

New Revenue Accounting Standard ASC 606

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Overview of New Revenue Standard (ASC 606)

Revenue is recognized when a customer obtains control of promised goods or services and is recognized in an amount that reflects the consideration that we expect to receive in exchange for those goods and services.

Professional Services:

- Revenue will either be recognized over the contract term of the associated software services contract or over the period of delivery of the professional fees, both of which are typically shorter than the customer relationship period that was previously used under ASC 605.

Brokerage Commissions:

- Commission revenue will be recognized when the orders for the underlying policies have been taken and transferred to the insurance carrier. As a result, revenue from these arrangements will be recognized as a lump sum and in earlier periods under the new standard in comparison to ASC 605 and the timing and amount of revenue recognized for annual and interim periods will change.

Deferral & Amortization of Commission and Fulfillment Costs:

- Assets recognized for the costs to obtain a contract, primarily sales commissions, will be amortized in a consistent manner with the transfer of the services to which the asset relates.
- Assets recognized for the costs to fulfill a contract will be amortized in a manner consistent with the transfer of the services to which the asset relates.

Key Changes to Benefitfocus

	ASC 605	ASC 606
Professional Services Revenue - Carrier segment	Implementation fees recognized over customer relationship period	Implementation fees recognized over contract period
Professional Services Revenue - Employer segment	Implementation fees recognized upon delivery	Implementation fees recognized over the delivery period
Brokerage Commission Revenue - Employer segment	Commissions recognized over policy term	Commission revenue recognized when orders are transferred to the customer
Professional Services Cost of Revenue	Expensed as incurred	Certain upfront customer fulfillment costs capitalized and amortized ratably over expected benefit period
Commissions Expense	Expensed upon booking	Capitalized and amortized ratably over expected benefit period

Selected 2017 GAAP & Non-GAAP Financial Metrics (Unaudited)

ASC 606 Impacts

(in millions)

	ASC 605					Change					ASC 606				
	1Q17	2Q17	3Q17	4Q17	2017	1Q17	2Q17	3Q17	4Q17	2017	1Q17	2Q17	3Q17	4Q17	2017
Revenue:															
Software Services	56.7	53.6	53.1	55.0	218.4	(10.2)	(11.0)	(10.8)	(1.5)	(33.5)	46.5	42.6	42.3	53.5	184.9
Professional Services	7.5	9.7	9.4	11.7	38.3	3.6	2.8	4.5	2.7	13.6	11.1	12.5	13.9	14.4	51.9
Total Revenue	64.2	63.3	62.5	66.7	256.7	(6.6)	(8.2)	(6.3)	1.2	(19.9)	57.6	55.1	56.2	67.9	236.8
Revenue:															
Employer	40.6	38.8	40.2	44.4	164.0	(4.8)	(5.1)	(4.0)	2.5	(11.4)	35.8	33.7	36.2	46.9	152.6
Insurance Carrier	23.6	24.5	22.3	22.3	92.7	(1.8)	(3.1)	(2.3)	(1.3)	(8.5)	21.8	21.4	20.0	21.0	84.2
Total Revenue	64.2	63.3	62.5	66.7	256.7	(6.6)	(8.2)	(6.3)	1.2	(19.9)	57.6	55.1	56.2	67.9	236.8
Margin:															
GAAP Software Gross Margin	61.6%	65.1%	61.6%	57.2%	61.4%	219	(30)	255	1,280	455	63.8%	64.8%	64.2%	70.0%	65.9%
GAAP Professional Service Gross Margin	-31.9%	-3.7%	-8.0%	17.2%	-3.8%	(631)	(1,391)	(784)	(4,331)	(2,006)	-38.2%	-17.6%	-15.9%	-26.1%	-23.9%
GAAP Consolidated Gross Margin	50.8%	54.5%	51.2%	50.2%	51.6%	(664)	(840)	(687)	(53)	(542)	44.1%	46.1%	44.3%	49.7%	46.2%
Non-GAAP Software Gross Margin	62.5%	65.7%	62.5%	58.1%	62.2%	215	(27)	254	1,263	450	64.6%	65.4%	65.0%	70.7%	66.7%
Non-GAAP Professional Service Gross Margin	-29.0%	-1.7%	-5.3%	19.2%	-1.5%	(629)	(1,394)	(804)	(4,295)	(1,998)	-35.3%	-15.7%	-13.4%	-23.7%	-21.5%
Non-GAAP Consolidated Gross Margin	51.8%	55.3%	52.4%	51.3%	52.7%	(652)	(828)	(675)	(55)	(534)	45.3%	47.0%	45.6%	50.7%	47.3%
GAAP Net Loss	(7.7)	(4.5)	(6.7)	(7.0)	(25.9)	(7.9)	(9.2)	(7.4)	0.1	(24.4)	(15.6)	(13.7)	(14.1)	(6.9)	(50.3)
Adjusted EBITDA	3.6	5.4	5.1	5.3	19.4	(7.9)	(9.3)	(7.4)	0.2	(24.4)	(4.3)	(3.9)	(2.3)	5.5	(5.0)

GAAP ASC 606 2017 Income Statement (Unaudited)

(in millions except share and per share data)

	Three Months Ended				
	Mar 31, 2017	June 30, 2017	Sep. 30, 2017	Dec 31, 2017	FY 2017
Revenue	57.6	55.1	56.2	67.9	236.8
Cost of revenue ⁽¹⁾⁽²⁾	32.2	29.7	31.3	34.2	127.4
Gross profit	25.4	25.4	24.9	33.7	109.4
Operating expenses: ⁽¹⁾⁽²⁾					
Sales and marketing	18.0	17.9	16.5	18.2	70.6
Research and development	12.2	12.4	12.6	12.3	49.5
General and administrative	7.8	5.9	6.8	6.8	27.3
Total operating expenses	38.0	36.2	35.9	37.3	147.4
Loss from operations	(12.6)	(10.8)	(11.0)	(3.6)	(38.0)
Other income (expense):					
Interest income	-	-	0.1	0.1	0.2
Interest expense on building lease financing obligations	(1.9)	(1.8)	(1.8)	(2.0)	(7.5)
Interest expense on other borrowings	(1.0)	(1.1)	(1.4)	(1.4)	(4.9)
Other expense	(0.1)	-	-	-	(0.1)
Total other (expense), net	(3.0)	(2.9)	(3.1)	(3.3)	(12.3)
Net loss	(15.6)	(13.7)	(14.1)	(6.9)	(50.3)
Comprehensive loss	(15.6)	(13.7)	(14.1)	(6.9)	(50.3)
Net loss per common share:					
Basic and diluted	\$ (0.51)	\$ (0.45)	\$ (0.45)	\$ (0.22)	\$ (1.62)
Weighted-average common shares outstanding:					
Basic and diluted	30,658,468	31,076,995	31,181,141	31,285,263	31,052,378
*					
(1) Stock-based compensation included in above line items:					
Cost of revenue	0.7	0.5	0.7	0.7	2.5
Sales and marketing	1.3	0.9	1.3	1.4	5.0
Research and development	0.7	0.7	0.7	0.8	3.0
General and administrative	1.7	0.7	1.7	1.6	5.7
(2) Amortization of acquired intangible assets included in above line items:					
Cost of revenue	0.0	0.0	0.0	0.0	0.1
Sales and marketing	0.0	0.0	0.0	0.0	0.1
Research and development	0.0	0.0	0.0	0.0	0.0
General and administrative	0.0	0.0	0.0	0.0	0.0

* The sum of the quarter amounts may not agree with the annual amounts due to rounding

ASC 606 2017 Balance Sheet (Unaudited)

(in millions)

	Three Months Ended			
	Mar 31, 2017	June 30, 2017	Sep 30, 2017	Dec 31, 2017
ASSETS				
Current Assets				
Cash and cash equivalents	57.7	59.4	54.6	55.3
Accounts receivable	27.3	27.8	33.3	30.1
Contract and other current assets	19.2	15.3	10.8	15.9
Total Current Assets	104.2	102.5	98.7	101.3
Property and equipment, net	78.0	76.4	75.0	72.7
Intangible assets, net	0.3	0.3	0.2	0.2
Goodwill	1.6	1.6	1.6	1.6
Deferred costs and other non-current assets	19.9	18.8	17.5	16.2
Total Assets	204.0	199.6	193.0	192.0
LIABILITIES & EQUITY				
Current Liabilities				
Accounts payable	5.0	5.1	1.4	4.3
Accrued expenses	10.1	8.5	8.9	9.1
Accrued compensation and benefits	10.8	14.7	11.9	14.2
Deferred revenue, current portion	35.6	41.4	41.7	43.8
Revolving lines of credit	14.0	20.0	28.0	24.0
Financing and capital lease obligations, current portion	3.2	3.2	3.4	3.4
Total Current Liabilities	78.7	92.9	95.3	98.8
Deferred revenue, net of current portion	18.2	12.5	13.3	11.2
Revolving line of credit, net of current portion	34.2	32.2	32.2	32.2
Financing and capital lease obligations, net of current portion	57.1	56.7	56.1	55.6
Other non-current liabilities	2.8	2.6	2.4	2.9
Total Liabilities	191.0	196.9	199.3	200.7
EQUITY				
Additional paid-in capital	339.5	343.1	347.9	352.5
Retained Earnings	(326.5)	(340.4)	(354.3)	(361.2)
Total Equity	13.0	2.7	(6.4)	(8.7)
Total Liabilities & Equity	204.0	199.6	193.0	192.0

ASC 606 2017 Reconciliation of GAAP and Non-GAAP Financial Measures

	Year Ended December 31, 2017		Year Ended December 31, 2017
Reconciliation from Net Loss to Adjusted EBITDA:		Reconciliation from Net Loss to Non-GAAP Net Loss:	
Net Loss	\$ (50.3)	Net Loss	\$ (50.3)
Depreciation	12.4	Costs not core to business	1.1
Amortization of software development costs	3.3	Amortization of acquired intangible assets	0.3
Amortization of acquired intangible assets	0.3	Stock-based compensation expense	16.1
Interest income	(0.2)	Total net adjustments	17.5
Interest expense on building lease financing obligations	7.4	Non-GAAP Net Loss	\$ (32.8)
Interest expense on other borrowings	4.9		
Income tax expense	0.0		
Stock-based compensation expense	16.1		
Costs not core to business	1.1		
Total net adjustments	45.3		
Adjusted EBITDA	\$ (5.0)		

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