

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

Form 10-Q

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2017
- 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 1-34761



AutoWeb, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

33-0711569
(I.R.S. Employer Identification Number)

18872 MacArthur Boulevard, Suite 200, Irvine, California
(Address of principal executive offices)

92612
(Zip Code)

(949) 225-4500
(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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
Non-accelerated filer
(Do not check if a smaller reporting company)

Accelerated filer
Smaller reporting company

Emerging growth company

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 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 October 30, 2017, there were 13,083,313 shares of the Registrant's Common Stock, \$0.001 par value, outstanding.

INDEX

PART I. FINANCIAL INFORMATION

Page

ITEM 1.	Financial Statements	
	Unaudited Consolidated Condensed Balance Sheets as of September 30, 2017 and December 31, 2016	1
	Unaudited Consolidated Condensed Statements of Income and Comprehensive Income for the Three and Nine Months Ended September 30, 2017 and 2016	2
	Unaudited Consolidated Condensed Statements of Cash Flows for the Nine Months Ended September 30, 2017 and 2016	3
	Notes to Unaudited Consolidated Condensed Financial Statements	4
ITEM 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations	15
ITEM 3.	Quantitative and Qualitative Disclosures About Market Risk	20
ITEM 4.	Controls and Procedures	20
<u>PART II. OTHER INFORMATION</u>		
ITEM 2.	Unregistered Sales of Equity Securities and Use of Proceeds	21
ITEM 6.	Exhibits	22
	Signatures	23

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

AUTOWEB, INC.
UNAUDITED CONSOLIDATED CONDENSED BALANCE SHEETS
(Amounts in thousands, except share and per-share data)

	September 30,	December 31,
	2017	2016
Assets		
Current assets:		
Cash and cash equivalents	\$ 44,696	\$ 38,512
Short-term investment	253	251
Accounts receivable, net of allowances for bad debts and customer credits of \$975 and \$1,015 at September 30, 2017 and December 31, 2016, respectively	27,503	33,634
Deferred tax asset	—	4,669
Prepaid expenses and other current assets	1,293	901
Total current assets	73,745	77,967
Property and equipment, net	4,635	4,430
Investments	680	680
Intangible assets, net	20,290	23,783
Goodwill	42,821	42,821
Long-term deferred tax asset	25,837	14,799
Other assets	667	801
Total assets	<u>\$ 168,675</u>	<u>\$ 165,281</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 10,054	\$ 9,764
Accrued employee-related benefits	2,215	4,530
Other accrued expenses and other current liabilities	7,518	8,315
Current portion of term loan payable	4,875	6,563
Total current liabilities	24,662	29,172
Convertible note payable	1,000	1,000
Long-term portion of term loan payable	5,250	7,500
Borrowings under revolving credit facility	8,000	8,000
Total liabilities	38,912	45,672
Commitments and contingencies (Note 10)	—	—
Stockholders' equity:		
Preferred stock, \$0.001 par value, 11,445,187 shares authorized		
Series A Preferred stock, none issued and outstanding	—	—
Series B Preferred stock, none and 168,007 shares issued and outstanding at September 30, 2017 and December 31, 2016, respectively	—	—
Common stock, \$0.001 par value; 55,000,000 shares authorized and 13,082,948 and 11,012,625 shares issued and outstanding at September 30, 2017 and December 31, 2016, respectively	13	11
Additional paid-in capital	352,810	350,022
Accumulated deficit	(223,060)	(230,424)
Total stockholders' equity	129,763	119,609
Total liabilities and stockholders' equity	<u>\$ 168,675</u>	<u>\$ 165,281</u>

See accompanying notes to unaudited consolidated condensed financial statements.

AUTOWEB, INC.
UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME
(Amounts in thousands, except per-share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenues:				
Lead fees	\$ 27,711	\$ 36,202	\$ 83,149	\$ 98,706
Advertising	8,946	7,371	24,914	16,412
Other revenues	215	338	741	1,188
Total revenues	36,872	43,911	108,804	116,306
Cost of revenues	25,786	28,156	74,171	72,995
Gross profit	11,086	15,755	34,633	43,311
Operating expenses:				
Sales and marketing	3,692	3,964	10,684	14,026
Technology support	3,141	2,943	9,582	10,775
General and administrative	2,844	3,346	9,116	10,405
Depreciation and amortization	1,192	1,270	3,623	3,809
Litigation settlements	(26)	(24)	(76)	(25)
Total operating expenses	10,843	11,499	32,929	38,990
Operating income	243	4,256	1,704	4,321
Interest and other income (expense), net	(93)	(206)	(289)	(643)
Income before income tax provision	150	4,050	1,415	3,678
Income tax provision	81	1,312	539	1,185
Net income and comprehensive income	\$ 69	\$ 2,738	\$ 876	\$ 2,493
Basic earnings per common share	\$ 0.01	\$ 0.26	\$ 0.08	\$ 0.23
Diluted earnings per common share	\$ 0.01	\$ 0.21	\$ 0.07	\$ 0.19

See accompanying notes to unaudited consolidated condensed financial statements.

AUTOWEB, INC.
UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Amounts in thousands)

	Nine Months Ended	
	September 30,	
	2017	2016
Cash flows from operating activities:		
Net income	\$ 876	\$ 2,493
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,499	5,492
Provision for bad debts	294	225
Provision for customer credits	29	411
Share-based compensation	2,918	3,171
Loss on disposal of assets	7	—
Change in deferred tax asset	119	553
Changes in assets and liabilities:		
Accounts receivable	5,808	(4,590)
Prepaid expenses and other current assets	(392)	196
Other assets	132	156
Accounts payable	290	3,747
Accrued expenses and other current liabilities	(3,112)	189
Non-current liabilities	—	38
Net cash provided by operating activities	12,468	12,081
Cash flows from investing activities:		
Investment in GoMoto	—	(375)
Purchase of intangible asset	(600)	—
Purchases of property and equipment	(1,618)	(1,871)
Net cash used in investing activities	(2,218)	(2,246)
Cash flows from financing activities:		
Payments on term loan borrowings	(3,938)	(3,938)
Proceeds from exercise of stock options	1,068	2,877
Repurchase of common stock	(1,196)	—
Payment of contingent fee arrangement	—	(38)
Net cash used in financing activities	(4,066)	(1,099)
Net increase in cash and cash equivalents	6,184	8,736
Cash and cash equivalents, beginning of period	38,512	23,993
Cash and cash equivalents, end of period	\$ 44,696	\$ 32,729
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	\$ 445	\$ 261
Cash paid for interest	\$ 648	\$ 661

See accompanying notes to unaudited consolidated condensed financial statements.

AUTOWEB, INC.
NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

1. Organization and Operations

AutoWeb, Inc. (“**AutoWeb**” or “**Company**”) is an automotive marketing services company that assists automotive retail dealers (“**Dealers**”) and automotive manufacturers (“**Manufacturers**”) market and sell new and used vehicles through its programs for online lead referrals, Dealer marketing products and services, online advertising and consumer traffic referral programs and mobile products.

The Company’s consumer-facing automotive websites (“**Company Websites**”) provide consumers with information and tools to aid them with their automotive purchase decisions and the ability to submit inquiries requesting Dealers to contact the consumers regarding purchasing or leasing vehicles (“**Leads**”). Leads are internally-generated from our Company Websites or acquired from third parties that generate Leads from their websites. The Company’s AutoWeb® consumer traffic referral product provides consumers who are shopping for vehicles online with targeted offers based on make, model and geographic location. As these consumers conduct online research on a Company Website or on the site of one of the Company’s network of automotive publishers, they are presented with relevant offers on a timely basis and, upon the consumer clicking on the displayed advertisement, are sent to the appropriate website location of one of the Company’s Dealer, Manufacturer or advertising customers.

The Company was incorporated in Delaware on May 17, 1996. Its principal corporate offices are located in Irvine, California. The Company’s common stock is listed on The Nasdaq Capital Market under the symbol AUTO.

On October 9, 2017, the Company changed its name from Autobytel Inc. to AutoWeb, Inc. In connection with this name change, the Company’s stock ticker symbol was changed from “ABTL” to “AUTO” on The Nasdaq Capital Market.

2. Basis of Presentation

The accompanying unaudited consolidated condensed financial statements are presented on the same basis as the Company’s Annual Report on Form 10-K for the year ended December 31, 2016 (“**2016 Form 10-K**”) filed with the Securities and Exchange Commission (“**SEC**”). AutoWeb has made its disclosures in accordance with U.S. generally accepted accounting principles (“**GAAP**”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation with respect to interim financial statements, have been included. The consolidated condensed statements of income and comprehensive income and cash flows for the periods ended September 30, 2017 and 2016 are not necessarily indicative of the results of operations or cash flows expected for the year or any other period. The unaudited consolidated condensed financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto in the 2016 Form 10-K.

3. Recent Accounting Pronouncements

Issued but not yet adopted by the Company

Accounting Standards Codification 606 “Revenue from Contracts with Customers.” In May 2014, Accounting Standards Update (“**ASU**”) No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” was issued. This ASU requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The standard will replace most existing revenue recognition guidance in GAAP when it becomes effective. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. In April 2016, ASU No. 2016-10, “Identifying Performance Obligations and Licensing” was issued. This ASU clarifies, i) the identification of performance obligations and, ii) licensing implementation guidance as it relates to Topic 606, Revenue from Contracts with Customers. In May 2016, ASU No. 2016-12, “Narrow-Scope Improvements and Practical Expedients” was issued. This ASU addresses certain issues as it relates to assessing collectability, presentation of sales taxes, noncash consideration, and completed contracts and contract modifications at transition as it relates to Topic 606, Revenue from Contracts with Customers. This ASU and related amendments are effective for public entities for annual periods beginning after December 15, 2017, including interim periods therein. The Company expects to adopt the ASU on a modified retrospective transition method and continues to evaluate the effect this guidance will have on the consolidated financial statements. The Company also believes the new disclosure requirements under ASC 2014-09 will have a significant impact to the consolidated financial statements.

Table of Contents

Accounting Standards Codification 842 "Leases." In February 2016, ASU No. 2016-02, "Leases (Topic 842)" was issued. This ASU will require lessees to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases of terms more than 12 months. The ASU will require both capital and operating leases to be recognized on the balance sheet. Qualitative and quantitative disclosures will also be required to help investors and other financial statement users better understand the amount, timing and uncertainty of cash flows arising from leases. The ASU will take effect for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Company expects this standard will have a material effect on its consolidated financial statements due to the recognition of new right-of-use assets and lease liabilities on its balance sheet for real estate and equipment operating leases. The Company is continuing to evaluate the effect this guidance will have on the consolidated financial statements and related disclosures.

Accounting Standards Codification 805 "Business Combinations." In January 2017, ASU No. 2017-01, "Clarifying the Definition of a Business" was issued. This ASU provides a more robust framework to use in determining when a set of assets and activities is a business. The amendments in this ASU are effective for annual periods beginning after December 15, 2017, and interim periods within those periods. The Company does not believe this ASU will have a material effect on the consolidated financial statements and related disclosures.

Accounting Standards Codification 350 "Intangibles – Goodwill and Other." In January 2017, ASU No. 2017-04, "Simplifying the Test for Goodwill Impairment" was issued. Under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss should not exceed the total amount of goodwill allocated to that reporting unit. The ASU also eliminated the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity should apply this ASU on a prospective basis and for its annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. The Company is continuing to evaluate the effect this guidance will have on the consolidated financial statements and related disclosures.

Accounting Standards Codification 718 "Compensation – Stock Compensation." In May 2017, ASU No. 2017-09, "Scope of Modification Accounting" was issued. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should apply this ASU on a prospective basis for an award modified on or after the adoption date for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted. The Company does not believe this ASU will have a material effect on the consolidated financial statements and related disclosures.

Recently adopted by the Company

Accounting Standards Codification 740 "Income Taxes." In November 2015, ASU No. 2015-17, "Balance Sheet Classification of Deferred Taxes" was issued. This ASU requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this update apply to all entities that present a classified statement of financial position. The Company adopted this ASU prospectively on January 1, 2017 and reclassified \$4.7 million of current deferred tax assets to long-term deferred tax assets. Prior periods were not retrospectively adjusted.

Accounting Standards Codification 323 "Investments-Equity Method and Joint Ventures." In March 2016, ASU No. 2016-07, "Simplifying the Transition to the Equity Method of Accounting" was issued. This ASU eliminates the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment was held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Thus, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The Company adopted this ASU on January 1, 2017 and it did not have a material effect on the consolidated financial statements.

Accounting Standards Codification 718 "Compensation-Stock Compensation." In March 2016, ASU No. 2016-09, "Improvements to Employee Share-Based Payment Accounting" was issued. This ASU provides for areas of simplification for several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows.

The changes in the new standard eliminate the accounting for excess tax benefits to be recognized in additional paid-in capital and tax deficiencies recognized either in the income tax provision or in additional paid-in capital. ASU 2016-09 requires recognition of excess tax benefits and tax deficiencies in the income statement on a prospective basis. For the nine months ended September 30, 2017, the Company recognized all excess tax benefits and tax deficiencies as income tax expense or benefit as a discrete event. Income tax benefit of approximately \$28,000 was recognized in the nine months ended September 30, 2017 as a result of the adoption of ASU 2016-09.

Table of Contents

The Company adopted the amendments on January 1, 2017 related to the timing of when excess tax benefits are recognized on a modified retrospective transition method. The Company recognized \$6.5 million of deferred tax assets relating to unrealized stock option benefits, resulting in a cumulative \$6.5 million adjustment to retained earnings.

The treatment of forfeitures has not changed as the Company is electing to continue its current process of estimating the number of forfeitures. As such, this has no cumulative effect on retained earnings. The Company has elected to present the cash flow statement on a prospective transition method and no prior periods have been adjusted.

The Company calculates diluted earnings per share using the treasury stock method for share-based payment awards. ASU 2016-09 eliminates excess tax benefits and deficiencies from the calculation of assumed proceeds under the treasury stock method, which the Company adopted on a prospective transition method.

Accounting Standards Codification 230 "Statement of Cash Flows." In August 2016, ASU No. 2016-15, "Classification of Certain Cash Receipts and Cash Payments" was issued. This ASU provides guidance on eight specific cash flow issues with the objective of reducing the existing diversity in practice for those issues. The amendments in this ASU are effective for annual periods beginning after December 15, 2017, and interim periods within those annual periods. The Company early adopted this ASU on January 1, 2017 and it did not have a material effect on the consolidated financial statements.

Accounting Standards Codification 810 "Consolidation." In October 2016, ASU No. 2016-17, "Interests Held through Related Parties That Are Under Common Control" was issued. This ASU amends the consolidation guidance on how a reporting entity that is the single decision maker of a variable interest entity ("VIE") should treat indirect interests in the entity held through related parties that are under common control with the reporting entity when determining whether it is the primary beneficiary of that VIE. The amendments in this ASU are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company adopted this ASU on January 1, 2017 and it did not have a material effect on the consolidated financial statements.

4. Disposal of Specialty Finance Leads Product

On December 19, 2016, AutoWeb and Car.com, Inc., a wholly owned subsidiary of AutoWeb ("Car.com"), entered into an Asset Purchase and Sale Agreement, by and among AutoWeb, Car.com, and Internet Brands, Inc., a Delaware corporation ("Internet Brands"), pursuant to which Internet Brands acquired substantially all of the assets of the automotive specialty finance leads group of Car.com ("Acquired Group"). The transaction was completed effective as of December 31, 2016. The transaction consideration consisted of \$3.2 million in cash paid at closing and \$1.6 million to be paid over a five-year period pursuant to a Transitional License and Linking Agreement ("Specialty Finance Leads License Agreement"). The Company recorded a gain on sale of approximately \$2.2 million in connection with the transaction in December 2016.

In connection with the transaction, Internet Brands, Car.com and AutoWeb entered into the Specialty Finance Leads License Agreement pursuant to which Car.com and AutoWeb will provide to Internet Brands certain transition services and arrangements. Pursuant to the Specialty Finance Leads License Agreement, (i) Internet Brands will pay AutoWeb \$1.6 million in fees over the five-year term of the Specialty Finance Leads License Agreement, and (ii) Car.com will (1) grant Internet Brands a limited, non-exclusive, non-transferable license to use the Car.com logo and name solely for sales and marketing purposes in Internet Brand's automotive specialty finance leads business; and (2) provide certain redirect linking of consumer traffic from the Acquired Group's current specialty finance leads application forms to a landing page designated by Internet Brands. The Company received \$0.2 million and recorded a \$0.1 million receivable during the nine months ended September 30, 2017 related to the Specialty Finance Leads License Agreement.

The disposal of the automotive specialty finance leads product did not qualify for presentation and disclosure as a discontinued operation because it did not represent a strategic shift that had or will have a major effect on the Company's operations. The pretax profit of the finance leads product for the three and nine months ended September 30, 2016 was \$0.1 million and \$0.4 million, respectively.

5. Net Earnings Per Share and Stockholders' Equity

Basic net earnings per share is computed using the weighted average number of common shares outstanding during the period, excluding any unvested restricted stock. Diluted net earnings per share is computed using the weighted average number of common shares, and if dilutive, potential common shares outstanding, as determined under the treasury stock and if-converted methods, during the period. Potential common shares consist of common shares issuable upon the exercise of stock options, common shares issuable upon the exercise of warrants, common shares issuable upon conversion of convertible notes and unvested restricted stock. The following are the share amounts utilized to compute the basic and diluted net earnings per share for the three and nine months ended September 30, 2017 and 2016:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Basic Shares:				
Weighted average common shares outstanding	12,881,812	10,842,853	11,729,181	10,729,802
Weighted average common shares repurchased	(60,230)	—	(20,297)	—
Weighted average unvested restricted stock	(119,584)	(116,667)	(115,574)	(120,134)
Basic Shares	<u>12,701,998</u>	<u>10,726,186</u>	<u>11,593,310</u>	<u>10,609,668</u>
Diluted Shares:				
Basic shares	12,701,998	10,726,186	11,593,310	10,609,668
Weighted average dilutive securities	498,587	931,175	621,449	880,653
Incremental shares from convertible preferred stock	—	1,680,070	1,064,660	1,680,070
Diluted Shares	<u>13,200,585</u>	<u>13,337,431</u>	<u>13,279,419</u>	<u>13,170,391</u>

For the three months ended September 30, 2017, weighted average dilutive securities included dilutive options and restricted stock awards. For the nine months ended September 30, 2017, weighted average dilutive securities included dilutive options, restricted stock awards and incremental shares of common stock issued in June 2017 upon the conversion of the Series B Junior Participating Convertible Preferred Stock, par value \$0.001 per share (“**Series B Preferred Stock**”), that was issued in connection with the October 2015 acquisition of AutoWeb, Inc. (“**AWI**”). For the three months ended September 30, 2016, weighted average dilutive securities included dilutive options, restricted stock awards, the warrant and convertible note issued in connection with the acquisition of AutoUSA, LLC (“**AutoUSA**”) on January 13, 2014 (“**AutoUSA Acquisition Date**”) and shares of Series B Preferred Stock issued in connection with the AWI acquisition prior to the conversion of the Series B Preferred Stock. For the nine months ended September 30, 2016, weighted average dilutive securities included dilutive options, restricted stock awards, the warrant issued in connection with the acquisition of AutoUSA and shares of Series B Preferred Stock issued in connection with the AWI acquisition prior to the conversion of the Series B Preferred Stock.

For the three and nine months ended September 30, 2017, 3.9 million and 3.1 million of potentially anti-dilutive securities related to common stock have been excluded from the calculation of diluted net earnings per share, respectively. For both the three and nine months ended September 30, 2016, 2.0 million of potentially anti-dilutive securities related to common stock have been excluded from the calculation of diluted net earnings per share.

On June 7, 2012, the Company announced that its board of directors had authorized the Company to repurchase up to \$2.0 million of the Company’s common stock, and on September 17, 2014 the Company announced that the board of directors had approved the repurchase of up to an additional \$1.0 million of the Company’s common stock. The Company repurchased 145,821 shares of the Company’s common stock with an average price of \$8.20 per share during the three and nine months ended September 30, 2017. No shares were repurchased during the three and nine months ended September 30, 2016. The repurchase of the Company’s common stock during the three months ended September 30, 2017 completes the previously authorized stock repurchase programs. On September 6, 2017, the Company announced that its board of directors had authorized the Company to repurchase up to \$3.0 million of the Company’s common stock. The authorization may be increased or otherwise modified, renewed, suspended or terminated by the Company at any time, without prior notice. The Company may repurchase the Company’s common stock from time to time on the open market or in private transactions. Shares repurchased under this program have been retired and returned to the status of authorized and unissued shares. The Company funded repurchases and anticipates that the Company would fund future repurchases through the use of available cash. The repurchase authorization does not obligate the Company to repurchase any particular number of shares. The timing and actual number of repurchases of additional shares, if any, under the Company’s stock repurchase program will depend upon a variety of factors, including price, market conditions, release of quarterly and annual earnings, and other legal, regulatory, and corporate considerations at the Company’s sole discretion. The impact of repurchases on the Company’s Tax Benefit Preservation Plan, as amended, and on the Company’s use of its net operating loss carryovers and other tax attributes if the Company were to experience an “ownership change,” as defined in Section 382 of the Internal Revenue Code, is also a factor that the Company considers in connection with share repurchases. As of September 30, 2017, \$3.0 million remains available for repurchase under the program.

On June 22, 2017, the Company obtained stockholder approval for the issuance of shares of the Company’s common stock upon (i) the conversion of the Company’s then outstanding Series B Preferred Stock; and (ii) the conversion of shares of Series B Preferred Stock that would be issued upon exercise of the AWI Warrant (described below). Upon obtaining stockholder approval for the conversion, each share of Series B Preferred Stock outstanding was automatically converted into 10 shares of the Company’s common stock, which resulted in the outstanding shares of Series B Preferred Stock being converted into 1,680,070 shares of the Company’s common stock, and the AWI Warrant converted into warrants to acquire up to 1,482,400 shares of the Company’s common stock.

[Table of Contents](#)

Warrants. The warrant to purchase 69,930 shares of the Company’s common stock issued in connection with the acquisition of AutoUSA was valued at \$7.35 per share for a total value of \$0.5 million (“**AutoUSA Warrant**”). The Company used an option pricing model to determine the value of the AutoUSA Warrant. Key assumptions used in valuing the AutoUSA Warrant are as follows: risk-free rate of 1.6%, stock price volatility of 65.0% and a term of 5.0 years. The AutoUSA Warrant was valued based on long-term stock price volatilities of the Company. The exercise price of the AutoUSA Warrant is \$14.30 per share (as may be adjusted for stock splits, stock dividends, combinations and other similar events). The AutoUSA Warrant became exercisable on January 13, 2017 and expires on January 13, 2019.

The warrant to purchase up to 148,240 shares of Series B Preferred Stock issued in connection with the acquisition of AWI (“**AWI Warrant**”) was valued at \$1.72 per share for a total value of \$2.5 million. The Company used an option pricing model to determine the value of the AWI Warrant. Key assumptions used in valuing the AWI Warrant are as follows: risk-free rate of 1.9%, stock price volatility of 74.0% and a term of 7.0 years. The AWI Warrant was valued based on long-term stock price volatilities of the Company’s common stock. On June 22, 2017, the Company received stockholder approval which resulted in the automatic conversion of the AWI Warrant into warrants to acquire up to 1,482,400 shares of the Company’s common stock at an exercise price of \$18.45 per share of common stock. The AWI Warrant becomes exercisable on October 1, 2018, subject to the following vesting conditions: (i) with respect to the first one-third (1/3) of the warrant shares, if at any time after the issuance date of the AWI Warrant and prior to the expiration date of the AWI Warrant the weighted average closing price of the Company’s common stock for the preceding 30 trading days (adjusted for any stock splits, stock dividends, reverse stock splits or combinations of the Company’s common stock occurring after the issuance date) (“**Weighted Average Closing Price**”) is at or above \$30.00; (ii) with respect to the second one-third (1/3) of the warrant shares, if at any time after the issuance date of the AWI Warrant and prior to the expiration date the Weighted Average Closing Price is at or above \$37.50; and (iii) with respect to the last one-third (1/3) of the warrant shares, if at any time after the issuance date of the AWI Warrant and prior to the expiration date the Weighted Average Closing Price is at or above \$45.00. The AWI Warrant expires on October 1, 2022.

6. Share-Based Compensation

Share-based compensation expense is included in costs and expenses in the accompanying Unaudited Consolidated Condensed Statements of Income and Comprehensive Income as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
	<i>(in thousands)</i>			
Share-based compensation expense:				
Cost of revenues	\$ 20	\$ 19	\$ 59	\$ 47
Sales and marketing [1]	409	384	1,222	1,358
Technology support [2]	138	83	401	513
General and administrative	397	460	1,238	1,267
Share-based compensation costs	<u>964</u>	<u>946</u>	<u>2,920</u>	<u>3,185</u>
Amount capitalized to internal use software	<u>1</u>	<u>6</u>	<u>2</u>	<u>14</u>
Total share-based compensation costs	<u>\$ 963</u>	<u>\$ 940</u>	<u>\$ 2,918</u>	<u>\$ 3,171</u>

- (1) Certain awards were modified in connection with the termination of an executive officer’s employment with the Company and their vesting accelerated in accordance with the terms of the applicable option agreements. The total expense related to these modifications and acceleration of vested awards was approximately \$0.3 million in the nine months ended September 30, 2016.
- (2) The vesting of certain awards was accelerated in accordance with the terms of the applicable option agreements in connection with the termination of an executive officer’s employment with the Company. The total expense related to acceleration of vested awards was approximately \$0.2 million in the nine months ended September 30, 2016.

[Table of Contents](#)

Service-Based Options. The Company granted the following service-based options for the three and nine months ended September 30, 2017 and 2016:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Number of service-based options granted	83,850	314,000	457,100	805,400
Weighted average grant date fair value	\$ 3.72	\$ 7.40	\$ 6.29	\$ 7.73
Weighted average exercise price	\$ 7.23	\$ 15.51	\$ 12.51	\$ 16.26

These options are valued using a Black-Scholes option pricing model and generally vest one-third on the first anniversary of the grant date and ratably over twenty-four months thereafter. The vesting of these awards is contingent upon the employee's continued employment with the Company during the vesting period and vesting may be accelerated in the event of a change in control of the Company.

Market Condition Options. On January 21, 2016, the Company granted 100,000 stock options to its chief executive officer with an exercise price of \$17.09 and grant date fair value of \$1.47 per option, using a Monte Carlo simulation model ("**CEO Market Condition Options**"). The CEO Market Condition Options were previously valued at \$2.94 per option but were revalued when the requisite stockholder approval for the Company's Amended and Restated 2014 Equity Incentive Plan was obtained in June 2016. The CEO Market Condition Options are subject to both stock price-based and service-based vesting requirements that must be satisfied for the CEO Market Condition Options to vest and become exercisable. The CEO Market Condition Options provide that the stock price-based vesting condition will be met (i) with respect to the first one-third (1/3) of the CEO Market Condition Options, if at any time after the grant date and prior to the expiration date of the CEO Market Condition Options the Weighted Average Closing Price is at or above \$30.00; (ii) with respect to the second one-third (1/3) of the CEO Market Condition Options, if at any time after the grant date and prior to the expiration date the Weighted Average Closing Price is at or above \$37.50; and (iii) with respect to the last one-third (1/3) of the CEO Market Condition Options, if at any time after the grant date and prior to the expiration date the Weighted Average Closing Price is at or above \$45.00. With respect to any of the CEO Market Condition Options for which the stock price-based requirements are met, these options are also subject to the following service-based vesting schedule: (i) thirty-three and one-third percent (33 1/3%) of these options vested on January 21, 2017 and (ii) one thirty-sixth (1/36th) of these options will vest on each successive monthly anniversary thereafter for the following twenty-four months ending on January 21, 2019. None of the stock-price based vesting requirements have been met as of September 30, 2017. The CEO Market Condition Options expire on January 21, 2023.

Stock option exercises. The following stock options were exercised during the three and nine months ended September 30, 2017 and 2016, respectively:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Number of stock options exercised	15,000	176,388	191,074	334,861
Weighted average exercise price	\$ 4.20	\$ 7.99	\$ 5.58	\$ 8.59

The grant date fair value of stock options granted during these periods was estimated using the Black-Scholes option pricing model using the following weighted average assumptions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Dividend yield	—	—	—	—
Volatility	63%	59%	62%	58%
Risk-free interest rate	1.8%	1.1%	1.8%	1.2%
Expected life (years)	4.4	4.4	4.4	4.4

Upon adoption of ASU 2016-09, "Improvements to Employee Share-Based Payment Accounting," the Company elected to estimate the number of forfeitures.

Restricted Stock Awards. The Company granted an aggregate of 125,000 restricted stock awards (“RSAs”) on April 23, 2015 in connection with the promotion of one of its executive officers. Of the 125,000 RSAs, 25,000 were service-based and the forfeiture restrictions lapse with respect to one-third of the restricted stock on each of the first, second and third anniversaries of the date of the award. Forfeiture restrictions lapsed on 8,333 shares of restricted stock on April 23, 2016 and April 23, 2017, respectively. This executive officer was also awarded 100,000 shares of the Company’s common stock in the form of performance-based restricted stock. The shares are subject to forfeiture upon the earlier of (such earliest date being referred to as the “**Termination Date**”) (i) a termination of the executive officer’s employment with the Company; (ii) March 31, 2018; and (iii) other events of forfeiture set forth in the award agreement, subject to the following: (i) the forfeiture restrictions with respect to 50,000 of the restricted shares will lapse if any time prior to the Termination Date the weighted average closing price of the Company’s common stock for the preceding 30 trading days is at or above \$30.00 per share, and (ii) the forfeiture restrictions with respect to any of the restricted shares that remain subject to forfeiture restrictions will lapse if any time prior to the Termination Date the weighted average closing price of the Company’s common stock for the preceding 30 trading days is at or above \$45.00 per share. None of the forfeiture restrictions on the performance-based restricted stock awards lapsed during the three and nine months ended September 30, 2017.

The Company granted an aggregate of 345,000 RSAs on September 27, 2017 to executive officers of the Company. The RSAs are service-based and the forfeiture restrictions lapse with respect to one-third of the restricted stock on each of the first, second and third anniversaries of the date of the award. Lapsing of the forfeiture restrictions may be accelerated in the event of a change in control of the Company and will accelerate upon the death or disability of the holder of the RSAs.

7. Investments

The Company’s investments at September 30, 2017 and December 31, 2016 consisted primarily of investments in privately-held SaleMove, Inc., a Delaware corporation (“**SaleMove**”), and GoMoto, Inc., a Delaware corporation (“**GoMoto**”).

In September 2013, the Company entered into a Convertible Note Purchase Agreement with SaleMove in which AutoWeb invested \$150,000 in SaleMove in the form of an interest bearing, convertible promissory note. In November 2014, the Company invested an additional \$400,000 in SaleMove in the form of an interest bearing, convertible promissory note. Upon closing of a preferred stock financing by SaleMove in July 2015, these two notes were converted in accordance with their terms into an aggregate of 190,997 Series A Preferred Stock, which shares are classified as a long-term investment on the consolidated balance sheet as of September 30, 2017.

In October 2013, the Company entered into a Reseller Agreement with SaleMove to become a reseller of SaleMove’s technology for enhancing communications with consumers. SaleMove’s technology allows Dealers and Manufacturers to enhance the online shopping experience by interacting with consumers in real-time, including live video, audio and text-based chat or by phone. The Company and SaleMove share equally in revenues from automotive-related sales of the SaleMove products and services. In connection with this reseller arrangement, the Company advanced to SaleMove \$1.0 million to fund SaleMove’s 50% share of various product development, marketing and sales costs and expenses, with the advanced funds to be recovered by the Company from SaleMove’s share of sales revenue. SaleMove advances are repaid to the Company from SaleMove’s share of net revenues and expenses from the Reseller Agreement. As of September 30, 2017, the net advances due from SaleMove totaled \$448,000 and are recorded as an other long-term asset on the Unaudited Consolidated Condensed Balance Sheets.

In December 2014, the Company entered into a Series Seed Preferred Stock Purchase Agreement with GoMoto in which the Company paid \$100,000 for 317,460 shares of Series Seed Preferred Stock, \$0.001 par value per share. The \$100,000 investment in GoMoto was recorded at cost because the Company does not have significant influence over GoMoto. In October 2015 and May 2016, the Company invested an additional \$375,000 and \$375,000, respectively, in GoMoto in the form of convertible promissory notes (“**GoMoto Notes**”). The GoMoto Notes accrue interest at an annual rate of 4.0% and are due and payable in full upon demand by the Company or at GoMoto’s option ten days’ written notice unless converted prior to the repayment of the GoMoto Notes. The GoMoto Notes will be converted into preferred stock of GoMoto in the event of a preferred stock financing by GoMoto of at least \$1.0 million prior to repayment of the GoMoto Notes. As of September 30, 2017, the Company maintains a reserve of \$0.8 million related to the GoMoto Notes and related interest receivable because the Company believes the amounts may not be recoverable.

8. Selected Balance Sheet Accounts

Property and Equipment. Property and equipment consists of the following:

	September 30, 2017	December 31, 2016
	<i>(in thousands)</i>	
Computer software and hardware	\$ 11,103	\$ 12,027
Capitalized internal use software	5,590	5,359
Furniture and equipment	1,707	1,332
Leasehold improvements	1,502	1,139
	<u>19,902</u>	<u>19,857</u>
Less—Accumulated depreciation and amortization	(15,267)	(15,427)
Property and Equipment, net	<u>\$ 4,635</u>	<u>\$ 4,430</u>

The Company periodically reviews the value of long-lived assets to determine if there are any impairment indicators. The Company assesses the impairment of these assets, or the need to accelerate amortization, whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The Company's judgments regarding the existence of impairment indicators are based on legal factors, market conditions and operational performance of the Company's long-lived assets. If such indicators exist, the Company evaluates the assets for impairment based on the estimated future undiscounted cash flows expected to result from the use of the assets and their eventual disposition. Should the carrying amount of an asset exceed its estimated future undiscounted cash flows, an impairment loss is recorded for the excess of the asset's carrying amount over its fair value. Fair value is generally determined based on a valuation process that provides an estimate of the fair value of these assets using an undiscounted cash flow model, which includes assumptions and estimates.

Concentration of Credit Risk and Risks Due to Significant Customers. Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. Cash and cash equivalents are primarily maintained with two high credit quality financial institutions in the United States. Deposits held by banks exceed the amount of insurance provided for such deposits. These deposits may be redeemed upon demand.

Accounts receivable are primarily derived from fees billed to Dealers and Manufacturers. The Company generally requires no collateral to support its accounts receivables and maintains an allowance for bad debts for potential credit losses.

The Company has a concentration of credit risk with its automotive industry related accounts receivable balances, particularly with Urban Science Applications (which represents Acura, Audi, Honda, Nissan, Infiniti, Subaru, Toyota, Volkswagen and Volvo), Media.net Advertising and General Motors. During the first nine months of 2017, approximately 33% of the Company's total revenues was derived from these three customers, and approximately 43%, or \$12.2 million of gross accounts receivables, related to these three customers at September 30, 2017. During the first nine months of 2016, approximately 27% of the Company's total revenues was derived from Urban Science Applications, Ford Direct and Trilogy, and approximately 40%, or \$13.0 million of gross accounts receivables, related to these three customers at September 30, 2016.

Intangible Assets. The Company amortizes specifically identified definite-lived intangible assets using the straight-line method over the estimated useful lives of the assets. The Company's intangible assets will be amortized over the following estimated useful lives (in thousands):

Definite-lived Intangible Asset	Estimated Useful Life	September 30, 2017			December 31, 2016		
		Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Trademarks/trade names/licenses/domains	3 – 7 years	\$ 6,119	\$ (3,511)	\$ 2,608	\$ 9,294	\$ (6,756)	\$ 2,538
Software and publications	3 years	1,300	(1,300)	—	1,300	(1,300)	—
Customer relationships	2 - 10 years	19,563	(9,780)	9,783	19,563	(7,454)	12,109
Employment/non-compete agreements	1-5 years	1,510	(1,488)	22	1,510	(1,273)	237
Developed technology	5-7 years	8,955	(3,278)	5,677	8,955	(2,256)	6,699
		<u>\$ 37,447</u>	<u>\$ (19,357)</u>	<u>\$ 18,090</u>	<u>\$ 40,622</u>	<u>\$ (19,039)</u>	<u>\$ 21,583</u>

[Table of Contents](#)

Indefinite-lived Intangible Asset	Estimated Useful Life	September 30, 2017			December 31, 2016		
		Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Trademark	Indefinite	\$ 2,200	\$ —	\$ 2,200	\$ 2,200	\$ —	\$ 2,200

Amortization expense is included in “Cost of revenues” and “Depreciation and amortization” in the Unaudited Consolidated Condensed Statements of Income. Amortization expense was \$1.3 million and \$4.1 million for the three and nine months ended September 30, 2017, respectively. Amortization expense was \$1.5 million and \$4.3 million for the three and nine months ended September 30, 2016, respectively.

Amortization expense for the remainder of the year and for future years is as follows:

Year	Amortization Expense (in thousands)
2017	\$ 1,313
2018	5,114
2019	3,741
2020	2,310
2021	2,201
2022	1,604
Thereafter	1,807
	<u>\$ 18,090</u>

Goodwill. Goodwill represents the excess of the purchase price over the fair value of net assets acquired. Goodwill is not amortized and is assessed annually for impairment or earlier, when events or circumstances indicate that the carrying value of such assets may not be recoverable. The Company did not record impairment related to goodwill as of September 30, 2017 and December 31, 2016.

Accrued Expenses and Other Current Liabilities. Accrued expenses and other current liabilities consisted of the following:

	September 30, 2017	December 31, 2016
	(in thousands)	
Accrued employee-related benefits	\$ 2,215	\$ 4,530
Other accrued expenses and other current liabilities:		
Other accrued expenses and current liabilities	7,087	7,849
Amounts due to customers	431	466
Total other accrued expenses and other current liabilities	<u>7,518</u>	<u>8,315</u>
Total accrued expenses and other current liabilities	<u>\$ 9,733</u>	<u>\$ 12,845</u>

Convertible Notes Payable. In connection with the acquisition of AutoUSA, the Company issued a convertible subordinated promissory note for \$1.0 million (“AutoUSA Note”) to AutoNationDirect.com, Inc. The fair value of the AutoUSA Note as of the AutoUSA Acquisition Date was \$1.3 million. This valuation was estimated using a binomial option pricing method. Key assumptions used by the Company’s outside valuation consultants in valuing the AutoUSA Note included a market yield of 1.6% and stock price volatility of 65.0%. As the AutoUSA Note was issued with a substantial premium, the Company recorded the premium as additional paid-in capital. Interest is payable at an annual interest rate of 6% in quarterly installments. The entire outstanding balance of the AutoUSA Note is to be paid in full on January 31, 2019. The holder of the AutoUSA Note may at any time convert all or any part, but at least 30,600 shares, of the then outstanding and unpaid principal of the AutoUSA Note into fully paid shares of the Company’s common stock at a conversion price of \$16.34 per share (as adjusted for stock splits, stock dividends, combinations and other similar events). In the event of default, the entire unpaid balance of the AutoUSA Note will become immediately due and payable and will bear interest at the lower of 8% per year and the highest legal rate permissible under applicable law.

9. Credit Facility

The Company and MUFG Union Bank, N.A. (“**Union Bank**”), have entered into a Loan Agreement dated February 26, 2013, as amended on September 10, 2013, January 13, 2014, May 20, 2015, June 1, 2016 and June 28, 2017 (the original Loan Agreement, as amended to date, is referred to collectively as the “**Credit Facility Agreement**”). The Credit Facility Agreement provides for (i) a \$9.0 million term loan (“**Term Loan 1**”); (ii) a \$15.0 million term loan (“**Term Loan 2**”); and (iii) an \$8.0 million working capital revolving line of credit (“**Revolving Loan**”).

Term Loan 1 is amortized over a period of four years, with fixed quarterly principal payments of \$562,500. Borrowings under Term Loan 1 bear interest at either (i) the bank’s Reference Rate (prime rate) minus 0.50% or (ii) the London Interbank Offering Rate (“**LIBOR**”) plus 2.50%, at the option of the Company. Interest under Term Loan 1 adjusts (i) at the end of each LIBOR rate period (1, 2, 3, 6 or 12 months terms) selected by the Company, if the LIBOR rate is selected; or (ii) with changes in Union Bank’s Reference Rate, if the Reference Rate is selected. Borrowings under Term Loan 1 are secured by a first priority security interest on all of the Company’s personal property (including, but not limited to, accounts receivable) and proceeds thereof. Term Loan 1 matures on December 31, 2017. Borrowing under Term Loan 1 was limited to use for the acquisition of AutoUSA, and the Company drew down the entire \$9.0 million of Term Loan 1, together with \$1.0 million under the Revolving Loan, in financing this acquisition. The outstanding balance of Term Loan 1 as of September 30, 2017 was \$1.1 million and is classified as a current liability on the Unaudited Consolidated Condensed Balance Sheets.

Term Loan 2 is amortized over a period of five years, with fixed quarterly principal payments of \$750,000. Borrowings under Term Loan 2 bear interest at either (i) LIBOR plus 3.00% or (ii) the bank’s Reference Rate (prime rate), at the option of the Company. Borrowings under the Revolving Loan bear interest at either (i) the LIBOR plus 2.50% or (ii) the bank’s Reference Rate (prime rate) minus 0.50%, at the option of the Company. Interest under both Term Loan 2 and the Revolving Loan adjust (i) at the end of each LIBOR rate period (1, 2, 3, 6 or 12 months terms) selected by the Company, if the LIBOR rate is selected; or (ii) with changes in Union Bank’s Reference Rate, if the Reference Rate is selected. The Company paid an upfront fee of 0.10% of the Term Loan 2 principal amount upon drawing upon Term Loan 2 and also pays a commitment fee of 0.10% per year on the unused portion of the Revolving Loan, payable quarterly in arrears. Borrowings under Term Loan 2 and the Revolving Loan are secured by a first priority security interest on all of the Company’s personal property (including, but not limited to, accounts receivable) and proceeds thereof. Term Loan 2 matures June 30, 2020. Pursuant to the Fifth Amendment to the Loan Credit Facility Agreement dated as of June 28, 2017, (i) the maturity date of the Revolving Loan was extended from April 30, 2018 to January 5, 2021 and (ii) the maturity date of the Standby Letter of Credit Sublimit under the Revolving Loan was extended from April 30, 2019 to January 5, 2022. Borrowings under the Revolving Loan may be used as a source to finance working capital, capital expenditures, acquisitions and stock repurchases and for other general corporate purposes. Borrowing under Term Loan 2 was limited to use for the acquisition of Dealix Corporation and Autotegrity, Inc. (collectively, “**Dealix/Autotegrity**”) in May 2015 and the Company drew down the entire \$15.0 million of Term Loan 2, together with \$2.75 million under the Revolving Loan and \$6.76 million from available cash on hand, in financing this acquisition. The outstanding balances of Term Loan 2 and the Revolving Loan as of September 30, 2017 were \$9.0 million and \$8.0 million, respectively.

The Credit Facility Agreement contains certain customary affirmative and negative covenants and restrictive and financial covenants, including that the Company maintain specified levels of minimum consolidated liquidity and quarterly and annual earnings before interest, taxes and depreciation and amortization, which the Company was in compliance with as of September 30, 2017.

10. Commitments and Contingencies

Employment Agreements

The Company has employment agreements and severance benefits/retention agreements with certain key employees. A number of these agreements require severance payments and continuation of certain insurance benefits in the event of a termination of the employee’s employment by the Company without cause or by the employee for good reason (as defined in these agreements). Stock option agreements and restricted stock award agreements with some key employees provide for acceleration of vesting of stock options and lapsing of forfeiture restrictions on restricted stock in the event of a change in control of the Company, upon termination of employment by the Company without cause or by the employee for good reason, or upon the employee’s death or disability.

Litigation

From time to time, the Company may be involved in litigation matters arising from the normal course of its business activities. Such litigation, even if not meritorious, could result in substantial costs and diversion of resources and management attention, and an adverse outcome in litigation could materially adversely affect its business, results of operations, financial condition and cash flows.

11. Income Taxes

The Company has adopted the provisions of ASU 2016-09 as of January 1, 2017 which requires recognition through opening retained earnings of any pre-adoption date net operating loss (“NOL”) carryforwards from nonqualified stock options and other employee share-based payments (e.g., restricted shares and share appreciation rights), as well as recognition of all income tax effects from share-based payments arising on or after January 1, 2017 in income tax expense. As a result, the Company has recognized through opening retained earnings \$18.4 million of pre-adoption date NOL carryforwards with remaining carryforward periods of at least seven years (the corresponding deferred tax asset is \$6.5 million). No valuation allowance is needed as the newly recognized NOL is considered more likely than not realizable given that it has sufficient positive sources of taxable income including continued profitability and utilization of NOLs, taxable reversing temporary differences and reliable forecast of income.

On an interim basis, the Company estimates what its anticipated annual effective tax rate will be and records a quarterly income tax provision in accordance with the estimated annual rate, plus the tax effect of certain discrete items that arise during the quarter. As the fiscal year progresses, the Company refines its estimates based on actual events and financial results during the year. This process can result in significant changes to the Company’s estimated effective tax rate. When this occurs, the income tax provision is adjusted during the quarter in which the estimates are refined so that the year-to-date provision reflects the estimated annual effective tax rate. These changes, along with adjustments to the Company’s deferred taxes and related valuation allowance, may create fluctuations in the overall effective tax rate from quarter to quarter.

The Company’s effective tax rate for the three and nine months ended September 30, 2017 differed from the U.S. federal statutory rate primarily due to state income taxes and tax deficiencies from stock-based compensation.

The total amount of unrecognized tax benefits, excluding associated interest and penalties, was \$0.5 million as of September 30, 2017, all of which, if subsequently recognized, would have affected the Company’s tax rate.

As of September 30, 2017 and December 31, 2016, the total balance of accrued interest and penalties related to uncertain tax positions was zero. The Company recognizes interest and penalties related to uncertain tax positions as a component of income tax expense, and the accrued interest and penalties are included in deferred and other long-term liabilities in the Company’s condensed consolidated balance sheets. There were no material interest or penalties included in income tax expense for the three and nine months ended September 30, 2017 and September 30, 2016.

The Company is subject to taxation in the U.S. and in various foreign and state jurisdictions. Due to expired statutes of limitation, the Company’s federal income tax returns for years prior to calendar year 2014 are not subject to examination by the U.S. Internal Revenue Service. Generally, for the majority of state jurisdictions where the Company does business, periods prior to calendar year 2013 are no longer subject to examination. The Company does not anticipate a significant change to the total amount of unrecognized tax benefits within the next twelve months. Audit outcomes and the timing of settlements are subject to significant uncertainty.

12. Subsequent Event

On October 5, 2017, the Company and DealerX Partners, LLC, a Florida limited liability company (“**DealerX**”), entered into a Master License and Services Agreement (“**DealerX License Agreement**”). Pursuant to the terms of the DealerX License Agreement, AutoWeb will receive a perpetual license to access and use DealerX’s proprietary platform and technology for targeted, online marketing. DealerX will operate the platform for AutoWeb and provide enhancements to and support for the DealerX platform for an initial five year period (“**Platform Support Obligations**”).

The transaction consideration consisted of: (i) \$8.0 million in cash paid to DealerX upon execution of the DealerX License Agreement and (ii) the right to 710,856 shares of the Company’s common stock, par value \$0.001 per share, representing approximately five percent of the Company’s outstanding Common Stock as of the date the parties entered into the DealerX License Agreement (“**Market Capitalization Shares**”) if on or before October 5, 2022: (i) AutoWeb’s market capitalization averages at least \$225.0 million over a consecutive 90 day period or (ii) there is a change in control of AutoWeb that reflects a market capitalization of at least \$225.0 million. If the Market Capitalization Shares are issued to DealerX, DealerX’s Platform Support Obligations will continue in perpetuity. Alternatively, upon the occurrence of certain events prior to the issuance of the Market Capitalization Shares, AutoWeb may elect to make an additional lump-sum payment of \$12.5 million (**Alternative Cash Payment**) in order to extend DealerX’s Platform Support Obligations in perpetuity. If the Alternative Cash payment is made, DealerX’s contingent right to receive the Market Capitalization Shares will be terminated.

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

Cautionary Note Concerning Forward-Looking Statements

The Securities and Exchange Commission ("SEC") encourages companies to disclose forward-looking information so that investors can better understand a company's future prospects and make informed investment decisions. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "anticipates," "could," "may," "estimates," "expects," "projects," "intends," "plans," "believes," "will" and words of similar substance used in connection with any discussion of future operations or financial performance identify forward-looking statements. In particular, statements regarding expectations and opportunities, industry trends, new product expectations and capabilities, and our outlook regarding our performance and growth are forward-looking statements. This Quarterly Report on Form 10-Q also contains statements regarding plans, goals and objectives. There is no assurance that we will be able to carry out our plans or achieve our goals and objectives or that we will be able to do so successfully on a profitable basis. These forward-looking statements are just predictions and involve risks and uncertainties, many of which are beyond our control, and actual results may differ materially from these statements. Factors that could cause actual outcomes or results to differ materially from those reflected in forward-looking statements include, but are not limited to, those discussed in this Item 2 and under the heading "Risk Factors" in our annual report on Form 10-K for the year ended December 31, 2016 ("**2016 Form 10-K**"). Investors are urged not to place undue reliance on forward-looking statements. Forward-looking statements speak only as of the date on which they were made. Except as may be required by law, we do not undertake any obligation, and expressly disclaim any obligation, to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise. All forward-looking statements contained herein are qualified in their entirety by the foregoing cautionary statements.

You should read the following discussion of our results of operations and financial condition in conjunction with our unaudited consolidated condensed financial statements and related notes included in Part I, Item 1 of this Quarterly Report on Form 10-Q and our audited consolidated financial statements and the notes thereto in the 2016 Form 10-K.

Our corporate website is located at www.autoweb.com. Information on our website is not incorporated by reference in this Quarterly Report on Form 10-Q. At or through the Investor Relations section of our website we make available free of charge our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and all amendments to these reports as soon as practicable after the reports are electronically filed with or furnished to the SEC.

Unless the context otherwise requires, the terms "we", "us", "our", "AutoWeb" and "Company" refer to AutoWeb, Inc. and its consolidated subsidiaries.

Basis of Presentation and Critical Accounting Policies

See Note 2, *Basis of Presentation*, to the accompanying unaudited consolidated condensed financial statements.

We prepare our financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP"), which require us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, actual results could differ materially from our estimates. To the extent that there are material differences between these estimates and our actual results, our financial condition or results of operations may be affected. For a detailed discussion of the application of our critical accounting policies, see Note 2 of the "Notes to Consolidated Financial Statements" in Part II, Item 8 "Financial Statements and Supplementary Data" in the 2016 Form 10-K. There have been no changes to our critical accounting policies since we filed our 2016 Form 10-K.

Recent Disposal

On December 19, 2016, AutoWeb and Car.com entered into an Asset Purchase and Sale Agreement with Internet Brands pursuant to which Internet Brands acquired substantially all of the assets of the automotive specialty finance leads group of Car.com. The transaction was completed effective as of December 31, 2016. The transaction consideration consisted of \$3.2 million in cash and \$1.6 million to be paid over a five year period pursuant to a Transitional License and Linking Agreement. The Company recorded a gain on sale of approximately \$2.2 million in connection with the transaction in the fourth quarter of 2016.

For additional information concerning this disposal, see Note 4, *Disposal of Specialty Finance Leads Product*, Notes to Unaudited Consolidated Condensed Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Overview

We are an automotive marketing services company that assists automotive retail dealers (“**Dealers**”) and automotive manufacturers (“**Manufacturers**”) market and sell new and used vehicles to consumers through our programs for online lead referrals, Dealer marketing products and services, online advertising and consumer traffic referral programs and mobile products.

Our consumer-facing automotive websites (“**Company Websites**”) provide consumers with information and tools to aid them with their automotive purchase decisions and the ability to submit inquiries requesting Dealers to contact the consumers regarding purchasing or leasing vehicles (“**Leads**”). Leads are internally-generated from our Company Websites (“**Internally-Generated Leads**”) or acquired from third parties (“**Non-Internally-Generated Leads**”) that generate Leads from their websites. Our AutoWeb® consumer traffic referral product provides consumers who are shopping for vehicles online with targeted offers based on make, model and geographic location. As these consumers conduct online research on a Company Website or on the site of one of our network of automotive publishers, they are presented with relevant offers on a timely basis and, upon the consumer clicking on the displayed advertisement, are sent to the appropriate website location of one of our Dealer, Manufacturer or advertising customers.

Our business, results of operations and financial condition are impacted by the volume and quality of our Leads. We measure Lead quality by the conversion of Leads to actual vehicle sales, which we refer to as the “buy rate.” Buy rate is the percentage of the consumers submitting Leads that we delivered to our customers represented by the number of these consumers who purchased vehicles within ninety days of the date of the Lead submission. We rely on detailed feedback from Manufacturers and wholesale customers to confirm the performance of our Leads. Our Manufacturer and other wholesale customers each match the Leads we deliver to our customers against vehicle sales to provide us with information about vehicle purchases by the consumers who submitted Leads that we delivered to these customers. AutoWeb also obtains vehicle registration data from a third party provider. This information, together with our internal analysis allows us to estimate the buy rates for the consumers who submitted the Internally Generated Leads and Non-Internally Generated Leads that we delivered to our customers, and based on these estimates, to estimate an industry average buy rate. Based on the most current information and our internal analysis, we have estimated that, on average, consumers who submit Internally-Generated Leads that we deliver to our customers have an estimated buy rate of approximately 18%. Buy rates that individual Dealers may achieve can be impacted by factors such as the strength of processes and procedures within the dealership to manage communications and follow up with consumers.

The paid search field has become more complex, with many of our paid traffic partners moving towards audience expansion marketing. During the quarter ended June 30, 2017, we identified that some of these audience expansions were not converting to automotive purchases at a range of close rates acceptable to us. This led us to halt these traffic campaigns in the second quarter. We are actively working to implement solutions, and have already begun to rebuild our original high-quality traffic stream. We are also continually looking to expand our methods and sources of traffic generation for both Leads and clicks, and are constantly using close rate data to identify if these new sources of traffic are performing to our high quality standards. Given the actions we are taking to address these traffic issues, and the widely accepted expectation for auto sales to decline in 2017, we expect to continue to experience an impact to revenue and margins at least for the remainder of the year ending December 31, 2017.

For the three and nine months ended September 30, 2017 our business, results of operations and financial condition were affected, and may continue to be affected in the future, by general economic, employment and market factors, conditions in the automotive industry, the markets for Leads and online advertising services, including, but not limited to, the following:

- Vehicle pricing.
- Purchase, lease and financing incentives for vehicles.
- The expectation that consumers will be purchasing fewer vehicles overall during their lifetime as a result of better quality vehicles and longer warranties.
- The impact of fuel prices on demand for the number and types of vehicles.
- Increases or decreases in the number of retail Dealers or in the number of wholesale customers in our customer base.
- The shift in the mix of our customers from retail customers (that purchase our products and services at higher margins) to Manufacturers and other wholesale customers (that purchase our products and services at lower margins).
- The effect of changes in search engine algorithms and methodologies on our Lead generation and website advertising activities and the resulting impact on pricing, Lead quality and margins.
- Volatility in spending by Manufacturers and others in their marketing budgets and allocations.
- The impact of competition and consolidation in the online automotive consumer referral industry.
- The effect of changes in transportation policies to increase public transit options and the impact of ride-sharing options, all of which may affect the desire or need by consumers to lease or purchase new or used vehicles, which in turn may adversely impact the volume of vehicle sales and leases.
- The increased focus in the automotive industry on sales of used vehicles, and our increasing investment in our used vehicle products and services to address this industry shift.

On October 5, 2017, we acquired a license to access and use a third party’s proprietary platform and technology for targeted, online marketing. See Note 12, Subsequent Event, Notes to Unaudited Consolidated Condensed Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Results of Operations

Three Months Ended September 30, 2017 Compared to the Three Months Ended September 30, 2016

The following table sets forth certain statement of income data for the three-month periods ended September 30, 2017 and 2016 (certain amounts may not calculate due to rounding):

	<u>2017</u>	<u>% of total revenues</u>	<u>2016</u>	<u>% of total revenues</u>	<u>\$ Change</u>	<u>% Change</u>
	<i>(Dollar amounts in thousands)</i>					
Revenues:						
Lead fees	\$ 27,711	75%	\$ 36,202	82%	\$ (8,491)	(23)%
Advertising	8,946	24	7,371	17	1,575	21
Other revenues	215	1	338	1	(123)	(36)
Total revenues	36,872	100	43,911	100	(7,039)	(16)
Cost of revenues	25,786	70	28,156	64	(2,370)	(8)
Gross profit	11,086	30	15,755	36	(4,669)	(30)
Operating expenses:						
Sales and marketing	3,692	10	3,964	9	(272)	(7)
Technology support	3,141	9	2,943	7	198	7
General and administrative	2,844	7	3,346	7	(502)	(15)
Depreciation and amortization	1,192	3	1,270	3	(78)	(6)
Litigation settlements	(26)	—	(24)	—	(2)	8
Total operating expenses	10,843	29	11,499	26	(656)	(6)
Operating income	243	1	4,256	10	(4,013)	(94)
Interest and other income (expense), net	(93)	—	(206)	(1)	113	(55)
Income before income tax provision	150	—	4,050	9	(3,900)	(96)
Income tax provision	81	—	1,312	3	(1,231)	(94)
Net income	\$ 69	—%	\$ 2,738	6%	\$ (2,669)	(97)%

Leads. Lead fees revenues decreased \$8.5 million, or 23%, in the third quarter of 2017 compared to the third quarter of 2016 primarily as a result of the elimination of poor quality traffic in the second quarter of 2017 coupled with the disposal of our specialty finance leads product in December 2016.

Advertising. Advertising revenues increased \$1.6 million, or 21%, in the third quarter of 2017 compared to the third quarter of 2016 as a result of an increase in click revenue associated with increased click volume and pricing.

Other Revenues. Other revenues consist primarily of revenues from our mobile products and revenues from our Reseller Agreement with SaleMove. Other revenues decreased to \$0.2 million in the third quarter of 2017 from \$0.3 million in the third quarter of 2016 primarily due to lower customer utilization of the mobile product.

Cost of Revenues. Cost of revenues consists of purchase request and traffic acquisition costs and other cost of revenues. Purchase request and traffic acquisition costs consist of payments made to our purchase request providers, including internet portals and online automotive information providers. Other cost of revenues consists of search engine marketing (“SEM”) and fees paid to third parties for data and content, including search engine optimization activity, included on our websites, connectivity costs, development costs related to our websites, compensation related expense and technology license fees, server equipment depreciation and technology amortization directly related to the Company Websites. SEM, sometimes referred to as paid search marketing, is the practice of bidding on keywords on search engines to drive traffic to a website.

Cost of revenues decreased \$2.4 million, or 8%, in the third quarter of 2017 compared to the third quarter of 2016 primarily due to decreased traffic acquisition costs associated with the reduction in lead volume combined with the decrease in cost of revenues associated with the specialty finance divestiture effective December 31, 2016.

Sales and Marketing. Sales and marketing expense includes costs for developing our brand equity, personnel costs and other costs associated with Dealer sales, website advertising, Dealer support and bad debt expense. Sales and marketing expense in the third quarter of 2017 decreased \$0.3 million, or 7%, compared to the third quarter of 2016 due primarily to lower headcount related costs.

Technology Support. Technology support expense includes compensation, benefits, software licenses and other direct costs incurred by the Company to enhance, manage, maintain, support, monitor and operate the Company’s websites and related technologies, and to operate the Company’s internal technology infrastructure. Technology support expense in the third quarter of 2017 increased by \$0.2 million, or 7%, compared to the third quarter of 2016 due primarily to lower software capitalization of development costs.

[Table of Contents](#)

General and Administrative. General and administrative expense consists of executive, financial and legal personnel expenses and costs related to being a public company. General and administrative expense in the third quarter of 2017 decreased by \$0.5 million, or 15%, from the third quarter of 2016 due to lower headcount related costs.

Depreciation and Amortization. Depreciation and amortization expense in the third quarter of 2017 decreased \$78,000 to \$1.2 million compared to \$1.3 million in the third quarter of 2016 primarily due to normal amortization.

Litigation Settlements. Payments received primarily from 2010 settlements of patent infringement claims against third parties relating to the third parties' methods of Lead delivery were \$26,000 for the third quarter of 2017 compared to \$24,000 in the third quarter of 2016.

Interest and Other Income (Expense), Net. Interest and other income (expense), net was \$0.1 million for the third quarter of 2017 compared to \$0.2 million in the third quarter of 2016. Interest expense decreased to \$198,000 in the third quarter of 2017 from \$212,000 in the third quarter of 2016 primarily due to a decreased balance on our term loans. We also recorded \$0.1 million in other income during the third quarter of 2017 related to the Specialty Finance Leads License Agreement with Internet Brands.

Income Taxes. Income tax expense was \$81,000 in the third quarter of 2017 compared to income tax expense of \$1.3 million in the third quarter of 2016. Income tax expense for the third quarter of 2017 differed from the federal statutory rate primarily due to state income taxes and the impact of stock-based compensation.

Nine Months Ended September 30, 2017 Compared to the Nine Months Ended September 30, 2016

The following table sets forth certain statement of income data for the nine-month periods ended September 30, 2017 and 2016 (certain amounts may not calculate due to rounding):

	<u>2017</u>	<u>% of total revenues</u>	<u>2016</u>	<u>% of total revenues</u>	<u>\$ Change</u>	<u>% Change</u>
	<i>(Dollar amounts in thousands)</i>					
Revenues:						
Lead fees	\$ 83,149	76%	\$ 98,706	85%	\$ (15,557)	(16)%
Advertising	24,914	23	16,412	14	8,502	52
Other revenues	741	1	1,188	1	(447)	(38)
Total revenues	108,804	100	116,306	100	(7,502)	(6)
Cost of revenues	74,171	68	72,995	63	1,176	2
Gross profit	34,633	32	43,311	37	(8,678)	(20)
Operating expenses:						
Sales and marketing	10,684	10	14,026	12	(3,342)	(24)
Technology support	9,582	9	10,775	9	(1,193)	(11)
General and administrative	9,116	8	10,405	9	(1,289)	(12)
Depreciation and amortization	3,623	3	3,809	3	(186)	(5)
Litigation settlements	(76)	—	(25)	—	(51)	204
Total operating expenses	32,929	30	38,990	33	(6,061)	(16)
Operating income	1,704	2	4,321	4	(2,617)	(61)
Interest and other income (expense), net	(289)	(1)	(643)	(1)	354	(55)
Income before income tax provision	1,415	1	3,678	3	(2,263)	(62)
Income tax provision	539	—	1,185	1	(646)	(55)
Net income	<u>\$ 876</u>	<u>1%</u>	<u>\$ 2,493</u>	<u>2%</u>	<u>\$ (1,617)</u>	<u>(65)%</u>

Leads. Lead fees revenues decreased \$15.6 million, or 16%, in the first nine months of 2017 compared to the first nine months of 2016 primarily as a result of the elimination of poor quality traffic in the second quarter of 2017 coupled with the disposal of our specialty finance leads product in December 2016.

Advertising. Advertising revenues increased \$8.5 million, or 52%, in the first nine months of 2017 compared to the first nine months of 2016 as a result of an increase in click revenue associated with increased click volume and pricing.

Other Revenues. Other revenues decreased to \$0.7 million in the first nine months of 2017 from \$1.2 million in the first nine months of 2016 primarily due to the discontinuation of a Manufacturer's brand utilizing other Company products and lower customer utilization of the mobile product.

[Table of Contents](#)

Cost of Revenues. Cost of revenues increased \$1.2 million, or 2%, in the first nine months of 2017 compared to the first nine months of 2016 primarily due to increased traffic acquisition costs associated with both lead and click volume offset by a decrease in cost of revenues associated with the specialty finance leads product divestiture effective December 31, 2016.

Sales and Marketing. Sales and marketing expense in the first nine months of 2017 decreased \$3.3 million, or 24%, compared to the first nine months of 2016 due primarily to non-recurring severance related expenses in the first nine months of 2016 coupled with lower headcount related costs in the first nine months of 2017.

Technology Support. Technology support expense in the first nine months of 2017 decreased by \$1.2 million, or 11%, compared to the first nine months of 2016 due primarily to non-recurring severance related expenses in the first nine months of 2016 and lower headcount related costs in the first nine months of 2017.

General and Administrative. General and administrative expense in the first nine months of 2017 decreased \$1.3 million, or 12%, from the first nine months of 2016 due to lower headcount related costs in the first nine months of 2017.

Depreciation and Amortization. Depreciation and amortization expense in the first nine months of 2017 decreased \$0.2 million to \$3.6 million compared to \$3.8 million in the first nine months of 2016 primarily due to normal amortization.

Litigation Settlements. Payments received primarily from 2010 settlements of patent infringement claims against third parties relating to the third parties' methods of Lead delivery were \$76,000 for the first nine months of 2017 compared to net payments received of \$25,000 in the first nine months of 2016 due to the payment of \$41,000 in settlement of CAN-SPAM claims assumed in connection with the acquisition of Dealix/Autotegrity in the first nine months of 2016.

Interest and Other Income (Expense), Net. Interest and other income (expense), net was \$0.3 million for the first nine months of 2017 compared to \$0.6 million in the first nine months of 2016. Interest expense decreased to \$602,000 in the first nine months of 2017 from \$661,000 in the first nine months of 2016 primarily due to a decreased balance on our term loans. We also recorded \$0.3 million in other income during the first nine months of 2017 related to the Specialty Finance Leads License Agreement with Internet Brands.

Income Taxes. Income tax expense was \$0.5 million in the first nine months of 2017 compared to income tax expense of \$1.2 million in the first nine months of 2016. Income tax expense for the first nine months of 2017 differed from the federal statutory rate primarily due to state income taxes and the impact of stock-based compensation.

Liquidity and Capital Resources

The table below sets forth a summary of our cash flows for the nine months ended September 30, 2017 and 2016:

	Nine Months Ended September 30,	
	2017	2016
	<i>(in thousands)</i>	
Net cash provided by operating activities	\$ 12,468	\$ 12,081
Net cash used in investing activities	(2,218)	(2,246)
Net cash used in financing activities	(4,066)	(1,099)

Our principal sources of liquidity are our cash and cash equivalents balances. Our cash and cash equivalents totaled \$44.7 million as of September 30, 2017 compared to \$38.5 million as of December 31, 2016.

For information concerning the Company's previously announced share repurchase authorization, see Note 5, Notes to Unaudited Consolidated Condensed Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Credit Facility and Term Loan. For information concerning our term and revolving bank loans, see Note 9, Notes to Unaudited Consolidated Condensed Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Net Cash Provided by Operating Activities. Net cash provided by operating activities in the nine months ended September 30, 2017 of \$12.5 million resulted primarily from net income of \$0.9 million, as adjusted for non-cash charges. We also had net increases in working capital, driven by a decrease in our accounts receivable balance related to the timing of payments received offset by cash used to reduce accrued liabilities of \$3.1 million primarily related to the payment of annual incentive compensation amounts accrued in 2016 and paid in the first nine months of 2017.

Net cash provided by operating activities in the nine months ended September 30, 2016 of \$12.1 million resulted primarily from net income of \$2.5 million, as adjusted for non-cash charges. We also had net decreases in working capital, driven by an increase in our accounts receivable balance related to the timing of payments received offset by an increase in accounts payable of \$3.7 million.

[Table of Contents](#)

Net Cash Used in Investing Activities. Net cash used in investing activities was \$2.2 million in the nine months ended September 30, 2017 which primarily related to purchases of property and equipment and expenditures related to capitalized internal use software.

Net cash used in investing activities was \$2.2 million in the nine months ended September 30, 2016 which primarily related to a \$0.4 million investment in GoMoto and purchases of property and equipment and expenditures related to capitalized internal use software of \$1.9 million.

Net Cash Used In Financing Activities. Net cash used in financing activities of \$4.1 million primarily related to payments of \$3.9 million made against the term loan borrowings and \$1.2 million used to repurchase Company common stock in the first nine months of 2017. In addition, stock options for 191,074 shares of the Company's common stock were exercised in the first nine months of 2017 resulting in \$1.1 million cash inflow.

Net cash used in financing activities of \$1.1 million primarily related to payments of \$3.9 million made against the term loan borrowings in the first nine months of 2016. In addition, stock options for 334,861 shares of the Company's common stock were exercised in the first nine months of 2016 resulting in \$2.9 million cash inflow.

Off-Balance Sheet Arrangements

At September 30, 2017, we had no off-balance sheet arrangements as defined in Regulation S-K, Item 303(a)(4)(D)(ii).

Item 3. *Quantitative and Qualitative Disclosures about Market Risk*

In the ordinary course of business, we are exposed to various market risk factors, including fluctuations in interest rates and changes in general economic conditions. For the three and nine months ended September 30, 2017 there were no material changes in the information required to be provided under Item 305 of Regulation S-K from the information disclosed in Item 7A of the 2016 Form 10-K.

Item 4. *Controls and Procedures*

As of the end of the period covered by this Quarterly Report on Form 10-Q, we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended ("**Exchange Act**"). Based on the evaluation, our Chief Executive Officer and our Chief Financial Officer believe that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective at ensuring that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act are (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required financial disclosure.

As of the end of the period covered by this Quarterly Report on Form 10-Q, there were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that have materially affected, or were reasonably likely to materially affect, our internal control over financial reporting.

Our management, including our Chief Executive Officer and our Chief Financial Officer, does not expect that our disclosure controls and internal control over financial reporting will prevent 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. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. 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. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of a simple error or mistake. Additionally, controls may be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the control.

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, a control 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 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table provides information with respect to Company purchases of AutoWeb, Inc. common stock during the three months ended September 30, 2017:

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs ⁽¹⁾	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
July 1, 2017 – July 31, 2017	—	—	—	\$ 1,220,364
August 1, 2017 – August 31, 2017	—	—	—	1,220,364
September 1, 2017 – September 30, 2017	145,821	\$ 8.20	145,821	24,751
Total	145,821	\$ 8.20	145,821	\$ 24,751

- (1) On June 7, 2012, the Company announced that its board of directors had authorized the Company to repurchase up to \$2.0 million of the Company's common stock, and on September 17, 2014 the Company announced that the board of directors had approved the repurchase of up to an additional \$1.0 million of the Company's common stock. The repurchase of the Company's common stock during the three months ended September 30, 2017 completes the previously authorized stock repurchase programs. Shares repurchased under this program have been retired and returned to the status of authorized and unissued shares. On September 6, 2017, the Company announced that its board of directors authorized the Company to repurchase an additional \$3.0 million of the Company's common stock. The authorization may be increased or otherwise modified, renewed, suspended or terminated by the Company at any time, without prior notice. The Company may repurchase the Company's common stock from time to time on the open market or in private transactions. The Company funded repurchases and anticipates that it will fund future repurchases through the use of available cash.

Item 6. Exhibits

- [2.1](#)† Asset Purchase and Sale Agreement dated as of December 19, 2016 by and among AutoWeb, Inc. (formerly Autobytel Inc.), Car.com, Inc., a Delaware corporation, and Internet Brands, Inc., a Delaware corporation, incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed with the SEC on December 21, 2016 (SEC File No. 001-34761)
- [3.1](#) Sixth Restated Certificate of Incorporation of AutoWeb, Inc. effective October 9, 2017, which is incorporated herein by reference to Exhibit 3.4 to the Current Report on Form 8-K filed with the SEC on October 10, 2017 (SEC File No. 001-34761)
- [3.2](#) Seventh Amended and Restated Bylaws of AutoWeb, Inc. dated October 9, 2017, which is incorporated by reference to Exhibit 3.5 to the Current Report on Form 8-K filed with the SEC on October 10, 2017 (SEC File No. 001-34761)
- 4.1 Tax Benefit Preservation Plan dated as of May 26, 2010 between AutoWeb, Inc. (formerly Autobytel Inc.) and Computershare Trust Company, N.A., as rights agent, together with the following exhibits thereto: Exhibit A – Form of Right Certificate; and Exhibit B – Summary of Rights to Purchase Shares of Preferred Stock of AutoWeb, Inc. (formerly Autobytel Inc.), which is incorporated herein by reference to [Exhibit 4.1](#) to the Current Report on Form 8-K filed with the SEC on June 2, 2010 (SEC File No. 000-22239), as amended by Amendment No. 1 to Tax Benefit Preservation Plan dated as of April 14, 2014, between AutoWeb, Inc. (formerly Autobytel Inc.) and Computershare Trust Company, N.A., as rights agent, which is incorporated herein by reference to Exhibit 4.1 to the Current Report on Form 8-K filed with the SEC on April 16, 2014 (SEC File No. 001-34761), and as amended by Amendment No. 2 to Tax Benefit Preservation Plan dated as of April 13, 2017, between AutoWeb, Inc. (formerly Autobytel Inc.) and Computershare Trust Company, N.A., as rights agent, which is incorporated herein by reference to [Exhibit 4.1](#) to the Current Report on Form 8-K filed with the SEC on April 14, 2017 (SEC File No. 001-34761)
- [4.2](#) Certificate of Adjustment Under Section 11(m) of the Tax Benefit Preservation Plan dated July 12, 2012, which is incorporated by reference to Exhibit 4.3 to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2012 filed with the SEC on November 8, 2012 (SEC File No. 001-34761)
- [10.1](#)■ Form of Restricted Stock Award Agreement pursuant to the AutoWeb, Inc. (formerly Autobytel Inc.) Amended and Restated 2014 Equity Incentive Plan which is incorporated herein by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the SEC on October 3, 2017 (SEC File No. 001-34761)
- [31.1](#)* Rule 13a-14(a)/15d-14(a) Certification by Principal Executive Officer
- [31.2](#)* Rule 13a-14(a)/15d-14(a) Certification by Principal Financial Officer
- [32.1](#)* Section 1350 Certification by Principal Executive Officer and Principal Financial Officer
- 101.INS†† XBRL Instance Document
- 101.SCH†† XBRL Taxonomy Extension Schema Document
- 101.CAL†† XBRL Taxonomy Calculation Linkbase Document
- 101.DEF†† XBRL Taxonomy Extension Definition Document
- 101.LAB†† XBRL Taxonomy Label Linkbase Document
- 101.PRE†† XBRL Taxonomy Presentation Linkbase Document

* Filed herewith.

■ Management Contract or Compensatory Plan or Arrangement.

‡ Certain schedules in this Exhibit have been omitted in accordance with Item 601(b)(2) of Regulation S-K. AutoWeb, Inc. will furnish supplementally a copy of any omitted schedule or exhibit to the Securities and Exchange Commission upon request; provided, however, that AutoWeb, Inc. may request confidential treatment pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended, for any schedule or exhibit so furnished.

†† Furnished with this report. In accordance with Rule 406T of Regulation S-T, the information in these exhibits shall not be deemed to be “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to liability under that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as expressly set forth by specific reference in such filing.

CERTIFICATION

I, Jeffrey H. Coats, certify that:

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

Date: November 2, 2017

/s/ Jeffrey H. Coats
Jeffrey H. Coats
President and Chief Executive Officer

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

In connection with the Quarterly Report of AutoWeb, Inc. (the “*Company*”) on Form 10-Q for the period ended September 30, 2017 (the “*Report*”), we, Jeffrey H. Coats, President and Chief Executive Officer of the Company, and Kimberly S. Boren, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

/s/ Jeffrey H. Coats

Jeffrey H. Coats
President and Chief Executive Officer
November 2, 2017

/s/ Kimberly S. Boren

Kimberly S. Boren
*Executive Vice President and
Chief Financial Officer*
November 2, 2017

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to AutoWeb, Inc. and will be retained by AutoWeb, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.
