</u>	<u>3,268</u>	<u>10,092</u>	<u>6,340</u>
Operating loss	<u>(297)</u>	<u>(119)</u>	<u>(1,516)</u>	<u>(1,304)</u>
Other income (expense), net				
Remeasurement of convertible preferred stock warrant liability	—	(3,725)	—	(3,725)
Interest income (expense), net	22	(445)	49	(810)
Other expense, net	(76)	(17)	(75)	(28)
Total other income (expense), net	<u>(54)</u>	<u>(4,187)</u>	<u>(26)</u>	<u>(4,563)</u>
Loss before income taxes	(351)	(4,306)	(1,542)	(5,867)
Provision for income taxes	18	—	44	—
Net loss	<u>\$ (369)</u>	<u>\$ (4,306)</u>	<u>\$ (1,586)</u>	<u>\$ (5,867)</u>
Net loss per share, basic and diluted	<u>\$ (0.03)</u>	<u>\$ (1.16)</u>	<u>\$ (0.15)</u>	<u>\$ (2.19)</u>
Weighted average shares used in computing net loss per share, basic and diluted	<u>10,589,038</u>	<u>3,724,760</u>	<u>10,329,874</u>	<u>2,678,787</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Comprehensive Loss
(In thousands)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net loss	\$ (369)	\$ (4,306)	\$ (1,586)	\$ (5,867)
Other comprehensive income (loss):				
Change in foreign currency translation adjustment	(133)	(6)	(104)	(19)
Comprehensive loss	<u>\$ (502)</u>	<u>\$ (4,312)</u>	<u>\$ (1,690)</u>	<u>\$ (5,886)</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	<u>Six Months Ended June 30,</u>	
	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Net loss	\$ (1,586)	\$ (5,867)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,775	1,408
Impairment of property and equipment	361	—
Stock-based compensation	1,075	75
Amortization of debt issuance costs	—	84
Remeasurement of convertible preferred stock warrant liability	—	3,725
Changes in operating assets and liabilities:		
Accounts receivable and unbilled revenue	(2,431)	(666)
Prepaid expenses and other assets	(568)	(201)
Accounts payable	1,105	(307)
Accrued expenses and other current liabilities	(701)	(216)
Deferred revenue	134	3,049
Net cash provided by (used in) operating activities	<u>(836)</u>	<u>1,084</u>
Cash flows from investing activities:		
Purchase of property and equipment	(5,643)	(2,870)
Investment in intangible and other assets	(26)	(24)
Net cash used in investing activities	<u>(5,669)</u>	<u>(2,894)</u>
Cash flows from financing activities:		
Proceeds from initial public offering, net of commissions and discounts	—	32,426
Proceeds from notes payable	—	1,500
Payment of debt issuance costs	—	(30)
Payments of offering costs	—	(846)
Proceeds from exercise of stock options	450	10
Proceeds from exercise of warrants	989	—
Proceeds from Employee Stock Purchase Plan	421	—
Net cash provided by financing activities	<u>1,860</u>	<u>33,060</u>
Increase (decrease) in cash and cash equivalents	(4,645)	31,250
Effect of exchange rate on cash and cash equivalents	(81)	5
Cash, cash equivalents and restricted cash at beginning of year	19,597	3,895
Cash, cash equivalents and restricted cash at end of period	<u>\$ 14,871</u>	<u>\$ 35,150</u>
Supplemental cash flow disclosures:		
Cash paid for interest	\$ —	\$ 721
Supplemental disclosure of non-cash financing activities:		
Conversion of convertible preferred stock into common stock	—	\$ 42,075
Reclassification of convertible preferred stock warrant liability into additional paid-in capital	\$ —	\$ 5,711
Issuance of warrants in connection with the issuance of notes payable to a financial institution	\$ —	\$ 111
Deferred offering costs included in other assets	\$ 66	\$ 986

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Notes to Condensed Consolidated Financial Statements

Note 1. Organization and Description of Business

ShotSpotter, Inc. (the “Company”) provides gunshot detection solutions that help law enforcement officials and security personnel identify, locate and deter gun violence. The Company offers its software solutions on a SaaS-based subscription model to its customers.

The Company’s principal executive offices are located in Newark, California. The Company has one subsidiary, ShotSpotter (Pty) Ltd. formed in South Africa.

Note 2. Initial Public Offering

In June 2017, the Company completed its initial public offering (“IPO”) in which the Company sold 3,220,000 shares of its common stock at a price of \$11.00 per share. The Company received net proceeds of \$32.4 million, after underwriting discounts and commissions, which was recorded to additional paid-in capital. The Company’s common stock commenced trading on the NASDAQ Capital Market on June 7, 2017 under the trading symbol “SSTI.”

- Immediately prior to the IPO, all outstanding Series B-1 convertible preferred stock warrants were remeasured at fair value using the Black-Scholes model, resulting in a loss of \$3.7 million, which was recorded in other expense, net.
- Upon the closing of the IPO, the entire balance of \$5.7 million in convertible preferred stock warrant liability was reclassified to additional paid-in capital. All preferred stock warrants were converted into common stock warrants. In addition, the Company issued to the lead underwriter in the IPO a warrant to purchase up to 84,000 shares of its common stock. See Note 8, *Convertible Preferred Stock Warrants and Common Stock Warrants*, for further details regarding the warrants.
- Upon the closing of the IPO, all shares of the then-outstanding convertible preferred stock were converted into 4,689,753 shares of common stock. This resulted in a reclassification of \$42.1 million to additional paid-in capital.
- Offering costs incurred by the Company were approximately \$1.9 million, excluding underwriting commissions and discounts, which was recorded to additional paid-in capital.

Note 3. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures normally included in the consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated financial statements include the results of the Company and its wholly-owned subsidiary, ShotSpotter (Pty) Ltd. All significant intercompany transactions have been eliminated during consolidation.

The condensed consolidated balance sheet as of December 31, 2017, included herein, was derived from the audited consolidated financial statements as of that date, but does not include all disclosures including certain notes required by U.S. GAAP on an annual reporting basis.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations, comprehensive loss and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full year 2018 or any future period.

June 2017 Amended and Restated Certificate of Incorporation

Prior to the IPO, the Company's Board of Directors (the "Board") and stockholders approved an amendment (the "Charter Amendment") to the Pre-IPO Certificate (as defined below) and an amended and restated certificate of incorporation ("Post-IPO Certificate") that became effective on June 12, 2017. The Charter Amendment increased the number of authorized shares of common stock from 8,600,000 to 500,000,000. Under the Post-IPO Certificate, the Company is authorized to issue two classes of stock to be designated Common Stock and Preferred Stock. See Note 6, *Capital Stock*, for further details regarding these classes of stock.

March 2017 Amendment and Restatement of Certificate of Incorporation

On March 27, 2017, the Company's Board and stockholders approved an amendment and restatement of the Company's then-existing certificate of incorporation (as so amended and restated, the "Pre-IPO Certificate") to provide, among other changes, that each share of Series A-2 convertible preferred stock would automatically convert into 0.715548 shares of common stock upon the consummation of an initial public offering of the Company's capital stock. All share and per share data related to balance sheet and net loss information in the accompanying condensed consolidated financial statements and their related notes have been retroactively adjusted to give effect to the application of this conversion feature when presenting the Series A-2 convertible preferred stock on an as-converted basis.

The Pre-IPO Certificate also provided for (1) an increase in the total number of authorized shares to 14,550,000 and (2) an increase in the number of authorized shares of common stock to 8,600,000, in each case to accommodate the new conversion feature for the outstanding shares of Series A-2 convertible preferred stock.

All share and per share data in the accompanying condensed consolidated financial statements and their related notes for all periods presented have been retroactively adjusted to give effect to the reverse stock split.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates its significant estimates including the valuation of accounts receivable, the lives of tangible and intangible assets, stock-based compensation expense, preferred stock warrant liabilities, and accounting for revenue recognition and income taxes. Management bases its estimates on historical experience and on various other market-specific and relevant assumptions it believes to be reasonable under the circumstances. Actual results could differ from those estimates and such differences could be material to the Company's financial position and results of operations.

Revenue Recognition

The Company generates substantially all of its revenues from the sale of gunshot detection subscription services, in which gunshot data generated by Company-owned sensors and software is sold to customers through a cloud-based hosting application for a specified contract period. Typically, the initial contract period is one to five years in length. The subscription contract is generally noncancelable without cause. Generally, these service arrangements do not provide the customer with the right to take possession of the hardware or software supporting the subscription service at any time. A small portion of the Company's revenues are generated from the delivery of setup services to install Company-owned sensors in the customer's coverage area and other services including training and license to integrate with third-party applications.

The Company generally invoices customers for 50% of the total contract value when the contract is fully executed and for the remaining 50% when the subscription service is operational and ready to go live – that is, when the customer has acknowledged the completion of all the deliverables in the signed customer acceptance form. The Company generally invoices subscription service renewals for 100% of the total contract value when the renewal contract is executed. For the public safety solution, the pricing model is based on a per-square-mile basis. For security solutions, the pricing model is on a customized-site basis. As a result of the process for invoicing contracts and renewals upon execution, cash flows from operations and accounts receivable can fluctuate due to timing of contract execution and timing of deployment.

Prior to the adoption of Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers* (“Topic 606”), the Company recognized revenue in accordance with Accounting Standard Codification (“ASC”) 605, *Revenue Recognition*, and, accordingly, when all of the following criteria were met.

- Persuasive evidence of an arrangement exists
- Delivery has occurred or services have been rendered
- The sales price is fixed or determinable
- Collection of the related receivable is reasonably assured

Under ASC 605, the Company recognized subscription revenues ratably over the subscription period committed by the customer and commencing when the subscription service was fully operational and ready to go live, that is, upon completion of all deliverables stated in the signed customer acceptance form, assuming all other revenue recognition criteria were met. The Company recognized revenues from setup fees ratably based on the expected customer relationship period, typically over five years, which could extend beyond the initial contract period. In determining the expected customer relationship period, the Company considered specific customer details and renewal history with similar customers. If a customer declined to renew its subscription prior to the end of five years, then the remaining setup fees were immediately recognized.

Effective January 1, 2018, after the adoption of Topic 606, the Company recognizes revenue upon the satisfaction of performance obligations. At contract inception, the Company assesses the services promised in its contracts with customers and identifies a performance obligation for each promise to transfer to the customer a good or service (or bundle of services) that is distinct. To identify the performance obligations, the Company considers all of the services promised in the contract regardless of whether they are explicitly stated or are implied by customary business practices. The Company determined that the subscription services, training, and licenses to integrate with third-party applications are each distinct services that represent separate performance obligations. The setup activities are not distinct from the subscription service and are combined into the subscription service performance obligation. However, setup fees may provide a material right to the customer that has influence over the customers' decision to renew. All setup fees are assessed on a quantitative and qualitative basis to determine whether they represent a distinct performance obligation. The total contract value is allocated to each performance obligation identified based on the standalone selling price of the service. Discounts are allocated pro-rata to the identified performance obligations.

Revenues from subscription services are recognized ratably, on a straight-line basis, over the term of the subscription. Revenues from material rights are recognized ratably over the period in which they are determined to provide a material right to the customer, which is generally three years. Revenues from training and licenses to integrate with third-party applications are recognized upon delivery which generally occurs when the subscription service is operational and ready to go live and these amounts are immaterial.

Subscription renewal fees are recognized ratably over the term of the renewal, which is typically one year. While most customers elect to renew their agreements, in some cases, they may not be able to obtain the proper approvals or funding to complete the renewal prior to expiration. For these customers, the Company stops recognizing subscription revenues at the end of the current contract term, even though services may continue to be provided for a period of time until the renewal process is completed. Once the renewal is complete, the Company recognizes subscription revenues for the period between the expiration of the term of the agreement and the completion of the renewal process in the month in which the renewal is executed. If a customer declines to renew its subscription prior to the end of three years, then the remaining fees from material rights, if any, are immediately recognized.

As of January 1, 2018, upon the adoption of ASC 606, the Company had total short-term and long-term deferred revenue of \$17.3 million. During the three months ended June 30, 2018, the Company recognized \$6.4 million in revenue from the beginning deferred revenue balance and \$2.3 million from new billings, and added \$8.1 million to total short-term and long-term deferred revenue from new billings. During the six months ended June 30, 2018, the Company recognized \$11.7 million in revenue from beginning deferred revenue of \$18.1 million and \$3.9 million from new billings, and added \$15.8 million to total short-term and long-term deferred revenue from new billings.

As of June 30, 2018, the Company has estimated remaining performance obligations for contractually committed revenues of \$12.8 million, \$14.8 million, \$11.0 million, \$7.6 million, and \$600,000 that will be recognized during the remainder of the year ended December 31, 2018, and years ended December 31, 2019, 2020, 2021, and 2022 through 2024, respectively. The timing of revenue recognition includes estimates of go live dates for contracts not yet

live. Contractually committed revenue includes deferred revenue as of June 30, 2018 and amounts under contract that will be invoiced after June 30, 2018.

During the three months ended June 30, 2018, the Company recognized revenues of \$8.7 million from customers in the United States and \$0.2 million from a customer in South Africa.

During the six months ended June 30, 2018, the Company recognized revenues of \$15.3 million from customers in the United States and \$0.5 million from a customer in South Africa.

Topic 606 also requires the capitalization of certain incremental costs of obtaining a contract, which impacts the period in which the Company records sales commissions expense. Historically, the Company recognized sales commissions expense upfront. Under Topic 606, the Company is required to capitalize these expenses. As there are not commensurate commissions earned on renewals of the subscription services, the Company concluded that the capitalized commissions are related to subscription services provided under both the initial contract and renewal periods. Therefore, the amortization period for the capitalized commissions is the customer life, which is determined to be five years. As the capitalized commissions are related to subscription services that are transferred over the customer's life, the Company amortizes the capitalized commissions on a straight-line basis of five years. For commissions that are earned on renewal contracts with an original duration of one year or less, the Company uses the practical expedient applicable to such commissions and recognizes the commissions as expense instead of capitalizing.

Accounts Receivable, net

Accounts receivable consist of trade accounts receivables from the Company's customers, net of allowance for doubtful accounts if deemed necessary. Accounts receivable may include unbilled amounts which are under contract but are not yet billable. Accounts receivables are recorded at the invoiced amount. The Company does not require collateral or other security for accounts receivable. The Company periodically evaluates the collectability of its accounts receivable and provides an allowance for potential credit losses based on the historical experience. At June 30, 2018 and December 31, 2017, the Company did not have an allowance for potential credit losses as there were no estimated credit losses.

Concentrations of Risk

Credit Risk – Financial instruments that potentially subject the Company to concentration of credit risk consisted primarily of restricted cash, cash and cash equivalents and accounts receivable from trade customers. The Company maintains its cash deposits at two domestic financial institutions. The Company is exposed to credit risk in the event of default by a financial institution to the extent that cash and cash equivalents are in excess of the amount insured by the Federal Deposit Insurance Corporation. The Company generally places its cash and cash equivalents with high-credit quality financial institutions. To date, the Company has not experienced any losses on its cash and cash equivalents

Concentration of Accounts Receivable –As of June 30, 2018, two customers accounted for 31% and 25% of the Company's accounts receivable. Fluctuations in accounts receivable result from timing of the Company's execution of contracts and collection of related payments. As of December 31, 2017, three customers accounted for 18%, 18% and 14% of the Company's accounts receivable.

Concentration of Revenues –For the three months ended June 30, 2018, two customers accounted for 24% and 14% of the Company's total revenues. For the three months ended June 30, 2017, one customer accounted for 17% of the Company's total revenues.

For the six months ended June 30, 2018, two customers accounted for 22% and 16% of the Company's total revenues. For the six months ended June 30, 2017, one customer accounted for 17% of the Company's total revenues.

Accounting Pronouncements Recently Adopted

Effective January 1, 2018, the Company adopted Topic 606. This standard outlines a single comprehensive model for entities to use in accounting for revenues arising from contracts with customers that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Topic 606 was adopted on a modified retrospective basis and the new standard was applied only to new contracts entered into after January 1, 2018, and contracts

that were not completed as of January 1, 2018. The cumulative effect of this adoption of Topic 606 as of January 1, 2018 resulted in a reduction to accumulated deficit of \$3.0 million, a reduction of short-term and long-term deferred revenue of \$1.2 million and the capitalization of commissions in assets of \$1.8 million.

The impact from the adoption of Topic 606 was as follows:

	Three Months Ended June 30, 2018			Six Months Ended June 30, 2018		
	As Reported	Effect of Change Increase/ (Decrease)	Amounts Without Adoption of Topic 606	As Reported	Effect of Change Increase/ (Decrease)	Amounts Without Adoption of Topic 606
Revenues	\$ 8,927	\$ 69	\$ 8,858	\$15,834	\$ 122	\$ 15,712
Costs	3,950	—	3,950	7,258	—	7,258
Gross profit	4,977	69	4,908	8,576	122	8,454
Sales and marketing expense	2,195	(116)	2,311	3,749	(257)	4,006
Operating loss	(297)	(185)	(482)	(1,516)	(379)	(1,895)
Net loss	(369)	(185)	(554)	(1,586)	(379)	(1,965)

	As of June 30, 2018		
	As Reported	Effect of Change Increase/ (Decrease)	Amounts Without Adoption of Topic 606
Assets			
Prepaid expenses and other current assets	\$ 1,704	\$ 564	\$ 1,140
Other assets	1,662	1,460	202
Total assets	39,825	2,024	37,801
Liabilities			
Deferred revenue, short term	16,230	515	15,715
Total current liabilities	22,089	515	21,574
Deferred revenue, long term	1,212	(1,182)	2,394
Total liabilities	23,392	(667)	24,059

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, which provides targeted improvements to the recognition, measurement, presentation and disclosure of financial assets and financial liabilities. Specific accounting areas addressed include equity investments and financial liabilities reported under the fair value option and valuation allowance assessment resulting from unrealized losses on available-for-sale securities. This ASU also changes certain presentation and disclosure requirements for financial instruments. This ASU is to be applied by means of a cumulative effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The Company adopted this ASU as of January 1, 2018. The adoption of this ASU did not have any impact on the Company's condensed consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, addressing eight specific cash flow issues in an effort to reduce diversity in practice. This ASU is effective for the Company as of January 1, 2018. Early adoption is permitted. The adoption of this ASU did not have any material impact on its condensed consolidated statements of cash flows.

In October 2016, the FASB issued ASU 2016-16, *Intra-Entity Transfers of Assets Other Than Inventory*. The guidance requires entities to recognize the income tax impact of an inter-entity sale or transfer of an asset other than inventory when the sale or transfer occurs, rather than when the asset has been sold to an outside party. The guidance will require a modified retrospective application with a cumulative catch-up adjustment to opening retained earnings. The

Company adopted this ASU as of January 1, 2018. The adoption of this ASU did not have any impact on the Company's condensed consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Restricted Cash*, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The Company adopted this ASU as of January 1, 2018. The adoption of this ASU did not have any material impact on the Company's condensed consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, *Scope of Modification Accounting*, which amends the scope of modification accounting for share-based payment arrangements, provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting under ASC 718, *Compensation – Stock Compensation*. The Company adopted this ASU as of January 1, 2018. The adoption of this ASU did not have any impact on the Company's condensed consolidated financial statements.

Recent Accounting Pronouncements Not Yet Effective

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which requires lessees to recognize right-of-use assets and corresponding liabilities for all leases with an initial term in excess of 12 months. This ASU is to be adopted using a modified retrospective approach, including a number of practical expedients, that requires leases to be measured and recognized under the new guidance at the beginning of the earliest period presented. This ASU is effective for the Company as of January 1, 2019. Early adoption is permitted. The Company is currently evaluating the effect this ASU will have on its condensed consolidated financial statements and related disclosures. The Company expects the asset leased under its headquarters office operating lease will be capitalized on the balance sheet upon adoption of ASU.

In July 2017, the FASB issued ASU 2017-11, *Earnings Per Share (Topic 260), Distinguishing Liabilities from Equity (Topic 480), Derivatives and Hedging (Topic 815)*. The amendments in Part I of this ASU change the classification analysis of certain equity-linked financial instruments (or embedded features) with down round features. When determining whether certain financial instruments should be classified as liabilities or equity instruments should be classified as liabilities or equity instruments, a down round feature no longer precludes equity classification when assessing whether the instrument is indexed to an entity's own stock. The amendments also clarify existing disclosure requirements for equity-classified instruments. The amendments in Part I of this ASU are effective for the Company as of January 1, 2019. The amendments in Part II of this ASU replace the indefinite deferral of certain guidance in Topic 480 with a scope exception. The amendments in Part II of this ASU do not require any transition guidance. The Company is currently evaluating the effect this ASU will have on its condensed consolidated financial statements

Note 4. Details of Certain Condensed Consolidated Balance Sheet Accounts

Prepaid expenses and other current assets (in thousands):

	June 30, 2018	December 31, 2017
Prepaid software and licenses	\$ 332	\$ 407
Prepaid insurance	580	211
Other prepaid expenses	150	137
Deferred commissions	564	—
Other	78	84
	<u>\$ 1,704</u>	<u>\$ 839</u>

Other assets (in thousands):

	June 30, 2018	December 31, 2017
Deferred commissions	\$ 1,460	\$ —
Other	202	143
	<u>\$ 1,662</u>	<u>\$ 143</u>

Accrued expenses and other current liabilities (in thousands):

	June 30, 2018	December 31, 2017
Payroll liabilities	\$ 1,136	\$ 1,697
Accrued employee paid time off	564	469
Accrued commissions	180	199
Accrued ESPP	91	115
Royalties payable	143	125
Professional fees	160	328
Use and other taxes	400	406
Other	453	476
	<u>\$ 3,127</u>	<u>\$ 3,815</u>

Note 5. Impairment of Property and Equipment

During the three months ended June 30, 2018 the Company recognized the expense of \$0.4 million for the impairment of property and equipment relating to the remaining book value of indoor sensor networks installed at certain security customers.

During the year ended December 31, 2017, the Company recognized impairment expense of \$0.8 million for the impairment of property and equipment relating to the remaining book value of deployed equipment in Puerto Rico and the U.S. Virgin Islands. Management concluded that the impairment charges were required because the equipment was presumed destroyed by the hurricanes in September 2017. The Company also recognized \$0.9 million in revenues relating to the remaining deferred set-up fees to be recognized on contracts with customers in Puerto Rico and the U.S. Virgin Islands. Management concluded that the revenues associated with these contracts was required to be accelerated because the contracts with customers in Puerto Rico and the U.S. Virgin Islands were expired at the time of the hurricanes and all subscription services were fully delivered.

Note 6. Capital Stock*Convertible Preferred Stock*

Immediately prior to the IPO, the Company had the following outstanding convertible preferred stock:

	Shares Authorized	Shares Issued and Outstanding	Aggregate Liquidation Preference (in thousands)
Series B-1	4,773,000	3,848,023	\$ 22,575
Series A-2	1,177,000	1,176,423	20,000
			<u>\$ 42,575</u>

Upon the closing of the IPO, all shares of convertible preferred stock then outstanding were automatically converted into an aggregate of 4,689,753 shares of common stock, resulting in the reclassification of the related redeemable convertible preferred stock into \$23,000 of common stock and \$42.1 million into additional paid-in capital.

As of June 30, 2018, there were no shares of convertible preferred stock outstanding.

Common Stock

The Company is authorized to issue 500,000,000 shares of common stock, with a par value of \$0.005 and each outstanding share of common stock is entitled to one vote, as provided in the Post-IPO Certificate.

At June 30, 2018, there were 10,759,719 shares of common stock issued and outstanding. At December 31, 2017, there were 9,827,129 shares of common stock issued and outstanding.

Preferred Stock

The Company is authorized to issue 20,000,000 shares of preferred stock, with a par value of \$0.005, as provided in the Post-IPO Certificate. As of June 30, 2018, there were no shares of preferred stock issued and outstanding.

Note 7. Net Loss per Share

The following table summarizes the computation of basic and diluted net loss per share (in thousands, except share and per share data):

	<u>Three Months Ended June 30,</u>		<u>Six Months Ended June 30,</u>	
	<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
Numerator:				
Net loss	\$ (369)	\$ (4,306)	\$ (1,586)	\$ (5,867)
Denominator:				
Weighted-average shares outstanding, basic and diluted	10,589,038	3,724,760	10,329,874	2,678,787
Net loss per share	\$ (0.03)	\$ (1.16)	\$ (0.15)	\$ (2.19)

The following potentially dilutive shares outstanding at the end of the periods presented were excluded in the calculation of diluted net loss per share as the effect would have been anti-dilutive:

	<u>As of June 30,</u>	
	<u>2018</u>	<u>2017</u>
Options to purchase common stock	828,822	1,303,336
Unvested restricted stock units	110,764	—
Warrants to purchase Series B-1 convertible preferred or common stock	173,110	714,596
Total	<u>1,112,696</u>	<u>2,017,932</u>

Note 8. Convertible Preferred Stock Warrants and Common Stock Warrants

Immediately prior to the Company's IPO, all outstanding Series B-1 convertible preferred stock warrants were remeasured to their fair value, using the Black-Scholes model. Refer to Note 3, *Summary of Significant Accounting Policies*, to the notes to the consolidated financial statement included in the final prospectus for our initial public offering dated as of on June 8, 2017 and filed with the SEC pursuant to Rule 424(b)(4) (the "Prospectus") for a description of the valuation method. The final remeasurement of the convertible preferred stock warrant liability resulted in a \$3.7 million loss which was recorded to other expense, net.

Upon the closing of the IPO, the entire balance of \$5.7 million in convertible preferred stock warrant liability was reclassified to additional paid-in capital. All convertible preferred stock warrants were converted into common stock warrants. In addition, the Company issued to the lead underwriter in the IPO a warrant to purchase up to 84,000 shares of its common stock.

As of June 30, 2018, the Company had the following common stock warrants issued and outstanding (in thousands, except share and per share data):

Warrant Class	Shares	Issuance Date	Price per Share	Expiration Date
Common stock warrant	3,766	July 2012	\$ 5.8667	July 2019
Common stock warrant	34,628	August 2012	\$ 5.8667	August 2019
Common stock warrant	50,716	February 2014	\$ 0.1700	February 2021
Common stock warrant (1)	84,000	June 2017	\$ 13.2000	June 2020
	<u>173,110</u>			

(1) This warrant was issued to the Company's lead underwriter in connection with the IPO.

Note 9. Equity Incentive Plans

2017 Equity Incentive Plan

In May 2017, the Board and the Company's stockholders approved the 2017 Equity Incentive Plan (the "2017 Plan"), which became effective in connection with the IPO. The 2017 Plan provides for the issuance of stock options, restricted stock units and other awards to employees, directors and consultants of the Company. A total of 2,413,659 shares of the Company's common stock were initially reserved for issuance under the 2017 Plan, which is the sum of (1) 900,000 shares, (2) the number of shares reserved for issuance under the 2005 Plan at the time the 2017 Plan became effective and (3) shares subject to stock options or other stock awards under the 2005 Plan that would have otherwise been returned to the 2005 Plan (up to a maximum of 1,314,752 shares). Under an "evergreen" provision, the number of shares of common stock reserved for issuance under the 2017 Plan will automatically increase on January 1 of each year, beginning on January 1, 2018 and ending on and including January 1, 2027, by of 5% of the total number of shares of our capital stock outstanding on December 31 of the preceding calendar year or a lesser number of shares determined by our Board of Directors. In accordance with the evergreen provision, the number of shares of common stock reserved for issuance under our 2017 Plan was automatically increased on January 1, 2018 by 491,356 shares, which was equal to 5% of the total number of shares of capital stock outstanding on December 31, 2017.

2005 Stock Plan

In February 2005, the Company adopted the 2005 Stock Plan, as amended in January 2010 and November 2012 (the "2005 Plan"). Under the 2005 Plan provisions, the Company was authorized to grant incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock units, and shares of restricted stock.

Following the effectiveness of the 2017 Plan in connection with the IPO, no further grants will be made under the 2005 Plan.

A summary of option activities under the 2005 Plan and 2017 Plan during the six months ended June 30, 2018 is as follows:

	Number of Options Outstanding	Weighted Average Exercise Price
Outstanding as of December 31, 2017	1,294,128	\$ 1.79
Granted	102,746	\$ 28.80
Exercised	(553,216)	\$ 0.81
Canceled	(14,836)	\$ 4.11
Outstanding as of June 30, 2018	<u>828,822</u>	\$ 5.75

During the six months ended June 30, 2018, the Company granted executive management restricted stock unit ("RSU") awards totaling 92,883 shares of common stock, with vesting terms of 35% upon the first anniversary and

21.667% on each of the three subsequent anniversaries. The weighted average fair value of \$17.87 per unit was calculated using the closing stock price on the grant dates.

During the six months ended June 30, 2018, the Company granted directors RSU awards totaling 17,881 shares of common stock. The fair value of \$28.45 per unit was calculated using the closing price on the grant date.

Our 2017 Plan include stock options, restricted stock units and other stock awards. The number of shares available for grant under these plans was 1,296,557 as of June 30, 2018.

2017 Employee Stock Purchase Plan

In May 2017, the Board and the Company’s stockholders adopted the 2017 Employee Stock Purchase Plan (“2017 ESPP”), which became effective in connection with the Company’s IPO. The 2017 ESPP allows eligible employees to purchase shares of the Company’s common stock in an offering at a discount of the then-current trading price, up to the lesser of (1) 85% of the fair market value of the common stock on the first day of the IPO or (2) 85% of the fair market value of the common stock on the purchase date. The 2017 ESPP permits the maximum discounted purchase price permitted under U.S. tax rules, including a “lookback.”

The 2017 ESPP initial offering period runs for approximately 24 months in length, and contains four 6-month purchase periods. An employee’s purchase rights terminate immediately upon termination of employment or other withdrawal from the 2017 ESPP. No participant will have the right to purchase shares of common stock in an amount that has a fair market value of more than \$25,000 determined as of the first day of the applicable purchase period, for each calendar year.

There are 200,000 shares of common stock reserved for issuance under the 2017 ESPP. In addition, the 2017 ESPP contains an “evergreen” provision which provides for an automatic annual share increase on January 1 of each year, in an amount equal to the lesser of (1) 2% of the total number of shares of common stock outstanding on December 31st of the preceding calendar year, (2) 150,000 shares or (3) such number of shares as determined by the Board. In accordance with the evergreen provision, the number of shares of common stock reserved for issuance under our 2017 ESPP was automatically increased on January 1, 2018 by 150,000 shares.

The Company accounts for employee stock purchases made under its 2017 ESPP using the estimate grant date fair value of accounting in accordance with ASC 718, *Stock Compensation*. The Company values ESPP shares using the Black-Scholes model.

There were 43,624 shares issued under the 2017 ESPP during the six months ended June 30, 2018.

Total stock-based compensation expense associated with the 2005 Plan, 2017 Plan and 2017 ESPP is recorded in the condensed consolidated statements of operations and was allocated as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Cost of revenues	\$ 75	\$ 9	\$ 132	\$ 10
Sales and marketing	199	15	265	20
Research and development	68	9	108	16
General and administrative	306	19	570	29
Total	\$ 648	\$ 52	\$ 1,075	\$ 75

Note 10. Commitments and Contingencies

Operating Lease

The Company leases its principal executive offices in Newark, California, under a non-cancelable operating lease which expires in 2021. The Company recognizes rent expense on a straight-line basis over the expected lease term. The difference between cash payments required and rent expense is recorded as deferred rent. Rent expense for the Company’s

facilities was \$0.1 million for both the three months ended June 30, 2018 and 2017. Rent expense for the Company's facilities was \$ 0.2 million for both the six months ended June 30, 2018 and 2017.

The following is a schedule of future minimum lease payments under the non-cancelable operating lease at June 30, 2018 (in thousands):

2018 (remainder of year)	\$	185
2019		352
2020		357
2021		304
2022		—
Total	\$	<u>1,198</u>

Contingencies

On November 6, 2017, three individuals, Ken Fisher, Kevin Baxter and Fred Holmes (the "Contractors"), filed a complaint with the Superior Court of California, County of Alameda, alleging breach of contract, a breach of the implied covenant of good faith and fair dealing and violation of Section 17200 et seq. of the California Business and Professions Code, purportedly predicated on an alleged breach of Section 10b-5 of the Securities Exchange Act of 1934. On the basis of these allegations, the Contractors petitioned for approximately \$6.5 million in damages. The Contractors filed a First Amended Complaint on November 22, 2017, adding claims for promissory estoppel, conversion, anticipatory breach of contract, and unjust enrichment. The Contractors then sought a writ of attachment in regards to their alleged damages, which the court denied on December 21, 2017. The Contractors subsequently filed a motion seeking leave of court to file a Second Amended Complaint ("SAC") on January 26, 2017. The motion was granted and on March 2, 2018 the Contractors filed a SAC asserting claims for breach of contract, anticipatory breach of contract, breach of the implied covenant, and conversion. On April 26, 2018, the Contractors filed a motion for leave to file a Third Amended Complaint ("TAC"). The Court granted the motion, and on June 14, 2018, the Contractors filed a TAC alleging breach of contract, breach of the covenant of good faith and fair dealing, conversion, violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, violation of Section 17200 et seq. of the California Business and Professions Code, Material Misrepresentations in Violation of Cal. Civ. Code § 1710, Negligent Misrepresentation, Fraudulent Concealment, violation of S.E.C. Rule 701 and 17 C.F.R. § 230.701, and Rescission. The TAC alleges that the Contractors were entitled to be granted options to purchase more than 250,000 shares of our common stock on the basis of a term sheet between us and the Contractors signed in July 2007. The Contractors claim that our subsequent one-for-five and one-for-17 reverse stock splits should not apply to their option awards. On the basis of their allegations, the Contractors have petitioned for damages, including punitive damages, and other costs and expenses, including attorneys' fees. The parties recently agreed to participate in a private mediation in an effort to resolve the dispute. We believe that the Contractors' claims are without merit and intend to dispute them vigorously.

The Company may become subject to legal proceedings, as well as demands and claims that arise in the normal course of our business. Such claims, even if not meritorious, could result in the expenditure of significant financial and management resources. The Company makes a provision for a liability relating to legal matters when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed and adjusted to include the impacts of negotiations, estimated settlements, legal rulings, advice of legal counsel, and other information and events pertaining to a particular matter.

An unfavorable outcome on any such matters could require us to pay substantial damages, or, in connection with any intellectual property infringement claims, could require us to pay ongoing royalty payments or could prevent us from selling certain of our products. As a result, a settlement of, or an unfavorable outcome on, any of the matters referenced above or other litigation matters could have a material adverse effect on our business, operating results, financial condition and cash flows.

Note 11. Subsequent Events

None.

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

You should read the following discussion and analysis of our financial condition and results of operations together with our condensed consolidated financial statements and accompanying notes included in this Quarterly Report on Form 10-Q and the financial statements and accompanying notes and other financial information in the Management's Discussion and Analysis of Financial Condition and Results of Operations included in 2017 Annual report on form 10-K, filed with the Securities and Exchange Commission ("SEC") pursuant to Rule 424(b)(4) under the Securities Act of 1933, as amended, on March 28, 2018 ("Annual Report"). This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements are often identified by the use of words such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "plan," "project," "will," "would" or the negative or plural of these words or similar expressions or variations. Such forward-looking statements are subject to a number of risks, uncertainties, assumptions and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified herein, and those discussed in the section titled "Risk Factors", set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and in our other SEC filings. You should not rely upon forward-looking statements as predictions of future events. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We are the leader in gunshot detection solutions that help law enforcement officials and security personnel deter and prevent gun violence. We offer our software solutions on a SaaS-based subscription model to customers around the world with current customers located in the United States and South Africa. Our public safety solution, ShotSpotter Flex, is deployed in urban, high-crime areas to help deter gun violence by accurately detecting and locating gunshots and sending near real-time alerts to law enforcement. Our security solutions, SST SecureCampus and ShotSpotter SiteSecure, are designed to help law enforcement and security personnel serving universities, corporate campuses and key infrastructure or transportation centers mitigate risk and enhance security by notifying authorities and first responders of an active-shooter event almost immediately.

Our solutions consist of our highly-specialized, cloud-based software integrated with proprietary, internet-enabled sensors and communication networks. The speed and accuracy of our solutions enable rapid response by law enforcement and security personnel, increase the chances of apprehending the shooter, aid in evidentiary collection and can serve as an overall deterrent. When a potential gunfire incident is detected by our sensors, our software precisely locates where the incident occurred. An alert containing critical information about the incident is transmitted directly to law enforcement or security personnel through any computer and to iPhone® or Android mobile devices.

We generate annual subscription revenues from the deployment of our public safety solution on a per-square-mile basis. As of June 30, 2018, we had coverage areas of over 630 square miles, which included 91 cities and 10 campuses/ sites across the United States and South Africa, including three of the ten largest cities in the United States, of which 583 miles have gone live.

We enter into subscription agreements on a term basis that typically range from one to five years in duration, with the majority having a contract term of one year. Substantially all of our sales are to governmental agencies and universities which often undertake a prolonged contract evaluation process that affects the size or the timing of our sales contracts and may likewise increase our customer acquisition costs. For a discussion of the risks associated with our sales cycle, see risks entitled "Our sales cycle can be unpredictable, time-consuming and costly, and our inability to successfully complete sales could harm our business" and "Because we generally recognize our subscription revenues ratably over the term of our contract with a customer, fluctuations in sales will not be fully reflected in our operating results until future periods" in Part II, Item 1A, *Risk Factors*, included in this Quarterly Report on Form 10-Q.

We rely on a limited number of suppliers and contract manufacturers to produce components of our solutions. We have no long-term contracts with these manufacturers and purchase from them on a purchase-order basis. Our outsourced manufacturers generally procure the components directly from third-party suppliers. Although we use a limited number of suppliers and contract manufacturers, we believe that we could find alternate suppliers or manufacturers if circumstances required us to do so, in part because a significant portion of the components required by our solutions is available off the shelf. For a discussion of the risks associated with our limited number of suppliers, see risk entitled “We rely on a limited number of suppliers and contract manufacturers, and our proprietary ShotSpotter sensors are manufactured by a single contract manufacturer” in Part II, Item 1A, *Risk Factors*, included in this Quarterly Report on Form 10-Q.

We generated revenues of \$8.9 million and \$5.8 million for the three months ended June 30, 2018 and 2017, respectively, a year-over-year increase of 53%. Revenues from our ShotSpotter Flex public safety solution during the three months ended June 30, 2018 and 2017 represented approximately 98% and 96% of total revenues, respectively. Our two current largest customers, the City of Chicago and the City of New York, accounted for 24% and 14%, respectively, of our total revenues for the three months ended June 30, 2018. For the three months ended June 30, 2017, our largest customer was the City of New York, representing 17% of our total revenues for that period. As a result of widespread destruction caused by hurricanes in the fall of 2017 in Puerto Rico and the U.S. Virgin Islands, in September 2017, we discontinued our service to our customers in those locations.

For the three months ended June 30, 2018 and 2017, revenues generated within the United States (including, for the three months ended June 30, 2017, Puerto Rico and the U.S. Virgin Islands) accounted for \$8.7 million and \$4.4 million, or 98% and 96% of total revenues, respectively, and \$0.2 million for both three months ended June 30, 2018 and 2017, was derived from our customer located in South Africa.

We generated revenues of \$15.8 million and \$10.4 million for the six months ended June 30, 2018 and 2017, respectively, a year-over-year increase of 52%. Revenues from our ShotSpotter Flex public safety solution during the six months ended June 30, 2018 and 2017 represented approximately 98% and 96% of total revenues, respectively. Our two current largest customers, the City of Chicago and the City of New York, accounted for 22% and 16%, respectively, of our total revenues for the six months ended June 30, 2018. For the six months ended June 30, 2017, our largest customer was the City of New York, representing 17% of our total revenues for that period. As a result of widespread destruction caused by hurricanes in the fall of 2017 in Puerto Rico and the U.S. Virgin Islands, in September 2017, we discontinued our service to our customers in those locations.

For the six months ended June 30, 2018 and 2017, revenues generated within the United States (including, for the six months ended June 30, 2017, Puerto Rico and the U.S. Virgin Islands) accounted for \$15.3 million and \$10.2 million, or 97% and 96% of total revenues, respectively, and \$0.5 million and \$0.4 million for the six months ended June 30, 2018 and 2017, respectively, was derived from our customer located in South Africa.

We have not yet achieved profitability and had net losses of \$0.4 million and \$4.3 million for the three months ended June 30, 2018 and 2017, respectively, and \$1.6 million and \$5.9 million for the six months ended June 30, 2018 and 2017, respectively. Our accumulated deficit was \$96.2 million and \$97.6 million as of June 30, 2018 and December 31, 2017, respectively.

During the three and six months ended June 30, 2018 we went “live” on 61 and 108 net new square miles of coverage, respectively. In each case, the increase in coverage was achieved through a combination of expansion with existing customers and new customers.

We have focused on rapidly growing our business and believe that its future growth is dependent on many factors, including our ability to increase our customer base, expand the coverage of our solutions among our existing customers, expand our international presence and increase sales of our security solutions. Our future growth will primarily depend on the market acceptance for gunshot detection solutions. Challenges we face in this regard include our target customers not having access to adequate funding sources, the fact that contracting with government entities can be complex, expensive, and time-consuming and the fact that our typical sales cycle is often very long and can be costly. To combat these challenges, we invest in research and development, increase awareness of our solutions, and hire additional sales representatives to drive sales in order to continue to maintain our position as a market leader. In addition, we believe that entering into strategic partnerships with other service providers to cities and municipalities offers another potential avenue for expansion, particularly for our ShotSpotter Flex solution.

We will also focus on expanding our business by increasing sales of our security solutions. By developing additional solutions through SST SecureCampus and ShotSpotter SiteSecure, we believe that our potential for growth has increased and that we are still in the early stages of penetrating the market for our security solutions. Our ability to penetrate these new markets will depend on the quality of our solutions and their perceived value as a risk management tool, as well as our ability to design our solutions to meet the demands of these customers. If these security solution markets do not develop as we expect, our revenues may not grow at the rate we expect. We see much greater opportunity in outdoor coverage and have made the strategic decision to no longer include indoor coverage as part of our service offering. However, we were recently awarded a patent on indoor sensor technology and we are evaluating the most effective way to leverage that patent, which may include partnering with established indoor players to offer a complete solution where there is demand.

With respect to international sales, we believe that we have the potential to expand our coverage within South Africa and to pursue opportunities in Europe, South America and other regions of the world. By adding additional sales resources in strategic locations, we believe we will be better positioned to reach these markets. However, we recognize that we have limited international operational experience and currently operate only in one region outside of the continental United States, South Africa. Operating successfully in international markets will require significant resources and management attention and will subject us to additional regulatory, economic and political risks. Moreover, we anticipate that different political and regulatory considerations that vary across different jurisdictions could extend what is already a lengthy sales cycle.

Given the importance of these strategies and challenges we face, we expect to continue to incur losses in the near term and, if we are unable to achieve our growth objectives, we may not be able to achieve profitability.

Net New “Go-Live” Miles

We focus on net new “go live” miles as a key quarterly business metric to measure our operational performance and inform strategic decisions. Net new “go-live” square miles represent the square miles covered by deployments that were formally approved by customers during the quarter, both from initial and expanded customer deployments, net of square miles that ceased to be “live” during the quarter due to customer cancellations. New square miles include deployed square miles that may have been sold, or booked, in prior quarters. We focus on net new “go-live” miles as a key quarterly business metric to measure our operational performance and inform strategic decisions.

This metric, presented below for the three and six months ended June 30, 2018 and 2017, is calculated on a quarterly basis using internal data and may be calculated in a manner different than similar metrics used by other companies.

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Net new "go-live" square miles added	61	44	108	74

Components of Results of Operations

Presentation of Financial Statements

Our condensed consolidated financial statements include the accounts of our wholly-owned South African subsidiary, ShotSpotter (Pty) Ltd. All intercompany balances and transactions have been eliminated in consolidation.

Revenues

We derive substantially all of our revenues from subscription services. We recognize subscription fees ratably, on a straight-line basis, over the term of the subscription, which for new customers is typically initially one to three years in length. Customer contracts include one-time set-up fees for the set-up of our sensors in the customer’s coverage areas, training and third-party integration licenses. If the set-up fees are deemed to be a material right, they are recognized ratably over three years. Training and third-party integration license fees are recognized upon delivery.

We generally invoice customers for 50% of the total contract value when the contract is fully executed and for the remaining 50% when the subscription service is operational and ready to go live – that is, when the customer has acknowledged the completion of all the deliverables in the signed customer acceptance form. All fees billed in advance of services being delivered are recorded as deferred revenue. For our public safety solution, our pricing model is based on a per-square-mile basis. For our security solutions, our pricing model is on a customized-site basis. As a result of our process for invoicing contracts and renewals upon execution, our cash flow from operations and accounts receivable can fluctuate due to timing of contract execution and timing of deployment.

We generally invoice subscription service renewals for 100% of the total contract value when the renewal contract is executed. Renewal fees are recognized ratably over the term of the renewal, which is typically one year. While most of our customers elect to renew their agreements, in some cases, they may not be able to obtain the proper approvals or funding to complete the renewal prior to expiration. For these customers, we stop recognizing subscription revenues at the end of the current contract term, even though we may continue to provide services for a period of time until the renewal process is completed. Once the renewal is complete, we then recognize subscription revenues for the period between the expiration of the term of the agreement and the completion of the renewal process in the month in which the renewal is executed. If a customer declines to renew its subscription prior to the end of five years, then the remaining setup fees are immediately recognized.

Costs

Costs include the cost of revenues and charges for impairment of property and equipment. Cost of revenues primarily includes depreciation expense associated with capitalized customer acoustic sensor networks, communication expenses, costs related to hosting our service application, costs related to operating our Incident Review Center (the “IRC”), providing remote and on-site customer support and maintenance and forensic services, certain personnel and related costs of operations, stock-based compensation and allocated overhead, which includes IT, facility and equipment depreciation costs.

In the near term, we expect our cost of revenues to increase in absolute dollars to the extent our installed base increases, but decrease as a percentage of revenues because certain of our costs of revenues are fixed and do not need to increase commensurate with increases in revenues. In addition, depreciation expense associated with deployed equipment is recognized only over the first five years of a customer contract.

Operating Expenses

Operating expenses consist of sales and marketing, research and development, and general and administrative expenses. Salaries, bonuses, stock-based compensation expense and other personnel costs are the most significant components of each of these expense categories. We include stock-based compensation expense incurred in connection with the grant of stock options and restricted stock units to the applicable operating expense category based on the equity award recipient’s functional area.

We are focused on executing on our growth strategy. As a result, in the near term we expect our total operating expenses to increase in absolute dollars as we incur additional expenses due to growth and as a result of operating as a public company. Although our operating expenses will fluctuate, we expect that over time, they will generally decrease as a percentage of revenues.

Sales and Marketing

Sales and marketing expenses primarily consist of personnel-related costs attributable to our sales and marketing personnel, commissions earned by our sales personnel, marketing expenses for trade shows, conferences and conventions, consulting fees, travel and facility-related costs and allocated overhead.

In the near term, we expect our sales and marketing expenses to increase in absolute dollars primarily due to planned growth in our sales and marketing organization. This growth will include adding sales and marketing personnel and expanding our marketing activities to continue to generate additional leads. Sales and marketing expense may fluctuate from quarter to quarter based on the timing of commission expense, marketing campaigns and tradeshow.

Research and Development

Research and development expenses primarily consist of personnel-related costs attributable to our research and development personnel, consulting fees and allocated overhead. We have devoted our product development efforts primarily to develop new lower-cost sensor hardware, develop new features including a mobile application, improve functionality of our solutions and adapt to new technologies or changes to existing technologies.

In the near term, we expect our research and development expenses to increase in absolute dollars as we increase our research and development headcount to further strengthen our software and invest in the development of our service.

We will continue to invest in research and development to leverage our large and growing database of acoustic events, which includes those from both gunfire and non-gunfire. We also intend to leverage third-party artificial intelligence and our own evolving cognitive and analytical applications to improve the efficiency of our solutions, which may include internal software applications, data analysis, event routing and customer outputs. Certain of these applications and outputs may expand the platform of services that we will be able to offer our customers.

General and Administrative

General and administrative expenses primarily consist of personnel-related costs attributable to our executive, finance, and administrative personnel, legal, accounting and other professional services fees, other corporate expenses and allocated overhead. We have recently incurred additional expenses in expanding our operations and for our initial public offering ("IPO"), and will continue to incur additional expenses as we operate as a public company, including increased personnel, legal, insurance and accounting expenses, and the additional costs of achieving and maintaining compliance with Section 404 of the Sarbanes-Oxley Act and other regulations.

In the near term, we expect our general and administrative expenses to increase significantly in absolute dollars as we grow our business, support our operations as a public company and increase our headcount.

Other Expense, Net

Other expense, net, consists primarily of interest expense on our outstanding debt net of interest income, and losses from the remeasurement of our convertible preferred stock warrant liability and losses from early extinguishment of debt. The convertible preferred stock warrant liability was reclassified into additional paid-in capital upon our IPO and will no longer be remeasured at each balance sheet date.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable.

Results of Operations

Comparison of Three Months Ended June 30, 2018 and 2017

The following table sets forth our selected condensed consolidated statements of operations data for the three months ended June 30, 2018 and 2017 (in thousands):

	Three Months Ended June 30,				Change	
	2018	As a % of Revenues	2017	As a % of Revenues	\$	%
Revenues	\$ 8,927	100 %	\$ 5,836	100 %	\$ 3,091	53 %
Costs						
Cost of revenues	3,589	40 %	2,687	46 %	902	34 %
Impairment of property and equipment	361	4 %	—	—	361	100 %
Total costs	3,950	44 %	2,687	46 %	1,263	47 %
Gross profit	4,977	56 %	3,149	54 %	1,828	58 %
Operating expenses:						
Sales and marketing	2,195	25 %	1,369	23 %	826	60 %
Research and development	1,255	14 %	928	16 %	327	35 %
General and administrative	1,824	20 %	971	17 %	853	88 %
Total operating expenses	5,274	59 %	3,268	56 %	2,006	61 %
Loss from operations	(297)	(3 %)	(119)	(2 %)	(178)	150 %
Other expense, net	(54)	(1 %)	(4,187)	(72 %)	4,133	(99 %)
Provision for income taxes	(18)	(0 %)	—	—	(18)	100 %
Net loss	\$ (369)	(4 %)	\$ (4,306)	(74 %)	\$ 3,937	(91 %)

Revenues

The increase of \$3.1 million was primarily attributable both to the expansion of existing customer coverage areas and an increase in new customers.

Costs

The increase of \$1.3 million was due primarily to a \$0.2 million increase in overhead expenses, due to an increase in employee headcount since June 30, 2017, and a \$0.4 million impairment charge to expense the remaining net book value of indoor sensor networks installed at certain security customers.

Gross margin increased by 2 percentage points because certain costs of revenues are fixed and did not increase commensurate with the increase in subscription revenues.

Operating Expenses

Sales and Marketing Expense

The increase of \$0.8 million was primarily due to an increase of \$0.5 million in salaries, commissions and stock-based compensation expense associated with expansion of our sales, marketing and customer success organization.

Research and Development Expense

The increase of \$0.3 million was due primarily to an increase in personnel and recruiting expenses due to the hiring of new personnel since June 30, 2017.

General and Administrative Expense

The increase of \$0.9 million was due to a \$0.6 million increase in legal, accounting and other outside services fees associated with operating as a public company and litigation expenses and a \$0.1 million increase in insurance premiums for director and officer liability insurance.

Other Expense, Net

The decrease of \$4.1 million in the three months ended June 30, 2018 was due to the final remeasurement of the preferred stock warrant liability immediately prior to our IPO that resulted in a \$3.7 million charge in June 2017 and the decrease in interest expense due to repayment of all of our outstanding debt balances during the year ended December 31, 2017.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable. For the three months ended June 30, 2018, our provision for income taxes consists of the foreign taxes only.

Comparison of Six Months Ended June 30, 2018 and 2017

The following table sets forth our selected condensed consolidated statements of operations data for the six months ended June 30, 2018 and 2017 (in thousands):

	Six Months Ended June 30,				Change	
	2018	As a % of Revenues	2017	As a % of Revenues	\$	%
Revenues	\$ 15,834	100 %	\$ 10,398	100 %	\$ 5,436	52 %
Costs						
Cost of revenues	6,897	44 %	5,362	52 %	1,535	29 %
Impairment of property and equipment	361	2 %	—	—	361	100 %
Total costs	7,258	46 %	5,362	52 %	1,896	35 %
Gross profit	8,576	54 %	5,036	48 %	3,540	70 %
Operating expenses:						
Sales and marketing	3,749	24 %	2,477	24 %	1,272	51 %
Research and development	2,491	16 %	1,962	19 %	529	27 %
General and administrative	3,852	24 %	1,901	18 %	1,951	103 %
Total operating expenses	10,092	64 %	6,340	61 %	3,752	59 %
Loss from operations	(1,516)	(10 %)	(1,304)	(13 %)	(212)	16 %
Other expense, net	(26)	(0 %)	(4,563)	(44 %)	4,537	(99 %)
Provision for income taxes	(44)	(0 %)	—	—	(44)	100 %
Net loss	\$ (1,586)	(10 %)	\$ (5,867)	(56 %)	\$ 4,281	(73 %)

Revenues

The increase of \$5.4 million was primarily attributable both to the expansion of existing customer coverage areas and an increase in new customers.

Costs

The increase of \$1.9 million was due primarily to a \$0.4 million impairment charge to expense the remaining net book value of indoor sensor networks installed at certain security customers, a \$0.2 million increase in telecommunication expenses, a \$0.2 million increase in overhead expenses, due to an increase in employee headcount since June 30, 2017, and a \$0.3 million increase in depreciation expense associated with expansions in existing customer coverage areas.

Gross margin increased by 6 percentage points because certain costs of revenues are fixed and did not increase commensurate with the increase in subscription revenues.

Operating Expenses

Sales and Marketing Expense

The increase of \$1.3 million was primarily due to an increase of \$0.8 million in salaries, commissions and stock-based compensation expense associated with expansion of our sales, marketing and customer success organization.

Research and Development Expense

The increase of \$0.5 million was due primarily to an increase in personnel and recruiting expenses due to the hiring of new personnel since June 30, 2017.

General and Administrative Expense

The increase of \$2.0 million was due to a \$1.0 million increase in legal and accounting fees associated with operating as a public company and litigation expenses, a \$0.4 million increase in the total directors' compensation, a \$0.2 million increase in salaries, benefits and bonuses resulting from an increase in hiring new personnel, and a \$0.1 million increase in insurance premiums for director and officer liability insurance.

Other Expense, Net

The decrease of \$4.5 million in the six months ended June 30, 2018 was due to the final remeasurement of the preferred stock warrant liability immediately prior to our IPO that resulted in a \$3.7 million charge in June 2017 and the decrease in interest expense due to repayment of all of our outstanding debt balances during the year ended December 31, 2017.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable. For the six months ended June 30, 2018, our provision for income taxes consists of the foreign taxes only.

Liquidity and Capital Resources

Sources of Funds

Our operations have been financed primarily through net proceeds from the sale of equity, debt financing arrangements and cash from operating activities. Our principal source of liquidity is cash and cash equivalents totaling \$14.8 million as of June 30, 2018.

In June 2017, we received net proceeds of \$32.4 million after deducting underwriting warrant, discounts and commissions, from our IPO.

We believe our existing cash and cash equivalent balances and cash flow from operations will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months. Our future capital requirements may vary materially from those currently planned and will depend on many factors, including our rate of revenue growth, the timing and extent of spending on sales and marketing, the expansion of sales and marketing activities, the timing of new product introductions, market acceptance of our products and overall economic conditions. To the extent that current and anticipated future sources of liquidity are insufficient to fund our future business activities and requirements, we may be required to seek additional capital or debt financing. Raising additional capital would result in additional dilution to our stockholders. The incurrence of debt financing would result in debt service obligations and the instruments governing such debt could provide for operating and financing covenants that would restrict our operations.

Use of Funds

Our historical uses of cash have primarily consisted of cash used for operating activities, such as expansion of our sales and marketing operations, research and development activities and other working capital needs, and cash used in investing activities, such as property and equipment expenditures to install infrastructure in customer cities in order to deliver our solutions.

In September 2017, we voluntarily repaid our outstanding borrowing of \$13.5 million under a promissory note previously issued by the Company (the "2015 Term Note").

Cash Flows

Comparison of the Six Months Ended June 30, 2018 and 2017

The following table presents a summary of our cash flows for the six months ended June 30, 2018 and 2017:

	June 30,	
	2018	2017
	(in thousands)	
Net cash provided by (used in):		
Operating activities	\$ (836)	\$ 1,084
Investing activities	(5,669)	(2,894)
Financing activities	1,860	33,060
Net change in cash and cash equivalents	<u>\$ (4,645)</u>	<u>\$ 31,250</u>

Operating Activities

For standard customer deployments, we typically achieve cash flow breakeven, on a direct variable cost-basis, in less than a year from the date of execution of the contract. Our net loss and cash flows provided by operating activities are significantly influenced by our increase in headcount to support our growth, sales and marketing expenses, and our ability to bill and collect in a timely manner.

Operating activities used \$0.9 million in the six months ended June 30, 2018 primarily from an increase in accounts receivable of \$2.2 million and net loss of \$1.6 million partially offset by \$1.8 million in depreciation and amortization, and \$1.1 million in stock-based compensation.

Operating activities provided \$1.1 million in the six months ended June 30, 2017, primarily from non-cash items aggregating \$5.3 million and net cash inflow from changes in operating assets and liabilities aggregating \$1.7 million, partially offset by our net loss of \$5.9 million. Non-cash items reflected \$3.7 million from the remeasurement of the convertible preferred stock warrant liability and \$1.4 million for depreciation and amortization. The change in operating assets and liabilities reflected an increase of \$3.0 million in deferred revenue as a result of new customer contracts and renewals, which was partially offset by an increase of \$0.7 million in accounts receivable due to an increase in billings from customers renewing their contracts during the period, a decrease of \$0.3 million in accounts payable due to timing of payments to our vendors, and an increase of \$0.2 million in prepaid expenses and other assets, primarily for prepaid insurance.

Investing Activities

Our investing activities consist primarily of capital expenditures to install our solutions in customer coverage areas, purchases of property and equipment, and investment in intangible assets.

Investing activities used \$5.7 million and \$2.9 million in the six months ended June 30, 2018 and 2017, respectively, primarily for property and equipment expenditures to install our solutions in customer coverage areas.

Financing Activities

Cash generated by financing activities includes borrowings under our term loan and proceeds from the exercise of warrants and stock options.

Financing activities provided \$1.9 million in the six months ended June 30, 2018, primarily from the proceeds from exercise of warrants and stock options.

Financing activities provided \$33.1 million in the six months ended June 30, 2017, primarily from \$32.4 million in net proceeds from our IPO, and \$1.5 million in borrowing under our 2015 Term Note, which was partly offset by \$0.8 million in payments for IPO-related costs.

Contractual Obligations and Commitments

There were no material changes during the six months ended June 30, 2018 to the contractual obligations and commitments disclosed in the Management's Discussion and Analysis of Financial Condition and Results of Operations section of our 2017 Annual Report on Form 10-K. See Note 10, *Commitments and Contingencies*, to the notes to the condensed consolidated financial statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q for additional information regarding commitments.

Off-Balance Sheet Arrangements

As of June 30, 2018, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities that were established for the purpose of facilitating off-balance sheet arrangements. We do not engage in off-balance sheet financing arrangements. In addition, we do not engage in trading activities involving non-exchange traded contracts.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. GAAP. The preparation of our condensed consolidated financial statements requires us to make estimates, assumptions and judgments that affect the reported amounts of revenue, assets, liabilities, costs and expenses. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates.

For the significant or material changes in our critical accounting policies during the six months ended June 30, 2018, see Note 3, *Summary of Significant Accounting Policies*, to the notes of our condensed consolidated financial statements included in this Quarterly Report on Form 10-Q.

Recently Issued Accounting Pronouncements

See Note 3, *Summary of Significant Accounting Policies*, to the notes to our condensed consolidated financial statements included in this Quarterly Report on Form 10-Q for a summary of recently issued accounting pronouncements.

Item 3. Qualitative and Quantitative Disclosures about Market Risk

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily the result of fluctuations in interest rates and foreign exchange rates as well as, to a lesser extent, inflation.

There were no material changes in our market risk during the three and six months ended June 30, 2018, compared to the market risk disclosed in the Qualitative and Quantitative Disclosures about Market Risk section of our 2017 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management has evaluated, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13-a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that as of June 30, 2018, our disclosure controls and procedures were effective to provide reasonable assurance that the information we are required to file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

Beginning January 1, 2018, we implemented ASU 2014-09 Revenue from Contracts with Customers (Topic 606) and ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of Effective Date. As a result of the adoption of the new standard, we have implemented changes to our controls related to revenue. These included the development of new policies based on the five-step model provided in the new revenue standard, enhanced contract review requirements, and other ongoing monitoring activities. These controls were designed to provide assurance at a reasonable level of the fair presentation of our condensed consolidated financial statements and related disclosures. There was no other change in our internal control over financial reporting during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including our principal executive officer and principal financial officer, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On November 6, 2017, three individuals, Ken Fisher, Kevin Baxter and Fred Holmes (the “Contractors”), filed a complaint with the Superior Court of California, County of Alameda, alleging breach of contract, a breach of the implied covenant of good faith and fair dealing and violation of Section 17200 et seq. of the California Business and Professions Code, purportedly predicated on an alleged breach of Section 10b-5 of the Securities Exchange Act of 1934. On the basis of these allegations, the Contractors petitioned for approximately \$6.5 million in damages. The Contractors filed a First Amended Complaint on November 22, 2017, adding claims for promissory estoppel, conversion, anticipatory breach of contract, and unjust enrichment. The Contractors then sought a writ of attachment in regards to their alleged damages, which the court denied on December 21, 2017. The Contractors subsequently filed a motion seeking leave of court to file a Second Amended Complaint (“SAC”) on January 26, 2017. The motion was granted and on March 2, 2018 the Contractors filed a SAC asserting claims for breach of contract, anticipatory breach of contract, breach of the implied covenant, and conversion. On April 26, 2018, the Contractors filed a motion for leave to file a Third Amended Complaint (“TAC”). The Court granted the motion, and on June 14, 2018, the Contractors filed a TAC alleging breach of contract, breach of the covenant of good faith and fair dealing, conversion, violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, violation of Section 17200 et seq. of the California Business and Professions Code, Material Misrepresentations in Violation of Cal. Civ. Code § 1710, Negligent Misrepresentation, Fraudulent Concealment, violation of S.E.C. Rule 701 and 17 C.F.R. § 230.701, and Rescission. The TAC alleges that the Contractors were entitled to be granted options to purchase more than 250,000 shares of our common stock on the basis of a term sheet between us and the Contractors signed in July 2007. The Contractors claim that our subsequent one-for-five and one-for-17 reverse stock splits should not apply to their option awards. On the basis of their allegations, the Contractors have petitioned for damages, including punitive damages, and other costs and expenses, including attorneys’ fees. The parties recently agreed to participate in a private mediation in an effort to resolve the dispute. We believe that the Contractors’ claims are without merit and intend to dispute them vigorously.

From time to time, we may become involved in lawsuits as well as subject to various legal proceedings, claims, threats of litigation, and investigations in the ordinary course of business, including claims of alleged infringement of third-party patents and other intellectual property rights, commercial, employment, and other matters. While certain matters to which we are a party may specify the damages claimed, such claims may not represent reasonably possible losses. Given the inherent uncertainties of litigation, the ultimate outcome of these matters cannot be predicted at this time, nor can the amount of possible loss or range of loss, if any, be reasonably estimated.

An unfavorable outcome on any litigation matters could require us to pay substantial damages, or, in connection with any intellectual property infringement claims, could require us to pay ongoing royalty payments or could prevent us from selling certain of our products. As a result, a settlement of, or an unfavorable outcome on, any of the matters referenced above or other litigation matters could have a material adverse effect on our business, operating results, financial condition and cash flows.

Item 1A. RISK FACTORS

Investing in our common stock involves a high degree of risk. You should consider carefully the risks and uncertainties described below, together with all of the other information in this report, including our condensed consolidated financial statements and related notes, before deciding whether to purchase shares of our common stock. We have marked with an asterisk () those risks described below that reflect substantive changes from the risks described in our Annual Report on Form 10-K for the year ended December 31, 2017. If any of the following risks is realized, our business, operating results, financial condition and prospects could be materially and adversely affected. In that event, the price of our common stock could decline, and you could lose part or all of your investment. Moreover, the risks described below are not the only ones that we face. Additional risks not presently known to us or that we currently deem immaterial may also affect our business, operating results, prospects or financial condition. You should carefully consider these risk factors, together with all of the other information included in this report as well as our other publicly available filings with the SEC.*

Risks Related to Our Business and Industry

Our success depends on maintaining and increasing our sales, which depends on factors we cannot control, including the availability of funding to our customers.

To date, substantially all of our revenues have been derived from contracts with local governments and their agencies, in particular the police departments of major cities in the United States. To a lesser extent, we also generate revenues from federal agencies, foreign governments and higher education institutions. We believe that the success and growth of our business will continue to depend on our ability to add new police departments and other government agencies as customers of our public safety solution and new universities, corporate campuses and key infrastructure and transportation centers as customers of our security solutions. Many of our target customers have restricted budgets, such that we are forced to compete with programs or solutions that offer an alternative use of the same funds. A number of factors could cause potential customers to delay or refrain from purchasing our solutions or prevent expansion of their use of our solutions, including:

- decreases or changes in available funding, including budgetary allocations, government grants and other government funding programs;
- potential delays or changes in appropriations or other funding authorization processes;
- changes in fiscal or contracting policies; and
- changes in elected or appointed officials.

The occurrence of any of the foregoing would impede our ability to maintain or increase the amount of revenues derived from these customers, which could have a material adverse effect on our business, operating results and financial condition.

Contracting with government entities can be complex, expensive and time-consuming.

The procurement process for government entities is in many ways more challenging than contracting in the private sector. We must comply with laws and regulations relating to the formation, administration, performance and pricing of contracts with government entities, including U.S. federal, state and local governmental bodies. These laws and regulations may impose added costs on our business or prolong or complicate our sales efforts, and failure to comply with these laws and regulations or other applicable requirements could lead to claims for damages from our customers, penalties, termination of contracts and other adverse consequences. Any such damages, penalties, disruptions or limitations in our ability to do business with government entities could have a material adverse effect on our business, operating results and financial condition.

Government entities often require highly specialized contract terms that may differ from our standard arrangements. For example, if the federal government provides grants to certain state and local governments for our solutions, and such governments do not continue to receive these grants, then these customers have the ability to terminate their contracts with us without penalty. Government entities often impose compliance requirements that are complicated, require preferential pricing or “most favored nation” terms and conditions, or are otherwise time-consuming and expensive to satisfy. Compliance with these special standards or satisfaction of such requirements could complicate our efforts to obtain business or increase the cost of doing so. Even if we do meet these special standards or requirements, the increased costs associated with providing our solutions to government customers could harm our margins. Additionally, even once we have secured a government contract, the renewal process can be lengthy and as time-consuming as the initial sale, and we may be providing our service for months past the contract expiration date without certainty if the renewal agreement will be signed or not.

Changes in the underlying regulatory conditions, political landscape or required procurement procedures that affect these types of customers could be introduced prior to the completion of our sales cycle, making it more difficult or costly to finalize a contract with a new customer or expand or renew an existing customer relationship. For example, customers may require a competitive bidding process with extended response deadlines, review or appeal periods, or customer attention may be diverted to other government matters, postponing the consideration of the purchase of our products. Such delays could harm our ability to provide our solutions efficiently and to grow or maintain our customer base.

If we are unable to maintain and expand coverage of our existing public safety customer accounts and further penetrate the public safety market, our revenues may not grow.

Our ability to increase revenues will depend in large part on our existing public safety solution customers renewing their annual subscriptions and expanding their mileage coverage. Most of our ShotSpotter Flex customers begin using our solution in a limited coverage area. Our experience has been, and we expect will continue to be, that after the initial implementation of our solutions, our new customers typically renew their annual subscriptions, and many also choose to expand their coverage area. If our existing customers do not renew their subscriptions, our revenues may decrease. However, some customers may choose to not renew or reduce their coverage. For example, as a result of widespread destruction caused by recent hurricanes in Puerto Rico and the U.S. Virgin Islands, in September 2017, we discontinued our service to our customers in coverage areas in those locations and we classified the contracts as expired because the customers were no longer live. The Housing Authority of Puerto Rico was historically one of our largest customers. We cannot be certain when or if our customers in Puerto Rico and the U.S. Virgin Islands will recover their infrastructure and become live customers again. If other existing customers do not choose to renew or expand their coverage areas, our revenues will not grow as we anticipate.

Our ability to further penetrate the market for our public safety solution depends on several factors, including: maintaining a high level of customer satisfaction and a strong reputation among law enforcement; increasing the awareness of our ShotSpotter Flex solution and its benefits; the effectiveness of our marketing programs; the availability of funding to our customers; and the costs of our ShotSpotter solution. Some potential public safety customers may be reluctant or unwilling to use our solution for a number of reasons, including concerns about additional costs, unwillingness to expose or lack of concern regarding the extent of gun violence in their community, uncertainty regarding the reliability and security of cloud-based offerings or lack of awareness of the benefits of our public safety solution. If we are unsuccessful in expanding the coverage of ShotSpotter Flex by existing customers or adding new ShotSpotter Flex customers, our revenues and growth prospects would suffer.

If we are unable to sell our solutions into new markets, our revenues may not grow.

Part of our growth strategy depends on our ability to increase sales of our security solutions and add new customers for our public safety solution in markets outside of the United States. Any new market into which we attempt to sell our solutions may not be receptive. For example, while we have seen growing interest in our security solutions, interest in the indoor gunshot detection offering has been limited. We see much greater opportunity in outdoor coverage and have made the strategic decision to no longer include indoor coverage as part of our service offering. However, we were recently awarded a patent on indoor sensor technology and we are evaluating the most effective way to leverage that intellectual property, which may include partnering with established indoor players to offer a complete solution where there is a demand.

Our ability to successfully face these challenges depends on several factors, including increasing the awareness of our solutions and their benefits; the effectiveness of our marketing programs; the costs of our solutions; our ability to attract, retain and effectively train sales and marketing personnel; and our ability to develop relationships with communication carriers and other partners. If we are unsuccessful in developing and marketing our solutions into new markets, new markets for our solutions might not develop or might develop more slowly than we expect, either of which would harm our revenues and growth prospects.

Our sales cycle can be lengthy, time-consuming and costly, and our inability to successfully complete sales could harm our business.

Our sales process involves educating prospective customers and existing customers about the use, technical capabilities and benefits of our solutions. Prospective customers, especially government agencies, often undertake a prolonged evaluation process that may last up to nine months or more and that typically involves comparing the benefits of our solutions to alternative uses of funds. We may spend substantial time, effort and money on our sales and marketing efforts without any assurance that our efforts will produce any sales.

Additionally, events affecting our customers' budgets or missions may occur during the sales cycle that could negatively impact the size or timing of a purchase after we have invested substantial time, effort and resources into a potential sale, contributing to more unpredictability in the growth of our business. If we are unable to succeed in closing sales with new and existing customers, our business, operating results and financial condition will be harmed.

Changes in the availability of federal funding to support local law enforcement efforts could impact our business.

Many of our customers rely to some extent on funds from the U.S. federal government in order to purchase and pay for our solutions. Any reduction in federal funding for local law enforcement efforts could result in our customers having less access to funds required to continue, renew, expand or pay for our solutions. For example, changes in policies with respect to “sanctuary cities” may result in a reduction in federal funds available to our current or potential customers. If federal funding is reduced or eliminated and our customers cannot find alternative sources of funding to purchase our solutions, our business will be harmed.

If our business does not grow as we expect, or if we fail to manage our growth effectively, our operating results and business prospects would suffer.

Our ability to successfully grow our business depends on a number of factors including our ability to:

- accelerate our acquisition of new customers;
- further sell expansions of coverage areas to our existing customers;
- expand our international footprint;
- expand into new vertical markets, such as our security solutions;
- increase awareness of the benefits that our solutions offer; and
- maintain our competitive and technology leadership position.

As usage of our solutions grows, we will need to continue to make investments to develop and implement new or updated solutions, technologies, security features and cloud-based infrastructure operations. In addition, we will need to appropriately scale our internal business systems and our services organization, including the suppliers of our detection equipment and customer support services, to serve our growing customer base. Any failure of, or delay in, these efforts could impair the performance of our solutions and reduce customer satisfaction.

Further, our growth could increase quickly and place a strain on our managerial, operational, financial and other resources, and our future operating results depend to a large extent on our ability to successfully manage our anticipated expansion and growth. To manage our growth successfully, we will need to continue to invest in sales and marketing, research and development, and general and administrative functions and other areas. We are likely to recognize the costs associated with these investments earlier than receiving some of the anticipated benefits, and the return on these investments may be lower, or may develop more slowly, than we expect, which could adversely affect our operating results.

If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities or develop new solutions or upgrades to our existing solutions, satisfy customer requirements, maintain the quality and security of our solutions or execute on our business plan, any of which could have a material adverse effect on our business, operating results and financial condition.

Our business is dependent upon our ability to deploy and deliver our solutions, and the failure to meet our customers' expectations could harm our reputation, which may have a material adverse effect on our business, operating results and financial condition.

Promoting and demonstrating the utility of our solutions as useful, reliable and important tools for law enforcement and security personnel is critical to the success of our business. Our ability to secure customer renewals and enter into new customer contracts is dependent on our reputation and our ability to deliver our solutions effectively. We believe that our reputation among police departments using ShotSpotter Flex is particularly important to our success. Our ability to meet customer expectations will depend on a wide range of factors, including:

- our ability to continue to offer high-quality, innovative and accurate gunshot detection services;
- our ability to maintain continuous monitoring during high outdoor-noise activity periods such as New Year's Day, the Fourth of July and Cinco de Mayo;
- our ability to maintain high customer satisfaction, including meeting our SLA standards;
- the perceived value and quality of our solutions;

- differences in opinion regarding the metrics that measure the success of our solutions;
- our ability to successfully communicate the unique value proposition of our solutions;
- our ability to provide high-quality customer support;
- any misuse or perceived misuse of our solutions;
- interruptions, delays or attacks on our platform;
- litigation- or regulation-related developments; and
- damage to or degradation of our sensors or sensor network by third parties.

Furthermore, negative publicity, whether or not justified, relating to events or activities attributable to us, our solutions, our employees, our partners or others associated with any of these parties, may tarnish our reputation. Damage to our reputation may reduce demand for our solutions and would likely have a material adverse effect on our business, operating results and financial condition. Moreover, any attempts to rebuild our reputation may be costly and time-consuming, and such efforts may not ultimately be successful.

Interruptions or performance problems associated with our technology and infrastructure may adversely affect our business and results of operations.

We may in the future experience performance issues due to a variety of factors, including infrastructure changes, human or software errors, website or third-party hosting disruptions or capacity constraints due to a number of potential causes including technical failures, natural disasters or security attacks. If our security is compromised, our platform is unavailable or our users are unable to receive our alerts or otherwise communicate with our IRC, within a reasonable amount of time or at all, our business could be negatively affected. In some instances, we may not be able to identify the cause or causes of these performance problems within an acceptable period of time.

In addition, IRC is located in a single facility. Although the functions of our IRC can be performed remotely, any interruption or delay in service from our IRC, such as from a communications or power outage, could limit our ability deliver our solutions. In addition, it may become increasingly difficult to maintain and improve the performance of our solutions, especially during peak usage times as the capacity of our IRC operations reaches its limits. If there is an interruption or delay in service from our IRC and a gunshot is detected but not reviewed in the allotted time, our software will queue the incident for off line review. This may result in delayed notifications to our customers and as a result, we could experience a decline in customer satisfaction with our solutions and our reputation and growth prospects could be harmed.

We expect to continue to make significant investments to maintain and improve the performance of our solutions. To the extent that we do not effectively address capacity constraints, upgrade our systems as needed and continually develop our technology to accommodate actual and anticipated changes in technology, our business, operating results and financial condition may be adversely affected.

We rely on wireless carriers to provide access to wireless networks through which our acoustic sensors communicate with our cloud network and with which we provide our notification services to customers, and any interruption of such access would impair our business.

We rely on wireless carriers, mainly AT&T and Verizon, to provide access to wireless networks for machine-to-machine data transmissions, which are an integral part of our services. Our wireless carriers may suspend wireless service to expand, maintain or improve their networks. These wireless carriers perform routine maintenance and periodic software and firmware updates that may damage our sensors or make them inoperable. Any suspension or other interruption of services would adversely affect our ability to provide our services to our customers and may adversely affect our reputation. In addition, the terms of our agreements with these wireless carriers provide that either party can cancel or terminate the agreement for convenience with 90 days' notice. If one of our wireless carriers were to terminate its agreement with us, we would need to source a different wireless carrier and/or modify our equipment during the notice period in order to minimize disruption in the performance of our solutions. Price increases or termination by our wireless carriers or changes to existing contract terms could have a material adverse effect on our business, operating results and financial condition.

We may be unable to continue delivery of our solutions due to natural disasters, power outages or other events impacting us or our customers, which could harm our operating results and financial condition.

We recognize revenue on a subscription basis as our solutions are provided to our customers over time. If our services are disrupted due to natural disasters, power outages or other events that we cannot control, as recently happened when hurricanes hit Puerto Rico and the U.S. Virgin Islands, we may not be able to continue providing our solutions as expected.

When we stop providing coverage, we also stop recognizing revenues as a result of the affected subscription agreement. If we are forced to discontinue our services due to natural disasters, power outages and other events outside of our control, our revenues may decline, which would negatively impact our results of operations and financial condition.

Any of our facilities may be harmed or rendered inoperable by natural or man-made disasters, including earthquakes, tornadoes, hurricanes, wildfires, floods, nuclear disasters, acts of terrorism or other criminal activities, infectious disease outbreaks, and power outages, which may render it difficult or impossible for us to operate our business for some period of time. For example, our IRC and a data center that hosts some of our customer services are located in the San Francisco Bay Area, a region known for seismic activity. Our facilities would likely be costly to repair or replace, and any such efforts would likely require substantial time. Any disruptions in our operations could negatively impact our business and operating results, and harm our reputation. In addition, we may not carry business insurance or may not carry sufficient business insurance to compensate for losses that may occur. Any such losses or damages could have a material adverse effect on our business, operating results and financial condition. In addition, the facilities of significant vendors, including the manufacturer of our proprietary acoustic sensor, may be harmed or rendered inoperable by such natural or man-made disasters, which may cause disruptions, difficulties or material adverse effects on our business.

Real or perceived false positive gunshot alerts or failure or perceived failure to generate alerts for actual gunfire could adversely affect our customers and their operations, damage our brand and reputation and adversely affect our growth prospects and results of operations.

A false positive alert, in which a non-gunfire incident is reported as gunfire, could result in an unnecessary rapid deployment of police officers and first responders, which may raise unnecessary fear among the occupants of a community or facility, and may be deemed a waste of police and first responder resources. A failure to alert law enforcement or security personnel of actual gunfire could result in a less rapid response by police officers and first responders, increasing the probability of injury or loss of life. Both false positive alerts and the failure to generate alerts of actual gunfire may result in customer dissatisfaction, potential loss of confidence in our solutions, and potential liabilities to customers or other third parties, any of which could harm our reputation and adversely impact our business and operating results. Additionally, the perception of a false positive alert or of a failure to generate an alert, even where our customers understand that our solutions were utilized correctly, could lead to negative publicity or harm the public perception of our solutions, which could harm our reputation and adversely impact our business and operating results.

Economic uncertainties or downturns, or political changes, could limit the availability of funds available to our customers and potential customers, which could materially adversely affect our business.

Current or future economic uncertainties or downturns could adversely affect our business and operating results. Negative conditions in the general economy both in the United States and abroad, including conditions resulting from changes in gross domestic product growth, financial and credit market fluctuations, political deadlock, natural catastrophes, such as the devastation caused by the hurricanes in Puerto Rico, warfare and terrorist attacks on the United States, Europe, the Asia Pacific region or elsewhere, could cause a decrease in funds available to our customers and potential customers and negatively affect the rate of growth of our business.

These economic conditions may make it extremely difficult for our customers and us to forecast and plan future budgetary decisions or business activities accurately, and they could cause our customers to reevaluate their decisions to purchase our solutions, which could delay and lengthen our sales cycles or result in cancellations of planned purchases. Furthermore, during challenging economic times or as a result of political changes, our customers may tighten their budgets and face constraints in gaining timely access to sufficient funding or other credit, which could result in an impairment of their ability to make timely payments to us. In turn, we may be required to increase our allowance for doubtful accounts, which would adversely affect our financial results.

We cannot predict the timing, strength or duration of any economic slowdown, instability or recovery, generally or within any particular industry, or the impact of political changes. If the economic conditions of the general economy or industries in which we operate worsen from present levels, or if recent political changes result in less funding being

available to purchase our solutions, our business, operating results, financial condition and cash flows could be adversely affected.

We have not been profitable historically and may not achieve or maintain profitability in the future.

We have posted a net loss in each year since inception and, had net losses of \$0.4 million and \$4.3 million during the three months ended June 30, 2018 and 2017, respectively, and \$1.6 million and \$5.9 million during the six months ended June 30, 2018 and 2017, respectively. As of June 30, 2018, we had an accumulated deficit of \$96.2 million. We are not certain whether or when we will obtain a high enough volume of sales of our solutions to sustain or increase our growth or achieve or maintain profitability in the future. We also expect our costs to increase in future periods, which could negatively affect our future operating results if our revenues do not increase. In particular, we expect to continue to expend substantial financial and other resources on:

- sales and marketing, including a significant expansion of our sales organization, both domestically and internationally;
- research and development related to our solutions, including investments in our engineering and technical teams;
- continued international expansion of our business; and
- general and administrative expenses, including legal and accounting expenses preparing for and related to being a public company.

These investments may not result in increased revenues or growth in our business. If we are unable to increase our revenues at a rate sufficient to offset the expected increase in our costs, our business, operating results and financial position may be harmed, and we may not be able to achieve or maintain profitability over the long term. Additionally, we may encounter unforeseen operating expenses, difficulties, complications, delays and other unknown factors that may result in losses in future periods. If our revenue growth does not meet our expectations in future periods, our financial performance may be harmed, and we may not achieve or maintain profitability in the future.

We may require additional capital to fund our business and support our growth, and our inability to generate and obtain such capital on acceptable terms, or at all, could harm our business, operating results, financial condition and prospects.

We intend to continue to make substantial investments to fund our business and support our growth. In addition, we may require additional funds to respond to business challenges, including the need to develop new features or enhance our solutions, improve our operating infrastructure or acquire or develop complementary businesses and technologies. As a result, in addition to the revenues we generate from our business and our existing cash balances, we may need to engage in additional equity or debt financings to provide the funds required for these and other business endeavors. If we raise additional funds through future issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing that we may secure in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. We may not be able to obtain such additional financing on terms favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support our business growth and to respond to business challenges could be significantly impaired, and our business may be adversely affected. In addition, our inability to generate or obtain the financial resources needed may require us to delay, scale back, or eliminate some or all of our operations, which may have a material adverse effect on our business, operating results, financial condition and prospects.

New competitors may enter the market for our public safety solution.

If cities and other government entities increase their efforts to reduce gun violence or our solutions gain visibility in the market, companies could decide to enter into the public safety solution market and thereby increase the competition we face. In addition to other gunshot detection products, we also compete with other technologies and solutions targeting our public safety customers' resources for law enforcement and crime prevention. Because there are several possible uses

for these limited budgetary resources, if we are not able to compete successfully for these limited resources, our business may not grow as we expect, which could adversely impact our revenues and operating results.

The competitive landscape for our security solutions is evolving.

The market for security solutions for university campuses, corporate campuses and transportation and key infrastructure centers includes a number of available options, such as video surveillance and increased human security presence, in addition to indoor gunshot detection companies with which we compete. Because there are several possible uses of funds for campus security needs, we may face increased challenges in demonstrating or distinguishing the benefits of SST SecureCampus and ShotSpotter SiteSecure, our security solutions. In particular, while we have seen growing interest in our security solutions, interest in the indoor gunshot detection offering has been limited. We expect future customer deployments for our security solutions to consist primarily of outdoor gunshot detection deployments. We see much greater opportunity in outdoor coverage and have made the strategic decision to no longer include indoor coverage as part of our service offering.

Failure to effectively develop and expand our sales and marketing capabilities could harm our ability to increase our customer base and achieve broader market acceptance of our solutions.

To increase total customers and customer coverage areas and to achieve broader market acceptance of our solutions, we will need to expand our sales and marketing organization and increase our business development resources, including the vertical and geographic distribution of our sales force and our teams of account executives focused on new accounts and responsible for renewal and growth of existing accounts.

Our business requires that our sales personnel have particular expertise and experience in working with law enforcement agencies, other government organizations and higher education institutions. We may not achieve revenue growth from expanding our sales force if we are unable to hire, develop and retain talented sales personnel with appropriate experience, if our new sales personnel are unable to achieve desired productivity levels in a reasonable period of time or if our sales and marketing programs are not effective.

The nature of our business exposes us to inherent liability risks.

Our solutions, including ShotSpotter Flex, SST SecureCampus and ShotSpotter SiteSecure, are designed to communicate real-time alerts of gunfire incidents to police officers and first responders. Due to the nature of such applications, we are potentially exposed to greater risks of liability for employee acts or omissions or system failures than may be inherent in other businesses. Although substantially all of our customer agreements contain provisions limiting our liability to our customers, we cannot be certain that these limitations will be enforced or that the costs of any litigation related to actual or alleged omissions or failures would not have a material adverse effect on us even if we prevail. Further, certain of our insurance policies and the laws of some states may limit or prohibit insurance coverage for punitive or certain other types of damages or liability arising from gross negligence, and we cannot assure you that we are adequately insured against the risks that we face.

The nature of our business may result in undesirable press coverage or other negative publicity.

Our solutions are used to assist law enforcement and first responders in the event that gunfire is detected. Even when our solutions work as intended, the incidents detected by our solutions could lead to injury, loss of life and other negative outcomes, and such events are likely to receive negative publicity. If we fail to detect an incident, or if we detect an incident, such as a terrorist attack or active-shooter event, but the response time of law enforcement or first responders is not sufficiently quick to prevent injury, loss of life, property damage or other adverse outcomes, we may receive negative media attention.

In addition, our solutions require that our customers monitor alerts and respond timely to notifications of gunshots. If our customers do not fully utilize our systems, we may be subject to criticism and unflattering media coverage regarding the effectiveness of our solutions and the cost of our solutions to our customers. Such negative publicity could have an adverse impact on new sales or renewals or expansions of coverage areas by existing customers, which would adversely impact our financial results and future prospects.

Real or perceived errors, failures or bugs in our software could adversely affect our operating results and growth prospects.

Because our software is complex, undetected errors, failures or bugs may occur. Our software is often installed and used with different operating systems, system management software, and equipment and networking configurations, which may cause errors or failures of our software or other aspects of the computing environment into which it is deployed. In addition, deployment of our software into computing environments may expose undetected errors, compatibility issues, failures or bugs in our software. Despite our testing, errors, failures or bugs may not be found in our software until it is released to our customers. Moreover, our customers could incorrectly implement or inadvertently misuse our software, which could result in customer dissatisfaction and adversely impact the perceived utility of our products as well as our brand. Any of these real or perceived errors, compatibility issues, failures or bugs in our software could result in negative publicity, reputational harm, loss of or delay in market acceptance of our software, loss of competitive position or claims by customers for losses sustained by them. In any such event, we may be required, or may choose, for customer relations or other reasons, to expend additional resources in order to correct the problem. Alleviating any of these problems could require significant expenditures of our capital and other resources and could cause interruptions or delays in the use of our solutions, which could cause us to lose existing or potential customers and could adversely affect our operating results and growth prospects.

Interruptions or delays in service from our third-party providers could impair our ability to make our solutions available to our customers, resulting in customer dissatisfaction, damage to our reputation, loss of customers, limited growth and reduction in revenues.

We currently use third-party data center hosting facilities to host certain components of our solutions. Our operations depend, in part, on our third-party providers' abilities to protect these facilities against damage or interruption from natural disasters, power or communications failures, cyber incidents, criminal acts and similar events. In the event that any of our third-party facility arrangements is terminated, or if there is a lapse of service or damage to a facility, we could experience service interruptions in our solutions as well as delays and additional expenses in arranging new facilities and services. Any changes in third-party service levels at our data centers or any errors, defects, disruptions, cyber incidents or other performance problems with our solutions could harm our reputation.

Any damage to, or failure of, the systems of our third-party providers could result in interruptions to our solutions. Despite precautions taken at our data centers, the occurrence of spikes in usage volume, natural disasters, cyber incidents, acts of terrorism, vandalism or sabotage, closure of a facility without adequate notice or other unanticipated problems could result in lengthy interruptions in the availability of our services. Problems faced by our third-party data center locations, with the network providers with whom they contract, or with the systems by which our communications providers allocate capacity among their customers, including us, could adversely affect the experience of our customers. Interruptions in our services might cause us to issue refunds to customers and subject us to potential liability.

Further, our insurance policies may not adequately compensate us for any losses that we may incur in the event of damage or interruption, and therefore the occurrence of any of the foregoing could subject us to liability, cause us to issue credits to customers or cause customers not to renew their subscriptions for our applications, any of which could materially adversely affect our business.

If our security measures or those of our customers or third-party providers are compromised, or if unauthorized access to the data of our customers is otherwise obtained, our solutions may be perceived as not being secure, our customers may be harmed and may curtail or cease their use of our solutions, our reputation may be damaged and we may incur significant liabilities.

Our operations involve the storage and transmission of gunfire incident data, including date, time, address and GPS coordinates, occurring in our customer's coverage area. Security incidents, whether as a result of third-party action, employee or customer error, technology impairment or failure, malfeasance or criminal activity, could result in unauthorized access to, or loss or unauthorized disclosure of, this gunfire incident data, which could result in litigation expenses or damages, indemnity and other contractual obligations and other possible liabilities, including but not limited to government fines and penalties and mitigation expenses, as well as negative publicity, which could damage our reputation, impair our sales and harm our customers and our business. Cyber incidents and malicious internet-based activity continue to increase generally, and providers of cloud-based services have been targeted. If third parties with whom we work, such as vendors or developers, violate applicable laws or our security policies, such violations may also put our gunfire incident data at risk and could in turn have an adverse effect on our business. In addition, such a violation could expose the locations of our sensors, including those sensors for which we obtained third-party consents that include confidentiality obligations. We may be unable to anticipate or prevent techniques used to obtain unauthorized access or to sabotage systems because such techniques change frequently and often are not detected until after an incident has occurred. As we increase our customer base and our brand becomes more widely known and recognized, third parties may increasingly seek to compromise our security controls or gain unauthorized access to customer data or other sensitive information. Further, because of the nature of the services that we provide to our customers, we may be a unique target for attacks.

Many governments have enacted laws requiring companies to notify individuals of data security incidents or unauthorized transfers involving certain types of personal data. In addition, some of our customers contractually require notification of any data security incident. Accordingly, security incidents experienced by our competitors, by our customers or by us may lead to public disclosures, which may lead to widespread negative publicity. Any security compromise in our industry, whether actual or perceived, could harm our reputation, erode customer confidence in the effectiveness of our security measures, negatively impact our ability to attract new customers, cause existing customers to elect not to renew their subscriptions or subject us to third-party lawsuits, regulatory fines or other action or liability, which could materially and adversely affect our business and operating results. Further, the costs of compliance with notification laws and contractual obligations may be significant and any requirement that we provide such notifications as a result of an actual or alleged compromise could have a material and adverse effect on our business.

While we maintain general liability insurance coverage and coverage for errors or omissions, we cannot assure you that such coverage would be adequate or would otherwise protect us from liabilities or damages with respect to claims alleging compromise or loss of data, or that such coverage will continue to be available on acceptable terms or at all.

We rely on the cooperation of customers and third parties to permit us to install our ShotSpotter sensors on their facilities, and failure to obtain these rights could increase our costs or limit the effectiveness of our ShotSpotter Flex solution.

Our ShotSpotter Flex solution requires us to deploy ShotSpotter sensors in our customer coverage areas, which typically entails the installation of approximately 20 to 25 sensors per square mile. The ShotSpotter sensors are mounted on city facilities and third-party buildings, and occasionally on city or utility-owned light poles, and installing the sensors requires the consent of the property owners, which can be time-consuming to obtain and can delay deployment. Generally, we do not pay a site license fee in order to install our sensors, and our contractual agreements with these facility owners provide them the right to revoke permission to use their facility with notice of generally 60 days.

To the extent that required consents delay our ability to deploy our solutions or facility owners do not grant permission to use their facilities, revoke previously granted permissions, or require us to pay a site license fee in order to install our sensors, our business may be harmed. If we were required to pay a site license fee in order to install sensors, our deployment expenses would increase, which would impact our gross margins. If we cannot obtain a sufficient number of sensor mounting locations that are appropriately dispersed in a coverage area, the effectiveness of our ShotSpotter Flex solution would be limited, we may need to reduce the coverage area of the solution, or we may not be able to meet our service level requirements, any of which could result in customer dissatisfaction or have a material adverse impact on our reputation, our business and our financial results.

If we fail to offer high-quality customer support, our business and reputation may suffer.

We offer customer support 24 hours a day, seven days a week, as well as training on best practices, forensic expertise and expert witness services. Providing these services requires that our personnel have specific experience, knowledge and expertise, making it more difficult for us to hire qualified personnel and to scale up our support operations. The importance of high-quality customer support will increase as we expand our business and pursue new customers. We may be unable to respond quickly enough to accommodate short-term increases in customer demand for support services or scale our services if our business grows. Increased customer demand for these services, without corresponding revenues, could increase our costs and harm our operating results. If we do not help our customers use applications within our solutions and provide effective ongoing support, our ability to sell additional applications to, or to retain, existing customers may suffer and our reputation with existing or potential customers may be harmed.

Our reliance on wireless carriers will require updates to our technology, and making such updates could result in disruptions in our service or increase our costs of operations.

The majority of our installed ShotSpotter sensors use third-generation (“3G”), cellular communications. Certain wireless carriers have advised us that they will discontinue their 3G services in the future and our ShotSpotter sensors will not be able to transmit on these networks. We will have to upgrade the sensors that use 3G cellular communications at no additional cost to our customers prior to the discontinuation of 3G services, the timing of which is uncertain. These sensor replacements will require significant capital expenditures and may also divert management’s attention and other important resources away from our customer service and sales efforts for new customers. We are currently deploying a ShotSpotter sensor that uses fourth-generation (4G) Long-Term Evolution (LTE) wireless technology. In the future, we may not be able to successfully implement new technologies or adapt existing technologies to changing market demands. If we are unable to adapt timely to changing technologies, market conditions or customer preferences, our business, operating results and financial condition could be materially and adversely affected.

We rely on a limited number of suppliers and contract manufacturers, and our proprietary ShotSpotter sensors are manufactured by a single contract manufacturer.

We rely on a limited number of suppliers and contract manufacturers. In particular, we use a single manufacturer, with which we have no long-term contract and from which we purchase on a purchase-order basis, to produce our proprietary ShotSpotter sensors. Our reliance on a sole contract manufacturer increases our risks since we do not currently have any alternative or replacement manufacturers, and we do not maintain a high volume of inventory. In the event of an interruption from a contract manufacturer, we may not be able to develop alternate or secondary sources without incurring material additional costs and substantial delays. Furthermore, these risks could materially and adversely affect our business if our contract manufacturer is impacted by a natural disaster or other interruption at a particular location because each of our contract manufacturers produces our products from a single location. Although our contract manufacturer has alternative manufacturing locations, transferring manufacturing to another location may result in significant delays in the availability of our sensors.

Many of the key components used to manufacture our proprietary ShotSpotter sensors also come from limited or sole sources of supply. Our contract manufacturer generally purchases these components on our behalf, and we do not have any long-term arrangements with our suppliers. We are therefore subject to the risk of shortages and long lead times in the supply of these components and the risk that suppliers discontinue or modify components used in our products. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantities and delivery schedules. Developing alternate sources of supply for these components may be time-consuming, difficult, and costly, and we or our suppliers may not be able to source these components on terms that are acceptable to us, or at all, which may undermine our ability to fill our orders in a timely manner.

If we experience significantly increased demand, or if we need to replace an existing supplier or contract manufacturer, we may be unable to supplement or replace such supply or contract manufacturing on terms that are acceptable to us, which may undermine our ability to deliver our products to customers in a timely manner. For example, for our ShotSpotter sensors, it may take a significant amount of time to identify a contract manufacturer that has the capability and resources to build the sensors to our specifications. Identifying suitable suppliers and contract manufacturers is an extensive process that requires us to become satisfied with their quality control, technical capabilities, responsiveness and service, financial stability, regulatory compliance, and labor and other ethical practices. Accordingly,

the loss of any key supplier or contract manufacturer could adversely impact our business, operating results and financial condition.

Our solutions use third-party software and services that may be difficult to replace or cause errors or failures of our solutions that could lead to a loss of customers or harm to our reputation and our operating results.

We license third-party software and depend on services from various third parties for use in our solutions. In the future, such software or services may not be available to us on commercially reasonable terms, or at all. Any loss of the right to use any of the software or services could result in decreased functionality of our solutions until equivalent technology is either developed by us or, if available from another provider, is identified, obtained and integrated, which could harm our business. In addition, any errors or defects in or failures of the third-party software or services could result in errors or defects in our solutions or cause our solutions to fail, which could harm our business and be costly to correct. Many of these providers attempt to impose limitations on their liability for such errors, defects or failures, and if enforceable, we may have additional liability to our customers or third-party providers that could harm our reputation and increase our operating costs.

We will need to maintain our relationships with third-party software and service providers, and obtain from such providers software and services that do not contain any errors or defects. Any failure to do so could adversely impact our ability to deliver effective products to our customers and could harm our operating results.

If we do not or cannot maintain the compatibility of our platform with applications that our customers use, our business could suffer.

Some of our customers choose to integrate our solutions with certain other systems used by our customers, such as real-time crime center platforms or computer-aided dispatch systems. The functionality and popularity of our solutions depend, in part, on our ability to integrate our solutions these systems. Providers of these systems may change the features of their technologies, restrict our access to their applications or alter the terms governing use of their applications in an adverse manner. Such changes could functionally limit or terminate our ability to use these technologies in conjunction with our solutions, which could negatively impact our customer service and harm our business. If we fail to integrate our solutions with applications that our customers use, we may not be able to offer the functionality that our customers need, and our customers may not renew their agreements, which would negatively impact our ability to generate revenues and adversely impact our business.

Concerns regarding privacy and government-sponsored surveillance may deter customers from purchasing our solutions.

Private citizens have become increasingly sensitive to real or perceived government or third-party surveillance and may wrongly believe that our outdoor sensors, as acoustic devices installed in urban areas or public facilities, such as universities, allow customers to listen to private conversations and monitor private citizen activity. Our sensors are not designed for “live listening” and are triggered only on loud impulsive sounds that may likely be gunfire. However, perceived privacy concerns may result in negative media coverage and efforts by private citizens to persuade municipalities, educational institutions or other potential customers not to purchase our solutions for their communities, campuses or facilities. If customers choose not to purchase our solutions due to privacy concerns, then the market for our solutions may develop more slowly than we expect, or it may not achieve the growth potential we expect, any of which would adversely affect our business and financial results.

Our future quarterly results of operations may fluctuate significantly due to a wide range of factors, which makes our future results difficult to predict.

Our revenues and results of operations could vary significantly from quarter to quarter as a result of various factors, many of which are outside of our control, including:

- the expansion or contraction of our customer base;
- the renewal or nonrenewal of subscription agreements with, and expansion of coverage areas by, existing customers;
- the size, timing and terms of our sales to both existing and new customers;

- the introduction of products or services that may compete with us for the limited funds available to our customers, and changes in the cost of such products or services;
- changes in our customers' and potential customers' budgets;
- our ability to control costs, including our operating expenses;
- our ability to hire, train and maintain our direct sales force;
- the timing of satisfying revenue recognition criteria in connection with initial deployment and renewals;
- fluctuations in our effective tax rate; and
- general economic and political conditions, both domestically and internationally.

Any one of these or other factors discussed elsewhere in this report may result in fluctuations in our revenues and operating results, meaning that quarter-to-quarter comparisons of our revenues, results of operations and cash flows may not necessarily be indicative of our future performance.

Because of the fluctuations described above, our ability to forecast revenues is limited and we may not be able to accurately predict our future revenues or results of operations. In addition, we base our current and future expense levels on our operating plans and sales forecasts, and our operating expenses are expected to be relatively fixed in the short term. Accordingly, we may not be able to reduce our costs sufficiently to compensate for an unexpected shortfall in revenues, and even a small shortfall in revenues could disproportionately and adversely affect our financial results for that quarter. The variability and unpredictability of these and other factors could result in our failing to meet or exceed financial expectations for a given period.

Because we generally recognize our subscription revenues ratably over the term of our contract with a customer, fluctuations in sales will not be fully reflected in our operating results until future periods.

Our revenues are primarily generated from subscriptions to our solutions. With the exception of a small number of legacy customers, our customers do not have the right to take possession of our equipment or software platform. Revenues from subscriptions to our software platform is recognized ratably over the subscription period beginning on the date that the subscription is made available to the customer, which we refer to as the “go-live” date. Historically, revenues from additional fees such as setup and training was recognized ratably over the estimated customer life beginning on the go-live date. Beginning on January 1, 2018, we adopted Accounting Standards Codification (“ASC”) Topic 606, *Revenue from Contracts with Customers*, the result of which, among other things, is that such training fees will instead be recognized upon delivery and setup fees are recognized ratably over three years if they are deemed to be a material right. For more information about ASC Topic 606, see Note 3, *Summary of Significant Accounting Policies*, to our condensed consolidated financial statements elsewhere in this Quarterly Report on Form 10-Q. Our agreements with our customers typically range from one to five years. As a result, much of the revenues that we report in each quarter are attributable to agreements entered into during previous quarters. Consequently, a decline in sales, customer renewals or market acceptance of our solutions in any one quarter would not necessarily be fully reflected in the revenues in that quarter, and would negatively affect our revenues and profitability in future quarters. This ratable revenue recognition also makes it difficult for us to rapidly increase our revenues through additional sales in any period, as revenues from new customers generally are recognized over the applicable agreement term. Our subscription-based approach may result in uneven recognition of revenues.

We recognize subscription revenues over the term of a subscription agreement. Once we enter into a contract with a customer, there is a delay until we begin recognizing revenues while we survey the coverage areas, obtain any required consents for installation, and install our sensors, which together can take up to several months or more. We begin recognizing revenues from a sale only when all of these steps are complete and the solution is live.

While most of our customers elect to renew their subscription agreements following the expiration of a term, in some cases, they may not be able to obtain the proper approvals or funding to complete the renewal prior to such expiration. For these customers, we stop recognizing subscription revenues at the end of the current term, even though we may continue to provide services for a period of time while the renewal process is completed. Once the renewal is complete, we then recognize subscription revenues for the period between the expiration of the term of the agreement and the completion of the renewal process. As a result of the widespread destruction caused by recent hurricanes in Puerto Rico

and the U.S. Virgin Islands, we discontinued our service to our customers in those service areas and classified the contracts as expired and stopped recognizing revenues. We cannot be certain when or if the affected customers will resume operations and renew their contracts.

The variation in the timeline for deploying our solutions and completing renewals may result in fluctuations in our revenues, which could cause our results to differ from projections. Additionally, while we generally invoice for 50% of the contract cost upon a customer's go-live date, our cash flows may be volatile and will not match our revenue recognition.

We are in the process of expanding our international operations, which exposes us to significant risks.

We currently operate in a single location outside the United States. A key component to our business strategy is to expand our international operations to increase our revenues from customers outside of the United States as part of our growth strategy. Operating in international markets requires significant resources and management attention and will subject us to regulatory, economic and political risks in addition to those we already face in the United States. In addition, we will need to invest time and resources in understanding the regulatory framework and political environments of our potential customers overseas in order to focus our sales efforts. Because such regulatory and political considerations are likely to vary across jurisdictions, this effort will require additional time and attention from our sales team and could lead to a sales cycle that is longer than our typical process for sales in the United States. We also may need to hire additional employees and otherwise invest in our international operations in order to reach new customers. Because of our limited experience with international operations as well as developing and managing sales in international markets, our international expansion efforts may not be successful.

In addition, we face and will continue to face risks in doing business internationally that could adversely affect our business, including:

- the potential impact of currency exchange fluctuations;
- the difficulty of staffing and managing international operations and the increased operations, travel, shipping and compliance costs associated with having customers in numerous international locations;
- potentially greater difficulty collecting accounts receivable and longer payment cycles;
- the availability of coverage by wireless carriers in international markets;
- higher or more variable costs associated with wireless carriers and other service providers;
- the need to offer customer support in various languages;
- challenges in understanding and complying with local laws, regulations and customs in foreign jurisdictions;
- export controls and economic sanctions administered by the Department of Commerce Bureau of Industry and Security and the Treasury Department's Office of Foreign Assets Control;
- compliance with various anti-bribery and anti-corruption laws such as the Foreign Corrupt Practices Act and United Kingdom Bribery Act of 2010;
- tariffs and other non-tariff barriers, such as quotas and local content rules;
- more limited protection for our intellectual property in some countries;
- adverse or uncertain tax consequences as a result of international operations;
- currency control regulations, which might restrict or prohibit our conversion of other currencies into U.S. dollars;
- restrictions on the transfer of funds;
- deterioration of political relations between the United States and other countries; and
- political or social unrest or economic instability in a specific country or region in which we operate, which could have an adverse impact on our operations in that location.

Also, we expect that due to costs related to our international expansion efforts and the increased cost of doing business internationally, we will incur higher costs to secure sales to international customers than the comparable costs for domestic customers. As a result, our financial results may fluctuate as we expand our operations and customer base worldwide.

Our failure to manage any of these risks successfully could harm our international operations, and adversely affect our business, operating results and financial condition.

We are dependent on the continued services and performance of our senior management and other key personnel, the loss of any of whom could adversely affect our business.

Our future success depends in large part on the continued contributions of our senior management and other key personnel. In particular, the leadership of key management personnel is critical to the successful management of our company, the development of our products, and our strategic direction. We also depend on the contributions of key technical personnel, some of whom are nearing retirement age and in the process of transferring relevant knowledge and expertise to other employees.

We do not maintain “key person” insurance for any member of our senior management team or any of our other key employees. Our senior management and key personnel are all employed on an at-will basis, which means that they could terminate their employment with us at any time, for any reason and without notice. The loss of any of our key management personnel could significantly delay or prevent the achievement of our development and strategic objectives and adversely affect our business.

If we are unable to attract, integrate and retain additional qualified personnel, including top technical talent, our business could be adversely affected.

Our future success depends in part on our ability to identify, attract, integrate and retain highly skilled technical, managerial, sales and other personnel. We face intense competition for qualified individuals from numerous other companies, including other software and technology companies, many of whom have greater financial and other resources than we do. Some of these characteristics may be more appealing to high-quality candidates than those we have to offer. In addition, new hires often require significant training and, in many cases, take significant time before they achieve full productivity. We may incur significant costs to attract and retain qualified personnel, including significant expenditures related to salaries and benefits and compensation expenses related to equity awards, and we may lose new employees to our competitors or other companies before we realize the benefit of our investment in recruiting and training them. Moreover, new employees may not be or become as productive as we expect, as we may face challenges in adequately or appropriately integrating them into our workforce and culture. If we are unable to attract, integrate and retain suitably qualified individuals who are capable of meeting our growing technical, operational and managerial requirements, on a timely basis or at all, our business will be adversely affected.

Volatility or lack of positive performance in our stock price may also affect our ability to attract and retain our key employees. Many of our senior management personnel and other key employees have become, or will soon become, vested in a substantial amount of stock or stock options. Employees may be more likely to leave us if the shares they own or the shares underlying their vested options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the options, or, conversely, if the exercise prices of the options that they hold are significantly above the market price of our common stock. If we are unable to appropriately incentivize and retain our employees through equity compensation, or if we need to increase our compensation expenses in order to appropriately incentivize and retain our employees, our business, operating results and financial condition would be adversely affected.

Changes in tax laws or the adoption of other tax reform policies could materially affect our financial position and results of operations.

On December 22, 2017, the 2017 Tax Cut and Jobs Act (the “Tax Act”) was enacted into law and the new legislation contains several key tax provisions, including a one-time mandatory transition tax on accumulated foreign earnings and a reduction of the corporate income tax rate to 21% effective January 1, 2018, among others. We are required to recognize the effect of the tax law changes in the period of enactment, such as determining the estimated transition tax, re-measuring our U.S. deferred tax assets and liabilities at a 21% rate as well as reassessing the net realizability of our deferred tax assets and liabilities. The one-time transition tax does not generate a tax liability as the deemed distribution is offset by

tax attributes. The provisional amount related to the re-measurement of our deferred tax balance is a reduction of approximately \$9.8 million. Due to the corresponding valuation allowance fully offsetting deferred taxes, there is no impact on our consolidated statements of operations.

In December 2017, the SEC staff issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act (SAB 118) which allows companies to record provisional amounts during a measurement period not to extend beyond one year of the enactment date. Since the Tax Act was passed late in the fourth quarter of 2017, and ongoing guidance and accounting interpretation are expected over the next 12 months, we consider the accounting of the transition tax and deferred tax re-measurements to be incomplete. Additional work will be necessary for a more detailed analysis of our deferred tax assets and liabilities and our historical foreign earnings as well as potential correlative adjustments. We expect to complete our analysis within the measurement period in accordance with SAB 118 and our analysis could result in subsequent adjustment to these amounts.

We may be subject to additional obligations to collect and remit certain taxes, and we may be subject to tax liability for past activities, which could harm our business.

State, local and foreign jurisdictions have differing rules and regulations governing sales, use, value added and other taxes, and these rules and regulations are subject to varying interpretations that may change over time, particularly with respect to software-as-a-service products like our solutions. Further, these jurisdictions' rules regarding tax nexus are complex and vary significantly. If one or more jurisdictions were to assert that we have failed to collect taxes for sales of our solutions, we could face the possibility of tax assessments and audits. A successful assertion that we should be collecting additional sales, use, value added or other taxes in those jurisdictions where we have not historically done so and do not accrue for such taxes could result in substantial tax liabilities and related penalties for past sales or otherwise harm our business and operating results.

Our ability to use our net operating losses to offset future taxable income may be subject to certain limitations.

As of December 31, 2017, we had federal and state net operating loss carryforwards ("NOLs"), of \$80.2 million and \$50.8 million, respectively, due to prior period losses, which expire in various years between 2018 through 2036, if not utilized. In general, under Section 382 of the Internal Revenue Code of 1986, as amended ("the Code"), a corporation that undergoes an "ownership change" is subject to limitations on its ability to utilize its NOLs to offset future taxable income. Past or future changes in our stock ownership, some of which are outside of our control, may have resulted or could result in an ownership change. State NOLs generated in one state cannot be used to offset income generated in another state.

Additionally, the Tax Act changes our ability to utilize future NOL carryforwards. For NOL carryforwards arising in tax years beginning after December 31, 2017, the Tax Act limits a taxpayer's ability to utilize such carryforwards to 80% of taxable income. In addition, NOL carryforwards arising in tax years ending after December 31, 2017 can be carried forward indefinitely, but carryback is generally prohibited. NOL carryforwards generated by us before January 1, 2018 will not be subject to the taxable income limitation and will continue to have a 20-year carryforward period. However, the changes in the carryforward and carryback periods as well as the new limitation on use of NOLs may significantly impact our ability to use NOL carryforwards generated after December 31, 2017, as well as the timing of any such use, and could seriously harm our business. For these reasons, we may not be able to realize a tax benefit from the use of our NOLs, whether or not we attain profitability.

We may be subject to litigation for a variety of claims, which could adversely affect our results of operations, harm our reputation or otherwise negatively impact our business.

We may be subject to litigation for a variety of claims arising from our normal business activities. These may include claims, suits, and proceedings involving labor and employment, wage and hour, commercial and other matters. The outcome of any litigation, regardless of its merits, is inherently uncertain. Any claims and lawsuits, and the disposition of such claims and lawsuits, could be time-consuming and expensive to resolve, divert management attention and resources, and lead to attempts on the part of other parties to pursue similar claims. Any adverse determination related to litigation could adversely affect our results of operations, harm our reputation or otherwise negatively impact our business. In addition, depending on the nature and timing of any such dispute, a resolution of a legal matter could materially affect our future operating results, our cash flows or both.

We are currently facing a lawsuit from three former contractors who allege a breach of contract, conversion, unjust enrichment, promissory estoppel and other related claims that they are entitled to receive options to purchase more than 250,000 shares of our common stock and have petitioned for “millions of dollars” in damages and other costs and expenses. Addressing this claim will require management attention and resources. While we believe these claims are without merit and are disputing them vigorously, we cannot provide assurance as to the outcome of this matter.

An unfavorable outcome on any litigation matters could require us to pay substantial damages, or, in connection with any intellectual property infringement claims, could require us to pay ongoing royalty payments or could prevent us from selling certain of our products. As a result, a settlement of, or an unfavorable outcome on, any of the matters referenced above or other litigation matters could have a material adverse effect on our business, operating results, financial condition and cash flows.

Changes in financial accounting standards may cause adverse and unexpected revenue fluctuations and impact our reported results of operations.

The accounting rules and regulations that we must comply with are complex and subject to interpretation by the Financial Accounting Standards Board (“FASB”), the Securities and Exchange Commission and various bodies formed to promulgate and interpret appropriate accounting principles. In addition, many companies’ accounting disclosures are being subjected to heightened scrutiny by regulators and the public. Further, the accounting rules and regulations are continually changing in ways that could impact our financial statements.

For example, in May 2014, the FASB issued ASC Topic 606, *Revenue from Contracts with Customers* (“Topic 606”). We adopted Topic 606 starting on January 1, 2018. Changes to accounting principles or our accounting policies on our financial statements going forward are difficult to predict, could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of the change. In addition, were we to change our critical accounting estimates, including the timing of recognition of subscription and professional services revenues and other revenue sources, our results of operations could be significantly impacted.

Proposed legislation that would ease restrictions on the purchase of suppressors could impact our business.

Legislation known as the Hearing Protection Act (the “HPA”), was introduced in the U.S. Congress in 2017 and later incorporated into the Sportsmen’s Heritage and Recreational Enhancement Act (the “SHARE Act”). If adopted, such legislation would ease restrictions on the sale of suppressors designed to reduce the noise related to gunshots, and ultimately could lead to increased use of gun suppressors in urban gun crime. While our technology has captured gunshots fired with a suppressor in some cases, we currently do not warrant detection to our customers. While we have not formally tested our detection rate of suppressed gunfire on a wide-scale basis, we continue to evaluate our systems effectiveness at detecting suppressed gunfire on a selected basis. If an increase in the use of suppressors in urban gun crime were to impact the effectiveness of our solutions to the point that customers began to require us to warrant as to the detection of suppressed gunfire, we may be required to deploy our sensors at a greater density per square mile (and thereby increase operating costs) or make potentially costly modifications to our technology, either of which could harm our business. Even with these modifications, there is no guarantee that performance standards on suppressed gunfire will meet our current performance levels or be sufficient to prevent customer losses and associated financial results.

Risks Related to Our Intellectual Property

Failure to protect our intellectual property rights could adversely affect our business.

Our success depends, in part, on our ability to protect proprietary methods and technologies that we develop or license under patent and other intellectual property laws of the United States, so that we can prevent others from using our inventions and proprietary information. If we fail to protect our intellectual property rights adequately, our competitors might gain access to our technology and our business might be adversely affected. However, defending our intellectual property rights might entail significant expenses. Any of our patent rights, copyrights, trademarks or other intellectual property rights may be challenged by others, weakened or invalidated through administrative process or litigation.

As of June 30, 2018, we had 29 U.S. patents directed to our technologies, as well as one granted patent in Israel. We have patent applications pending for examination in the United States, Europe, Mexico and Brazil, but we cannot guarantee that these patent applications will be granted. We also license three other U.S. patents from one or more third parties. The patents that we own or those that we license from others (including those that may be issued in the future) may not provide us with any competitive advantages or may be challenged by third parties.

Additionally, the process of obtaining patent protection is expensive and time-consuming, and we may not be able to prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. Even if issued, there can be no assurance that these patents will adequately protect our intellectual property, as the legal standards relating to the validity, enforceability and scope of protection of patent and other intellectual property rights are uncertain.

Any patents that are issued may subsequently be invalidated or otherwise limited, allowing other companies to develop offerings that compete with ours, which could adversely affect our competitive business position, business prospects and financial condition. In addition, issuance of a patent does not guarantee that we have a right to practice the patented invention. Patent applications in the United States are typically not published until 18 months after their earliest priority date or, in some cases, not at all, and publications of discoveries in industry-related literature lag behind actual discoveries. We cannot be certain that third parties do not have blocking patents that could be used to prevent us from marketing or practicing our software or technology.

Effective patent, trademark, copyright and trade secret protection may not be available to us in every country in which our software is available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the United States (in particular, some foreign jurisdictions do not permit patent protection for software), and mechanisms for enforcement of intellectual property rights may be inadequate. Additional uncertainty may result from changes to intellectual property legislation enacted in the United States, including the recent America Invents Act, or to the laws of other countries and from interpretations of the intellectual property laws of the United States and other countries by applicable courts and agencies. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

We rely in part on trade secrets, proprietary know-how and other confidential information to maintain our competitive position. Although we endeavor to enter into non-disclosure agreements with our employees, licensees and others who may have access to this information, we cannot assure you that these agreements or other steps we have taken will prevent unauthorized use, disclosure or reverse engineering of our technology. Moreover, third parties may independently develop technologies or products that compete with ours, and we may be unable to prevent this competition.

We might be required to spend significant resources to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Litigation also puts our patents at risk of being invalidated or interpreted narrowly and our patent applications at risk of not issuing. Additionally, we may provoke third parties to assert counterclaims against us. We may not prevail in any lawsuits that we initiate, and the damages or other remedies awarded, if any, may not be commercially viable. Any litigation, whether or not resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel, which may adversely affect our business, operating results, financial condition and cash flows.

We may be subject to intellectual property rights claims by third parties, which are extremely costly to defend, could require us to pay significant damages and could limit our ability to use certain technologies.

Companies in the software and technology industries, including some of our current and potential competitors, own large numbers of patents, copyrights, trademarks and trade secrets and frequently enter into litigation based on allegations of infringement or other violations of intellectual property rights. In addition, many of these companies have the capability to dedicate substantially greater resources to enforce their intellectual property rights and to defend claims that may be brought against them. The litigation may involve patent holding companies or other adverse patent owners that have no relevant product revenues and against which our patents may therefore provide little or no deterrence. We may have previously received, and may in the future receive, notices that claim we have misappropriated, misused, or infringed other parties' intellectual property rights, and, to the extent we gain greater market visibility, we face a higher risk of being the subject of intellectual property infringement claims.

There may be third-party intellectual property rights, including issued or pending patents that cover significant aspects of our technologies or business methods. Any intellectual property claims, with or without merit, could be very time-consuming, could be expensive to settle or litigate and could divert our management's attention and other resources. These claims could also subject us to significant liability for damages, potentially including treble damages if we are found to have willfully infringed patents or copyrights. These claims could also result in our having to stop using technology found to be in violation of a third party's rights. We might be required to seek a license for the intellectual property, which may not be available on reasonable terms or at all. Even if a license were available, we could be required to pay significant

royalties, which would increase our operating expenses. As a result, we may be required to develop alternative non-infringing technology, which could require significant effort and expense. If we cannot license or develop technology for any infringing aspect of our business, we would be forced to limit or stop sales of our software and may be unable to compete effectively. Any of these results would adversely affect our business, operating results, financial condition and cash flows.

If we are unable to protect our intellectual property, or if we infringe on the intellectual property rights of others, our business may be harmed.

Our success depends in part on intellectual property rights to the services that we develop. We rely on a combination of contractual and intellectual property rights, including non-disclosure agreements, patents, trade secrets, copyrights and trademarks, to establish and protect our intellectual property rights in our names, services, innovations, methodologies and related technologies. If we lose intellectual property protection or the ability to secure intellectual property protection on any of our names, confidential information or technology, this could harm our business. Our intellectual property rights may not prevent competitors from independently developing services and methodologies similar to ours, and the steps we take might be inadequate to deter infringement or misappropriation of our intellectual property by competitors, former employees or other third parties, any of which could harm our business. We have registered patents and pending patent applications directed to our technology. We have registered trademarks in the United States that have various expiration dates unless renewed through customary processes. Our registered patents and/or trademark registrations may be unenforceable or ineffective in protecting our intellectual property. Most of our patents and pending patent applications have been filed only in the United States and are therefore not enforceable in countries outside of the United States. Our trademarks may be unenforceable in countries outside of the United States, which may adversely affect our ability to build our brand outside of the United States.

Although we are not presently aware that our conduct of our business infringes on the intellectual property rights of others, third parties may nevertheless assert infringement claims against us in the future. We may be required to modify our products, services, internal systems or technologies, or obtain a license to permit our continued use of those rights. We may be unable to do so in a timely manner, or upon reasonable terms and conditions, which could harm our business. In addition, future litigation over these matters could result in substantial costs and resource diversion. Adverse determinations in any litigation or proceedings of this type could subject us to significant liabilities to third parties and could prevent us from using some of our services, internal systems or technologies.

Our use of open source software could subject us to possible litigation.

A portion of our technologies incorporates open source software, and we expect to continue to incorporate open source software into our platform in the future. Few of the licenses applicable to open source software have been interpreted by courts, and their application to the open source software integrated into our proprietary technology platform may be uncertain. If we fail to comply with these licenses, then pursuant to the terms of these licenses, we may be subject to certain requirements, including requirements that we make available the source code for our software that incorporates the open source software. We cannot assure you that we have not incorporated open source software in our software in a manner that is inconsistent with the terms of the applicable licenses or our current policies and procedures. If an author or other third party that distributes such open source software were to allege that we had not complied with the conditions of one or more of these licenses, we could incur significant legal expenses defending against such allegations. Litigation could be costly for us to defend, have a negative effect on our operating results and financial condition or require us to devote additional research and development resources to change our technology platform.

Risks Related to the Ownership of Our Common Stock

Our stock price may be volatile or may decline regardless of our operating performance, resulting in substantial losses for investors.

The market price of our common stock may be highly volatile and may fluctuate substantially as a result of a variety of factors, some of which are related in complex ways. Since shares of our common stock were sold in our IPO, in June 2017 at a price of \$11.00 per share, our stock price has ranged from an intraday low of \$9.33 to an intraday high of \$45.22 through August 2, 2018.

The market price of our common stock may fluctuate significantly in response to numerous factors, many of which are beyond our control, including the factors listed below and other factors described in this “Risk Factors” section:

- actual or anticipated fluctuations in our operating results;
- the financial projections we may provide to the public, any changes in these projections or our failure to meet these projections;
- failure of securities analysts to initiate or maintain coverage of our company, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;
- ratings changes by any securities analysts who follow our company;
- changes in the availability of federal funding to support local law enforcement efforts, or local budgets;
- announcements by us of significant technical innovations, acquisitions, strategic partnerships, joint ventures or capital commitments;
- changes in operating performance and stock market valuations of other software companies generally;
- price and volume fluctuations in the overall stock market, including as a result of trends in the economy as a whole;
- changes in our board of directors or management;
- sales of large blocks of our common stock, including sales by our executive officers, directors and significant stockholders;
- lawsuits threatened or filed against us;
- short sales, hedging and other derivative transactions involving our capital stock;
- general economic conditions in the United States and abroad; and
- other events or factors, including those resulting from war, incidents of terrorism or responses to these events.

In addition, stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many software companies. Stock prices of many software companies have fluctuated in a manner unrelated or disproportionate to the operating performance of those companies. In the past, stockholders have instituted securities action litigation following periods of market volatility. If we were to become involved in securities litigation, it could subject us to substantial costs, divert resources and the attention of management from our business and adversely affect our business, operating results, financial condition and cash flows.

Substantial future sales of shares of our common stock could cause the market price of our common stock to decline.

Approximately 5.3 million shares of our common stock as of June 30, 2018 have the right, subject to various conditions and limitations, to include their shares of our common stock in registration statements relating to our securities including approximately 3.3 million shares that were registered in connection with the Registration Statement on Form S-3 that became effective on July 27, 2018. If the offer and sale of these shares are registered, they will be freely tradable without restriction under the Securities Act. In addition, non-affiliates have the ability to sell shares of our common stock in the open market or through block trades without subject to volume restrictions under Rule 144 of the Securities Act. In addition, in the future we may issue common stock or other securities if we need to raise additional capital. The number of new shares of our common stock issued in connection with raising additional capital could constitute a material portion of the then outstanding shares of our common stock. In the event a large number of shares of common stock are sold in the public market, such share sales could reduce the trading price of our common stock.

If securities or industry analysts do not publish research or reports about our business, or publish negative reports about our business, our share price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business, our market and our competitors. We do not have any control over these analysts. If one or more of the analysts who cover us downgrade our shares of common stock or change their opinion of our shares of common stock, our share price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

We may invest or spend the proceeds of our IPO offering in ways with which you may not agree or in ways that may not yield a return.

We used \$13.7 million of the net proceeds from our IPO during the year ended December 31, 2017 for the repayment of all of our outstanding indebtedness, including early termination fees. We have used, are using and intend to continue to use the remaining net proceeds for working capital and general corporate purposes, including sales and marketing activities, general and administrative matters and capital expenditures. In addition, we may use a portion of the net proceeds we received from our IPO for the acquisition of, or strategic investment in, technologies, solutions or businesses that complement our business, although we currently have no present commitments or agreements to enter into any such acquisition or investment. Our management will have considerable discretion in the application of these remaining net proceeds, and you will not have the opportunity, to assess whether the proceeds are being used appropriately. Such proceeds may be used for purposes that do not increase the value of our business, which could cause the price of our common stock to decline.

We are an “emerging growth company” and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an “emerging growth company,” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”), and we take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We will remain an “emerging growth company” for up to five years, although we will cease to be an “emerging growth company” upon the earliest of (i) the last day of fiscal year 2022, (ii) the last day of the first fiscal year in which our annual gross revenues are \$1.07 billion or more, (iii) the date on which we have, during the previous rolling three-year period, issued more than \$1 billion in non-convertible debt securities or (iv) the date on which we are deemed to be a “large accelerated filer” as defined in the Securities Exchange Act of 1934, or the Exchange Act. We cannot predict if investors will find our common stock less attractive or our company less comparable to certain other public companies because we will rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

We incur substantial costs as a result of being a public company.

As a public company, we are incurring significant levels of legal, accounting, insurance and other expenses that we did not incur as a private company. We are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act, the Dodd-Frank Act, the listing requirements of the Nasdaq Capital Market and other applicable securities rules and regulations. Compliance with these rules and regulations increases our legal and financial compliance costs, makes some activities more difficult, time-consuming or costly and increases demand on our systems and resources as compared to when we operated as a private company. The Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and operating results. The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. In order to maintain and, if required, improve our disclosure controls and procedures and internal control over financial reporting to meet this standard, significant resources and management oversight may be required. As a result, management’s attention may be diverted from other business concerns, which could adversely affect our business and operating results. Although we have already hired additional corporate employees to comply with these requirements, we may need to hire more corporate employees in the future or engage outside consultants, which would increase our costs and expenses.

In addition, changing laws, regulations and standards relating to corporate governance and public disclosure are creating uncertainty for public companies, increasing legal and financial compliance costs and making some activities more time-consuming. These laws, regulations and standards are subject to varying interpretations, in many cases due to their lack of specificity, and, as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. We intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative expenses and a diversion of management's time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to their application and practice, regulatory authorities may initiate legal proceedings against us and our business may be adversely affected.

As a result of disclosure of information in this report and in the filings that we are required to make as a public company, our business, operating results and financial condition have become more visible, which has resulted in, and may in the future result in threatened or actual litigation, including by competitors and other third parties. If any such claims are successful, our business, operating results and financial condition could be adversely affected, and even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the resources of our management and adversely affect our business, operating results and financial condition.

We do not intend to pay dividends for the foreseeable future.

We have never declared or paid any cash dividends on our common stock and do not intend to pay any cash dividends in the foreseeable future. We anticipate that we will retain all of our future earnings for use in the development of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of our board of directors. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments.

Our executive officers, directors and principal stockholders own a significant percentage of our stock and may be able to exert significant control over matters subject to stockholder approval.

Our directors, executive officers and holders of more than 5% of our common stock, certain of which are represented on our board of directors, together with their affiliates, beneficially own a significant portion of the voting power of our outstanding capital stock. As a result, these stockholders may be able to determine the outcome of matters submitted to our stockholders for approval. This ownership could affect the value of your shares of common stock by, for example, these stockholders electing to delay, defer or prevent a change in corporate control, merger, consolidation, takeover or other business combination. This concentration of ownership may also adversely affect the market price of our common stock.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of our company more difficult, limit attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our certificate of incorporation and bylaws may have the effect of delaying or preventing a change of control or changes in our management. Our certificate of incorporation and bylaws include provisions that:

- establish a classified board of directors so that not all members of our board of directors are elected at one time;
- permit the board of directors to establish the number of directors and fill any vacancies and newly-created directorships;
- provide that directors may only be removed for cause;
- require super-majority voting to amend some provisions in our certificate of incorporation and bylaws;
- authorize the issuance of "blank check" preferred stock that our board of directors could use to implement a stockholder rights plan;
- eliminate the ability of our stockholders to call special meetings of stockholders;

- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and
- establish advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted upon by stockholders at annual stockholder meetings.

In addition, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which generally prohibits stockholders owning 15% or more of our outstanding voting stock from merging or otherwise combining with us for a period of three years following the date on which the stockholder became a 15% stockholder without the consent of our board of directors. These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management, and otherwise discourage management takeover attempts.

Our certificate of incorporation designates the Court of Chancery of the State of Delaware as the exclusive forum for certain litigation that may be initiated by our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us.

Pursuant to our certificate of incorporation, unless we consent in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware is the sole and exclusive forum for (1) any derivative action or proceeding brought on our behalf, (2) any action asserting a claim of breach of a fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders, (3) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, our certificate of incorporation or our bylaws or (4) any action asserting a claim governed by the internal affairs doctrine. Our certificate of incorporation further provides that the federal district courts of the United States of America will be the exclusive forum for resolving any complaint asserting a cause of action arising under the Securities Act. Our certificate of incorporation further provides that any person or entity purchasing or otherwise acquiring any interest in shares of our common stock is deemed to have notice of and consented to the foregoing provision. The forum selection clause in our certificate of incorporation may limit our stockholders' ability to obtain a favorable judicial forum for disputes with us.

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

(a) Unregistered Sales of Equity Securities

On May 10, 2018, we issued 52 shares of our common stock to a holder of one of our outstanding warrants upon that holder's exercise pursuant to a cashless exercise provision. The warrant had an exercise price of \$5.8667 per share. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

On May 14, 2018, we issued 632 shares of our common stock to a holder of one of our outstanding warrants upon that holder's exercise pursuant to a cashless exercise provision. The warrant had an exercise price of \$5.8667 per share. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

On May 15, 2018, we issued 105 shares of our common stock to a holder of one of our outstanding warrants upon that holder's exercise pursuant to a cashless exercise provision. The warrant had an exercise price of \$5.8667 per share. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

On June 4, 2018, we issued 2,544 shares of common stock were issued to a holder of one of our outstanding warrants upon the exercise of warrants for cash of \$14,925. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

On June 26, 2018, we issued 26 shares of common stock were issued to a holder of one of our outstanding warrants upon the exercise of warrants for cash of \$153. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

On June 29, 2018, we issued 656 shares of common stock were issued to a holder of one of our outstanding warrants upon the exercise of warrants for cash of \$3,849. The shares of common stock were issued by the Company in reliance on Section 4(a)(2) of the Securities Act of 1933, as amended.

(b) Use of Proceeds

On June 12, 2017, we closed our initial public offering of 3,220,000 shares of common stock at an offering price of \$11.00 per share, which includes 420,000 shares of common stock sold upon full exercise of the underwriters' over-allotment option. The Company received net proceeds of \$32.4 million, after deducting underwriting discounts and commissions. All of the shares issued and sold in our initial public offering were registered under the Securities Act pursuant to a registration statement on Form S-1 (File No. 333-217603), which was declared effective by the SEC on June 6, 2017. Roth Capital Partners acted as sole book-running manager of our initial public offering, Imperial Capital and Northland Capital Markets acted as co-manager and as co-lead manager, respectively.

No offering expenses were paid directly or indirectly to any of our directors or officers (or their associates) or persons owning ten percent or more of any class of our equity securities or to any other affiliates. There has been no material change in the planned use of proceeds from our initial public offering from those disclosed in the final prospectus for our initial public offering dated as of on June 8, 2017 and filed with the SEC pursuant to Rule 424(b)(4).

During the six months ended June 30, 2018, approximately \$4.7 million was used for working capital and general corporate purposes.

Item 6. Exhibits

A list of exhibits is set forth below.

Exhibit Index

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Certificate of Incorporation	8-K	001-38107	3.1	June 13, 2017	
3.2	Amended and Restated Bylaws	8-K	001-38107	3.2	June 13, 2017	
31.1*	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
31.2*	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
32.1*	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					X
101.INS*	XBRL Instance Document					X
101.SCH*	XBRL Taxonomy Extension Schema Document					X
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document					X
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document					X
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document					X
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document					X

* Furnished herewith and not deemed to be “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and shall not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

SIGNATURES

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

SHOTSPOTTER, INC.

Date: August 8, 2018

By: /s/ Ralph A. Clark
Ralph A. Clark
President and Chief Executive Officer

Date: August 8, 2018

By: /s/ Alan R. Stewart
Alan R. Stewart
Chief Financial Officer

CERTIFICATION

I, Ralph A. Clark, certify that:

1. I have reviewed this quarterly report on Form 10-Q of ShotSpotter, Inc.;
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(s) 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(s) 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.

August 8, 2018

/s/ Ralph A. Clark

Ralph A. Clark

President and Chief Executive Officer

CERTIFICATION

I, Alan R. Stewart, certify that:

1. I have reviewed this quarterly report on Form 10-Q of ShotSpotter, Inc.;
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(s) 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(s) 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.

August 8, 2018

/s/ Alan R. Stewart

Alan R. Stewart
Chief Financial Officer

CERTIFICATION

Pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350), Ralph A. Clark, the President, Chief Executive Officer and Director of ShotSpotter, Inc. (the "Company") and Alan R. Stewart, Chief Financial Officer of the Company, each hereby certifies that, to the best of his knowledge:

1. The Company's Quarterly Report on Form 10-Q for the period ended June 30, 2018, to which this Certification is attached as Exhibit 32.1 ("the Quarterly Report") fully complies with the requirements of Section 13(a) or Section 15(d) of the Exchange Act; and

2. The information contained in the Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

In Witness Whereof, the undersigned have set their hands hereto as of the 8th day of August, 2018.

/s/ Ralph A. Clark

Ralph A. Clark

President and Chief Executive Officer

/s/ Alan R. Stewart

Alan R. Stewart

Chief Financial Officer

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of ShotSpotter, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing."