

CHEGG, INC  
Form 10-K  
February 23, 2017  
Table of Contents

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2016

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 001-36180

CHEGG, INC.  
(Exact name of registrant as specified in its charter)

Delaware 20-3237489  
(State or other jurisdiction of (I.R.S. employer  
incorporation or organization) identification no.)

3990 Freedom Circle  
Santa Clara, CA, 95054

(Address of principal executive offices)

(408) 855-5700

(Registrant's telephone number, including area code)

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

Title of each class	Name of each exchange on which registered
Common Stock, \$0.001 par value per share	The New York Stock Exchange

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

None

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
 Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the  
Act. Yes  No

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 (Exchange Act) 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  
Website, 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

Edgar Filing: CHEGG, INC - Form 10-K

registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2016, the last business day of the registrant's most recently completed second fiscal quarter, based upon the closing price of such stock on such date as reported by the New York Stock Exchange on such date, was approximately \$402,351,715. Shares of Common Stock held by each executive officer and director have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of January 31, 2017, the Registrant had 91,830,713 outstanding shares of Common Stock.

#### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement for the Registrant's 2016 Annual Meeting of Stockholders are incorporated by reference in Part III of this Annual Report on Form 10-K to the extent stated herein. The Proxy Statement will be filed within 120 days of the Registrant's fiscal year ended December 31, 2016.

Table of Contents

## TABLE OF CONTENTS

	Page
<u>PART I</u>	
<u>Item 1. Business</u>	<u>4</u>
<u>Item 1A. Risk Factors</u>	<u>11</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>35</u>
<u>Item 2. Properties</u>	<u>35</u>
<u>Item 3. Legal Proceedings</u>	<u>35</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>36</u>
<u>PART II</u>	
<u>Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities</u>	<u>37</u>
<u>Item 6. Selected Financial Data</u>	<u>38</u>
<u>Item 7. Management's Discussion and Analysis of Financial Condition and Result of Operations</u>	<u>40</u>
<u>Item 8. Consolidated Financial Statements and Supplementary Data</u>	<u>58</u>
<u>Item 9. Change in and Disagreements with Accountants On Accounting and Financial Disclosure</u>	<u>93</u>
<u>Item 9A. Controls and Procedures</u>	<u>93</u>
<u>Item 9B. Other Information</u>	<u>93</u>
<u>PART III</u>	
<u>Item 10. Directors, Executive Officers and Corporate Governance</u>	<u>94</u>
<u>Item 11. Executive Compensation</u>	<u>94</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>94</u>
<u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u>	<u>94</u>
<u>Item 14. Principal Accountant Fees and Services</u>	<u>94</u>
<u>PART IV</u>	
<u>Item 15. Exhibits and Financial Statement Schedules</u>	<u>95</u>
<u>Item 16. Form 10-K Summary</u>	<u>95</u>
<u>Signatures</u>	<u>96</u>
<u>Index to Exhibits</u>	<u>98</u>

Unless the context requires otherwise, the words “we,” “us,” “our,” “Company” and “Chegg” refer to Chegg, Inc. and its subsidiaries taken as a whole.

“Chegg,” “Chegg.com,” “Chegg Study,” “Chegg for Good,” “Student Hub,” “internships.com,” “ResearchReady,” “InstaEDU,” “EasyBib” and “#1 In Textbook Rentals,” are some of our trademarks used in this Annual Report on Form 10-K. Solely for convenience, our trademarks, trade names and service marks referred to in this Annual Report on Form 10-K appear without the ®, ™ and SM symbols, but those references are not intended to indicate, in any way, that we will not assert, to the fullest extent under applicable law, our rights to these trademarks and trade names. Other trademarks appearing in this Annual Report on Form 10-K are the property of their respective holders.

Table of Contents

NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained in this Annual Report on Form 10-K other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. The words “believe,” “may,” “will,” “estimate,” “continue,” “anticipate,” “intend,” “project,” “endeavor,” “expect,” “plans to,” “if,” “future,” and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described in Part I, Item 1A, “Risk Factors” in this Annual Report on Form 10-K. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this Annual Report on Form 10-K may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.

We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

## Table of Contents

### PART I

#### ITEM 1. BUSINESS

##### Overview

Chegg is the leading student-first connected learning platform. We help students study more effectively for college admissions exams, find the right college to accomplish their goals, get better grades and test scores while in school, and find internships that allow them to gain valuable skills to help them enter the workforce after college. We strive to improve the overall return on investment in education by helping students learn more in less time and at a lower cost. During 2016, nearly 6.5 million students turned to Chegg to help them save money and improve their outcomes.

In 2016, over 1.5 million students subscribed to our Chegg Services, an increase of 47% year over year from 1.0 million in 2015. Chegg Services include Chegg Study, Chegg Tutors, Writing Tools (newly acquired in May 2016), Enrollment Marketing, Brand Partnership, Internships, and Test Prep. Our Chegg Study service provides step-by-step Textbook Solutions and Expert Answers, helping students with their course work. When students need additional help on a subject, they can reach a live tutor online, anytime, anywhere through Chegg Tutors. When students need help creating citations for their papers, they can use one of our Writing Tools properties, including EasyBib, Citation Machine, BibMe, CiteThisForMe and NormasAPA. In 2016, we matched approximately 5.3 million domestic and international students with colleges, universities and other academic institutions, which we collectively refer to as "colleges," in the United States, to help them find the best fit school for them. As of December 31, 2016, we provided access to approximately 340,000 internships to help students gain skills and experiences that are critical to securing their first job. Our Test Prep service is designed to help students increase their standardized SAT and ACT exam scores to improve their chances of getting accepted to a school of their choice. Through our strategic partnership with Ingram Content Group (Ingram), we offer Required Materials, which includes an extensive print textbook and eTextbook library for rent and sale, helping students save money compared to the cost of buying new. In 2016, students rented or bought over 5.7 million textbooks and eTextbooks from Chegg.

To deliver these services, we partner with several third parties. In 2016, we entered into agreements with a wide range of colleges to help shape their incoming classes. We sourced print textbooks, eTextbooks and supplemental materials directly or indirectly from thousands of publishers in the United States, including Pearson, Cengage Learning, McGraw Hill, Wiley and MacMillan. We have a large network of students and professionals who leverage our platform to earn money by tutoring in their spare time. Thousands of employers leverage our platform to post their internships and jobs. In addition, because we have a large student audience, local and national brands partner with us to reach the college and high school demographic.

##### Our Offering

We offer products and services that help students improve their outcomes throughout their educational journey. Our offerings fall into two categories: Chegg Services, which encompasses all of our digital products and services, and Required Materials, which primarily includes our print textbook and eTextbook business.

##### Chegg Services

**Chegg Study.** Our Chegg Study service helps students master challenging concepts on their own. For high demand print and electronic textbooks, primarily in the subjects of sciences, technology, engineering, mathematics, statistics, business and economics, we offer "Textbook Solutions," which are step-by-step answers to the questions at the end of each chapter in textbooks. For other questions, we offer our Expert Answers service, where a student can ask a

question on our website and subject matter experts will provide detailed answers. As of December 31, 2016, Chegg had an archive of over 8 million responses, which students can immediately access. These services are available on our website and on mobile devices through our native application and our mobile website.

Chegg Tutors. Complementing our other study tools, we have live tutors on our connected learning platform. Students can access help online, anytime, anywhere either synchronously or asynchronously. Instead of paying for expensive, offline tutors that require scheduling and travel time, students can come to Chegg to find tutors whenever they need additional help on a subject and pay as little as \$0.40 per minute. Our tutors are qualified to help students with a wide range of topics, including history, foreign languages, English literature, science, technology, engineering, mathematics and business, along with test prep and a variety of other highly-requested subjects. Students can subscribe to weekly or monthly packages, or choose to use the service on a pay-as-you-go basis.

## Table of Contents

**Writing Tools.** In May of 2016 we acquired Imagine Easy Solutions (Imagine Easy), the provider of the popular EasyBib, Citation Machine, BibMe, CiteThisForMe, NormasAPA and other tools with capabilities such as citation, bibliography and anti-plagiarism. When students need to cite their sources in written work, they can use our Imagine Easy writing tools to automatically generate sources in the required formats. These tools offer a variety of advertising-supported and paid subscription products. In 2016, students logged approximately 265 million individual online sessions, lasting on average more than 8 minutes per session. Since their launch, students worldwide have created more than 1.5 billion citations using Imagine Easy's writing productivity tools.

**Enrollment Marketing Services.** In January 2017, we announced a strategic partnership with the National Research Center for College & University Admissions (NRCCUA) where NRCCUA will assume responsibility for managing, renewing, and maintaining our existing university contracts and become the exclusive reseller of the digital enrollment marketing services that we provide to colleges and universities. Through this strategic partnership, we provide colleges with admission and transfer support through our enrollment marketing services. We delivered 5.3 million paid inquiries for interested students during 2016. Using the information from the college-bound high school students who fill out a profile using our College Admissions and Scholarship Services and from our affiliate network, and only after the student has agreed to be referred, we provide colleges with potential candidates and help them cost effectively attract and shape their classes. Our College Admissions and Scholarship Services further allow high school students to connect with their “best fit” educational and scholarship opportunities. Students in high school or college can use our “Scholarship Match” tool to create a profile that includes information such as their high school, GPA, intended major, demographic background, college preferences and areas of interest. Based on this information, our services can connect these students with scholarship opportunities.

**Brand Partnership.** We offer unique and compelling ways for brands with relevant products and services to reach and engage high school and college students at important and memorable transition points in their lives, such as preparing for college, preparing for back-to-school or as they approach graduation and prepare for a career or graduate school. We work closely with brands to integrate their services and products with ours. Our brand advertising services include digital advertising on our platform, product samples, white label integrations, discounts, and other promotions shipped directly to students in our distinctive orange Chegg boxes and experiential offerings that may include, for example, on-campus events, sponsorships and other brand ambassador work. During the year ended December 31, 2016, we had advertising contracts with over 55 consumer brands.

**Internships.** Internships are a highly effective way for students to gain work experience before graduation. In a recent survey, 65% of companies that responded offered full-time jobs to interns. As of December 31, 2016, we provide students access to approximately 340,000 internships with more than 122,000 employers across the country. Students search and apply for internships directly through our website, internships.com. Students can upload their resume to be matched by us to internship opportunities. Employers can post their internships and manage the process with our applicant tracking system. We currently offer internships as a free service.

**Test Prep.** In November 2015, we launched a beta version of our interactive Test Prep product, covering the SAT and ACT exams. Our goal is to provide all students access to an affordable, high-quality and comprehensive online test preparation product that helps students improve their test scores. After our initial launch of a free version which allowed us to learn from user behavior, we are currently testing various paid models with students.

## Required Materials

**Print Textbooks and eTextbooks.** For students looking to save on the cost of required materials, we rent and sell print textbooks and eTextbooks. Most of the print textbook transactions are rentals, although we also offer both new and used books for sale at a slight markup to our acquisition cost. In 2014, we implemented a partnership with Ingram, which we expanded in May 2015 so that Ingram fulfills all of our print textbook rentals and a portion of our textbook

sales. We offer a compelling value proposition to students as the price to rent a book through Chegg is significantly lower than the purchase price of a new or used book. Orders are shipped to students in a distinctive orange Chegg box and typically arrives within three business days. At the end of the academic term, students can return a rented textbook in this same box for free. In participation with certain publishers, we also offer “Instant Access” to eTextbooks that is a one-week free trial of our eTextbook service, and allows the student to access the eTextbook while the print copy is in transit. Our data shows students value this service and find it a great way to learn more about our eTextbook experience. All eTextbooks obtained from Chegg are accessed through our proprietary HTML5-web-based eTextbook Reader. Our eTextbook Reader provides students with access to eTextbooks on PCs, tablets and smart phones, providing access anytime, anywhere that students are connected to the Internet and students can save a portion of the book for offline access. Our eTextbook Reader enables fast and easy navigation, keyword search, text highlighting, note taking and further preserves those notes in an online notepad with persistence of highlighting and notes across platforms. In 2016, we rented or sold over 5.7 million print textbooks and eTextbooks.



## Table of Contents

**Supplemental Materials.** In addition to textbooks, we offer students access to other materials from publishers, professors, students and subject matter experts. These include related materials like study guides, lab manuals or digital services provided by publishers, commonly known as “Whole Course Solutions” or “Integrated Learning Systems.” We tailor our merchandising of these materials based on the student’s core textbook.

**Textbook Buyback.** We offer students, on behalf of our fulfillment partner Ingram, the ability to sell us their textbooks, even if they were not originally purchased from us, and in turn those textbooks are offered to other students for purchase or rent, or sold to wholesalers. Students provide us with the ISBN of each textbook they want to sell, and we let them know how much we are willing to pay based on our real-time market driven algorithms. Ingram reimburses us the amounts we pay to students for these purchases. If our offer is accepted, we provide a pre-printed label and shipping instructions.

## Technology and Platform Integration

Our technology is designed to create a connected learning platform that is built to enable our future growth at scale. We employ technological innovations whenever possible to increase efficiency and scale in our business. Our products rely upon and leverage the information underlying our Student Graph discussed in more detail below. We will continue to invest in building technologies around our data, search and solutions. The key elements of our technology platform are:

**Personalization and Merchandising Technology.** We create a personalized experience for each student throughout our connected learning platform, building awareness of our multiple services and also connecting them with opportunities through third-party partners and brands. We are able to accomplish this personalization and customization as a result of our Student Graph and our search technology.

**Student Graph.** Our Student Graph is the accumulation of the collective activity of students in our connected learning platform. Students provide us information each time they engage with our connected learning platform. Our Student Graph also includes information we access from public and private sources to integrate into our connected learning platform such as textbook information, information about colleges and scholarship data. We are able to collect, organize and process this information to algorithmically create a personalized experience for each student on our network.

**Search.** Search is an easy on-ramp for students to discover all of our services. Students can search by book, ISBN, author’s name or course. Many students come to us for textbook rentals, and in our search results we not only provide the relevant textbook, but also begin to build awareness of our other services. For instance, when a student searches for a textbook, we can also expose that student to Chegg Tutors, Expert Answers, and Textbook Solutions that are relevant to that textbook. We may also display a free Chegg Study offer where we have Textbook Solutions for that textbook. We also provide personalized search results based on information in our Student Graph.

**Data Sourcing and Graph Technology.** Not all information relevant to students on our platform is made available by service, product, list or user-input. Therefore, we have developed proprietary technologies to collect disparate, distributed sets of data. For example, we access data from public and private sources to integrate into our platform to inform our decisions about our textbook catalog and pricing.

**Mobile Solutions.** We have mobile applications on Apple iOS and Google Android. Our mobile apps are built as hybrid applications leveraging the Chegg application programming interface (API) and server-side HTML5. We also maintain a mobile version of our website: [m.chegg.com](http://m.chegg.com). Taking advantage of capabilities unique to the mobile platform, we offer some functionality on mobile that is not available on our website, such as textbook barcode

scanning for price comparisons, Chegg Flashcards, and Chegg Textbook Solutions.

Open Platform. We have established a proprietary API layer that enables us to extend our product and service offerings to additional, relevant business partners. We have enhanced our technology to enable Chegg student experiences to be consumed on other websites or portals. Internships.com, which we acquired in 2014, began offering its services through this API layer in December 2013. We have established four other use cases and have applied unique technology to each case, with the aim of providing students with access to relevant products and services beyond those that we have developed or provided on our website, including native mobile applications, hub applications, bridge to third-party tools, an externalizing catalog and Platform-as-a-Service.

## Table of Contents

**Content Conversion Platform.** We have developed a proprietary set of technologies that ingests each publisher's unique source files and creates HTML5-based documents. Our web-based eTextbook Reader, which is embedded with digital rights management, allows us to provide our content across technology platforms, have a deep understanding of how content is consumed and deliver content securely.

**Real-time Sourcing and Pricing Technologies.** We have internally developed proprietary pricing and sourcing systems which consider market price, content selection and availability, and other factors, in determining price and origin of content and services we offer to students.

**Programmatic Advertising.** In our acquisition of Imagine Easy, we also acquired their programmatic advertising team and technology team, StudyBreak Media™. StudyBreak Media has expanded their work as part of our learning platform, building custom ad tech solutions that maximize the value of our digital inventory. Through StudyBreak Media, we combine a deep understanding of programmatic technology trends with data science, engineering and machine learning. The result is a mediation platform that blends with our direct sales force to maximize the value of the impressions we serve.

**Infrastructure.** Our technology resides at a major cloud-hosting provider divided between the U.S. West Coast and U.S. East Coast. We use one region for our test/development/stage/failover environment and the other for our production environment. The architecture is also designed to provide for international expansion if we expand into new international markets.

**Network Security.** Our platform includes encryption, antivirus, firewall and patch-management technologies to help protect our systems distributed across cloud-hosting providers and our business offices.

**Internal Management Systems.** We rely on third-party technology solutions and products as well as internally developed and proprietary systems, in which we have made substantial investment, to provide rapid, high-quality customer service, internal communication, software development, deployment, and maintenance.

## Customers

In 2016, approximately 3.5 million individuals paid for our products and services directed at college and high school students up from approximately 3.1 million and 3.0 million in 2015 and 2014, respectively. In 2016, we entered into agreements to provide enrollment marketing services to over 400 colleges, including public and private colleges. We have conducted national campaigns with a number of brands attractive to college and high school students. During 2016, we had advertising contracts with over 55 consumer brands.

## Sales and Marketing

### Students

We use several major direct marketing channels relevant to students. We deploy search engine optimization (SEO) techniques designed to increase the visibility of Chegg.com content in organic, unpaid search engine result listings. We supplement our SEO efforts through search engine marketing using keyword simulation and bid management tools to analyze and categorize search keywords, optimize bidding, increase impressions and drive conversion. We also use display marketing to drive awareness of our brand and services by running display advertising on major online and mobile advertising networks, such as Google Display Network. We integrate our textbook services on affiliates' websites and work with a large advertising network that recruits individual online affiliates in exchange for pre-determined revenue share or commissions. We utilize three types of email marketing campaigns: onboarding

programs to drive activation and retention, personalized cross-sell campaigns to deepen engagement, and promotional campaigns to drive sales and interests. We use social media to manage organic and paid programs across top websites, including Facebook, Twitter and YouTube. We also acquire and engage students through content generated by student bloggers, syndicated through partners, around key student concerns and interests such as admissions, transition to college, picking a major, and resume preparation.

Through our campus activation programs, we partner with brands to bring entertainment events, such as concerts, trial promotions, on campus ambassadors and product giveaways to students. We also engage students on campus to help them elevate their voice behind timely social issues beyond academics, such as the “It’s On Us” campaign relating to the prevention of on-campus sexual violence. The Chegg for Good program connects students and employees with partners to engage them in causes related to education and the environment. We work with the nonprofit conservation organization American Forest to

7

---

## Table of Contents

plant trees around the world and our funding has enabled the planting of more than six million trees to date. The Chegg Foundation, a California nonprofit public benefit corporation, engages in charitable and education-related activities. As part of our College Admissions and Scholarship Services marketing efforts, we identify select partner organizations who offer complementary content and services that support students in exploring colleges. We enable these partner organizations to use our college match service through their websites to enable students to request information about colleges that may be of interest to them.

### Colleges and Brands

We secure contracts with brands through direct sales by our field sales organization, which sells brand advertising services to large brand advertisers and advertising agencies seeking to reach and engage college and high school students. This team has field sales people and inside client success managers as well as operations and marketing support. In January 2017, we signed a strategic alliance agreement with NRCCUA, who is our exclusive reseller to colleges for our digital marketing services.

### Student Advocacy

We are committed to providing a high level of customer service to our students. We trust our students, understand the critical role our products and services have in their education, and strive to resolve all problems quickly and thoroughly. Our student advocacy team can be reached directly through phone, email, and online chat during business hours. We also proactively monitor social media to identify and solve problems before we are otherwise informed of their existence. We endeavor to respond to students' concerns within five minutes.

### Competition

While we do not have any competitors that compete with us across our business in its entirety, we face significant competition in each aspect of our business, and we expect such competition to increase. The actual and potential competition in each of our primary areas of operations is described below.

**Products and Services for Students.** Our Chegg Services face competition from different businesses depending on the offering. For Chegg Study, our competitors primarily include publishers that provide study materials and online instructional systems. Additionally, we face competition from free services such as Yahoo! Answers and Brain.ly for our Expert Answers service. For our Chegg Tutors services, we face competition from other online tutoring services such as Tutors.com and Varsity Tutors. For our writing tools, we primarily face competition from other citation generating services such as Noodle Tools. The market for textbooks and supplemental materials is intensely competitive and subject to rapid change. We face competition from college bookstores, some of which are operated by Follett and Barnes & Noble Education, online marketplaces such as Amazon.com and providers of eTextbooks such as Apple iTunes, and Blackboard, as well as various private textbook rental websites. Many students purchase from multiple textbook providers, are highly price sensitive and can easily shift spending from one provider or format to another. As a consequence, our Required Materials product line, which includes eTextbooks, competes primarily on price and further on selection and functionality and compatibility of our eTextbook Reader across a wide variety of desktop and mobile devices.

**Enrollment Marketing Services.** With respect to our enrollment marketing services, we compete against traditional methods of student recruitment, including student data providers such as standardized test providers, radio, television and Internet advertising and print mail marketing programs. In this area, we compete primarily on the basis of the number of high-quality connections between prospective students and colleges we are able to provide as well as on price. We are able to create these connections by providing prospective students with an easy-to-use platform to input

their academic information and aspirations, learn about colleges, locate scholarships and financial aid and facilitate and streamline the application process.

**Brands.** With respect to brands, we compete with online and offline outlets that generate revenues from advertisers and marketers, especially those that target high school and college students. In this area, we seek to partner with brands that have offerings that will interest or delight students and have received very positive comments and feedback from students on these offerings. We provide these brands with preferential access to our audience, which we believe represents a highly engaged portion of the target demographic of our brand partners.

## Table of Contents

We believe that we have competitive strengths, some of which are discussed above, that position us favorably in each aspect of our business. However, the education industry is evolving rapidly and is increasingly competitive. A variety of business models are being pursued or may be considered for the provision of print textbooks and eTextbooks, some of which may be more profitable or successful than our business model.

### Intellectual Property

We use proprietary technology to operate our business and our success depends, in part, on our ability to protect our technology and intellectual property. We rely on a combination of patent, copyright, trademark and trade secret laws, as well as contractual restrictions, to establish and protect our intellectual property. We maintain a policy requiring our employees, contractors, consultants and other third parties to enter into confidentiality and proprietary rights agreements to control access to our proprietary information. These laws, procedures and restrictions provide only limited protection and any of our intellectual property rights may be challenged, invalidated, circumvented, infringed or misappropriated. Further, the laws of certain countries do not protect proprietary rights to the same extent as the laws of the United States and, therefore, in certain jurisdictions, we may be unable to protect our proprietary technology.

As of December 31, 2016, we had thirteen patents which will expire between 2032 and 2034 and 28 patent applications pending in the United States. We own three U.S. copyrights registrations and have unregistered copyrights in our eTextbook Reader software, software documentation, marketing materials and website content that we develop. We own the registered U.S. trademarks “Chegg,” “Chegg.com,” “Chegg Study,” “Chegg for Good,” “Student Hub,” “internships.com,” “ResearchReady,” “InstaEDU,” “EasyBib” and “#1 In Textbook Rentals,” among others as well as a variety of service marks. As of December 31, 2016, we owned over 600 registered domain names. We also have a number of pending trademark applications in the United States and foreign jurisdictions and unregistered marks that we use to promote our brand. From time to time we expect to file additional patent, copyright and trademark applications in the United States and abroad.

### Government Regulation

We are subject to a number of laws and regulations that affect companies conducting business on the Internet and in the education industry, many of which are still evolving and could be interpreted in ways that could harm our business. The manner in which existing laws and regulations will be applied to the Internet and students in general and how they will relate to our business in particular, are often unclear. For example, we often cannot be certain how existing laws will apply in the e-commerce and online context, including with respect to such topics as privacy, defamation, pricing, credit card fraud, advertising, taxation, sweepstakes, promotions, content regulation, financial aid, scholarships, student matriculation and recruitment, quality of products and services and intellectual property ownership and infringement.

Numerous laws and regulatory schemes have been adopted at the national and state level in the United States, and in some cases internationally, that have a direct impact on our business and operations. For example:

The CAN-SPAM Act of 2003 and similar laws adopted by a number of states, regulate unsolicited commercial emails, create criminal penalties for emails containing fraudulent headers and control other abusive online marketing practices. Similarly, the U.S. Federal Trade Commission (FTC) has guidelines that impose responsibilities on us with respect to communications with consumers and impose fines and liability for failure to comply with rules with respect to advertising or marketing practices they may deem misleading or deceptive.

The Telephone Consumer Protection Act of 1991 (TCPA) restricts telemarketing and the use of automated telephone equipment. The TCPA limits the use of automatic dialing systems, artificial or prerecorded voice messages, SMS text messages and fax machines. It also applies to unsolicited text messages advertising the commercial availability of goods or services. Additionally, a number of states have enacted statutes that address telemarketing. For example, some states, such as California, Illinois and New York, have created do-not-call lists. Other states, such as Oregon and Washington, have enacted “no rebuttal statutes” that require the telemarketer to end the call when the consumer indicates that he or she is not interested in the product being sold. Restrictions on telephone marketing, including calls and text messages, are enforced by the FTC, the Federal Communications Commission, states and through the availability of statutory damages and class action lawsuits for violations of the TCPA.

The Credit Card Accountability Responsibility and Disclosure Act of 2009, or CARD Act, and similar laws and regulations adopted by a number of states regulate credit card and gift certificate use fairness, including expiration dates and fees. Our business also requires that we comply with payment card industry data security



## Table of Contents

and other standards. In particular, we are subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, or if our data security systems are breached or compromised, we may be liable for card issuing banks' costs, subject to fines and higher transaction fees and lose our ability to accept credit and debit card payments from our customers, process electronic funds transfers or facilitate other types of online payments, and our business and operating results could be adversely affected.

Regulations related to the Program Participation Agreement of the U.S. Department of Education and other similar laws and regulate the recruitment of students to colleges and other institutions of higher learning.

The Children's Online Privacy Protection Act imposes additional restrictions on the ability of online services to collect information from minors. In addition, certain states, including Utah and Massachusetts, have laws that impose criminal penalties on the production and distribution of content that is "harmful to a minor."

The Digital Millennium Copyright Act (DMCA) provides relief for claims of circumvention of copyright protected technologies and includes a safe harbor intended to reduce the liability of online service providers for hosting, listing or linking to third-party content that infringes copyrights of others.

The Communications Decency Act provides that online service providers will not be considered the publisher or speaker of content provided by others, such as individuals who post content on an online service provider's website.

## Employees

As of December 31, 2016, we had 766 full-time employees. We also engage temporary, seasonal employees and consultants. None of our employees are represented by labor unions or covered by a collective bargaining agreement. We have not experienced any work stoppages and we consider our relations with our employees to be good.

## Seasonality

Information about seasonality is set forth in the section "Seasonality of Our Business" in Part II, Item 7 of this Annual Report on Form 10-K.

## Information about Segment and Geographic Revenues

Information about segment and geographic revenues is set forth in Note 19 of the Notes to Consolidated Financial Statements included in Part II, Item 8, "Consolidated Financial Statements and Supplementary Data" of this Annual Report on Form 10-K.

## Corporate History

We were incorporated in Delaware in July 2005. We launched our online print textbook rental business in 2007. We hired our current Chief Executive Officer in 2010, who implemented our current business strategy to create the leading student-first connected learning platform for students to help them improve their outcomes. Beginning in 2010, we made a series of strategic acquisitions to expand our Chegg Services, including Cramster in 2010 to add our Chegg Study service, Zinch in 2011 to add our College Admissions and Scholarship Services, InstaEDU in 2014 to add our Tutoring service, internships.com in 2014 to add to our internship service, and Imagine Easy Solutions in 2016 to add a portfolio of online writing tools. We completed our initial public offering (IPO) in November 2013 and our common stock is listed on the New York Stock Exchange under the symbol "CHGG." Our principal executive

offices are located at 3990 Freedom Circle, Santa Clara, California 95054 and our telephone number is (408) 855-5700.

#### Available Information

Our website address is [www.chegg.com](http://www.chegg.com) and our Investor Relations website address is [investor.chegg.com](http://investor.chegg.com). Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to reports filed pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended (Exchange Act), are filed with the U.S. Securities and Exchange Commission (SEC). We are subject to the informational requirements of the Exchange Act and file or furnish reports, proxy statements, and other information with the SEC. Such reports and other information filed by the

## Table of Contents

Company with the SEC are available free of charge on our website at investor.chegg.com when such reports are available on the SEC's website. We use our www.chegg.com/mediacenter website as a means of disclosing material non-public information and for complying with our disclosure obligations under Regulation FD. Accordingly, investors should monitor www.chegg.com/mediacenter, in addition to following our press releases, SEC filings and public conference calls and webcasts.

The public may read and copy any materials filed by Chegg with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Room 1580, Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC at www.sec.gov.

The contents of the websites referred to above are not incorporated into this filing. Further, our references to the URLs for these websites are intended to be inactive textual references only.

### ITEM 1A. RISK FACTORS

The risks and uncertainties set forth below, as well as other risks and uncertainties described elsewhere in this Annual Report on Form 10-K including in our consolidated financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" or in other filings by Chegg with the SEC, could adversely affect our business, financial condition, results of operations and the trading price of our common stock. Additional risks and uncertainties that are not currently known to us or that are not currently believed by us to be material may also harm our business operations and financial results. Because of the following risks and uncertainties, as well as other factors affecting our financial condition and operating results, past financial performance should not be considered to be a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

#### Risks Related to Our Business and Industry

Our limited operating history, recent business model transition and evolving digital offerings make it difficult to evaluate our current business and future prospects.

Although we began our operations in July 2005, we did not launch our online print textbook rental business until 2007 or begin generating revenues at scale from print textbook rentals until 2010. We began transitioning to a new model for our Required Materials product line in August 2014 through our strategic partnership with Ingram to accelerate our transition away from the more capital intensive aspects of the print textbook rental business. We have completed our transition to a fully digital company as of November 2016 as Ingram now fulfills all print textbook rental orders. We continue to market, use our branding and maintain the customer experience around print textbook rentals, while Ingram funds all rental textbook inventory, fulfillment, logistics, and has title and risk of loss related to textbook rentals for the textbooks they own.

Since July 2010, we also have been focused on expanding our other offerings, in many instances through the acquisition of other companies, to include supplemental materials, multiplatform eTextbook Reader software, Chegg Study, Chegg Tutors, Chegg Test Prep, Chegg Writing Tools, College Admissions and Scholarship Services, purchases of used textbooks, internships, careers, college counseling, enrollment marketing services and brand advertising. Our newer products and services, or any other products and services we may introduce or acquire, may not be integrated effectively into our business, achieve or sustain profitability or achieve market acceptance at levels sufficient to justify our investment.

Our ability to fully integrate new products and services into our connected learning platform or achieve satisfactory financial results from them is unproven. Because we have a limited operating history, in particular operating a fully digital platform, and the market for our products and services, including newly acquired or developed products and services, is rapidly evolving, it is difficult for us to predict our operating results, particularly with respect to our newer

offerings, and the ultimate size of the market for our products and services. If the market for a connected learning platform does not develop as we expect, or if we fail to address the needs of this market, our business will be harmed. We face the risks, expenses and difficulties typically encountered by companies in their early stage of development, including, but not limited to our ability to successfully:

- execute on our relatively new and evolving business model;
- develop new products and services, both independently and with developers or other third parties;
- attract and retain students and increase their engagement with our connected learning platform and our mobile applications;
- attract and retain colleges, universities and other academic institutions and brands to our marketing services;
- manage the growth of our business, including increasing or unforeseen expenses;

Table of Contents

- develop and scale a high performance technology infrastructure to efficiently handle increased usage by students, especially during peak periods prior to each academic term;
- maintain and manage relationships with strategic partners, including Ingram, NRCCUA, and other distributors, publishers, wholesalers, colleges and brands;
- develop a profitable business model and pricing strategy;
- compete with companies that offer similar services or products;
- expand into adjacent markets;
- navigate the ongoing evolution and uncertain application of regulatory requirements, such as privacy laws, to our business, including our new products and services;
- integrate and realize synergies from businesses that we acquire; and
- expand into foreign markets.

We have encountered and will continue to encounter these risks and if we do not manage them successfully, our business, financial condition, results of operations and prospects may be materially and adversely affected.

Our operating results are expected to be difficult to predict based on a number of factors.

We expect our operating results to fluctuate in the future based on a variety of factors, many of which are outside our control and are difficult to predict. As a result, period-to-period comparisons of our operating results may not be a good indicator of our future or long-term performance. The following factors may affect us from period-to-period and may affect our long-term performance:

- our ability to attract and retain students and increase their engagement with our connected learning platform and mobile applications, particularly related to our Chegg Services subscribers;
- the rate of adoption of our offerings;
- our ability to successfully utilize the information gathered from our connected learning platform to enhance our Student Graph and target sales of complementary products and services to our students;
- changes in demand and pricing for print textbooks and eTextbooks; Ingram's ability to manage fulfillment processes to handle significant volumes during peak periods and as a result of the potential growth in volume of transactions over time; changes by our competitors to their product and service offerings;
- price competition and our ability to react appropriately to such competition;
- our ability and Ingram's ability to manage their textbook library;
- our ability to execute on our strategic partnership with Ingram;
- disruptions to our internal computer systems and our fulfillment information technology infrastructure, particularly during peak periods; the amount and timing of operating costs and capital expenditures relating to expansion of our business, operations and infrastructure;
- our ability to successfully manage the integration of operations, technology and personnel resulting from our acquisitions;
- governmental regulation in particular regarding privacy and advertising and taxation policies; and
- general macroeconomic conditions and economic conditions specific to higher education.

Table of Contents

We have a history of losses and we may not achieve or sustain profitability in the future.

We have experienced significant net losses since our incorporation in July 2005, and we may continue to experience net losses in the future. Our net losses for the years ended December 31, 2016, 2015, and 2014 were \$42.2 million, \$59.2 million, and \$64.8 million, respectively. As of December 31, 2016, we had an accumulated deficit of \$371.3 million. We expect to make significant investments in the development and expansion of our business and our cost of revenues and operating expenses may increase. We may not succeed in increasing our revenues sufficiently to offset these higher expenses, and our efforts to grow the business may prove more expensive than we currently anticipate. We may incur significant losses in the future for a number of reasons, including slowing demand for print textbook rentals or our other products and services; increasing competition, particularly for the price of textbooks; decreased spending on education; and other risks described in this Annual Report on Form 10-K. We may encounter unforeseen expenses, challenges, complications and delays and other unknown factors as we pursue our business plan and our business model continues to evolve. While Chegg Services revenues have grown in recent periods, this growth may not be sustainable and we may not be able to achieve profitability. To achieve profitability, we may need to change our operating infrastructure and scale our operations more efficiently. We also may need to reduce our costs or implement changes in our product offerings to improve the predictability of our revenues. For example, we have recently transitioned substantially all of our print textbook rental revenues to commissions-based revenues in January 2017. If we fail to implement these changes on a timely basis or are unable to implement them due to factors beyond our control, our business may suffer. If we do achieve profitability, we may not be able to sustain or increase such profitability.

We operate in a rapidly changing market and we have recently transitioned our business model to a fully digital business. If we do not successfully adapt to known or unforeseen market developments, our business may be harmed.

The market for our connected learning platform is still unproven and rapidly changing. Historically, we generated the majority of our revenues from print textbooks. Print textbook rental is highly capital intensive and presents both business planning and logistical challenges that are complex. To reduce our investment in the highly capital intensive nature of print textbook rentals, we entered into a partnership with Ingram wherein Ingram makes all new investments in the rental library of print textbooks, taking title and risk of loss for the books, and provides logistical and fulfillment services for the print textbooks that we rent and sell. The partnership allows us to market, use our branding and maintain the customer experience around print textbook rentals, while reducing our investments in textbook inventory, fulfillment and logistics operations. As a result of this change, we stopped making additional investments in our textbook library beginning in May 2015 and we liquidated substantially all of our remaining inventory of print textbooks during 2016. The transition of these aspects of our print textbook offerings to Ingram is now complete. Our partnership with Ingram is non-exclusive and subject to significant risks, including Ingram's ability to acquire textbooks and manage logistical and fulfillment activities for us, our ability to create a successful and profitable partnership, and that we and/or Ingram may elect to terminate the partnership sooner than anticipated.

We have added and plan to continue to add new offerings to our connected learning platform, including, for example writing tools, to diversify our sources of revenues, which will require us to make substantial investments in the products and services we develop or acquire. New offerings may not achieve market success at levels that recover our investment or contribute to profitability. Because these offerings are not as capital intensive as our print textbook rental service, the barriers to entry for existing and future competitors may be lower and allow for even more rapid changes to the market. Furthermore, the market for these other products and services is relatively new and may not develop as we expect. If the market for our offerings does not develop as we expect, or if we fail to address the needs of this market, our business will be harmed. We may not be successful in executing on our evolving business model, and if we cannot provide an increasing number of products and services that students, colleges and brands find compelling, we will not be able to continue our recent growth and increase our revenues, margins and profitability.

For all of these reasons, the evolution of our business model is ongoing and the future revenues and income potential of our business is uncertain.

If our efforts to attract new students to use our products and services and increase student engagement with our connected learning platform are not successful, our business will be adversely affected.

The growth of our business depends on our ability to attract new students to use our products and services and to increase the level of engagement by existing students with our connected learning platform. The substantial majority of our revenues depends on small transactions made by a widely dispersed student population with an inherently high rate of turnover primarily as a result of graduation. Many of the students we desire to attract are accustomed to obtaining textbooks through bookstores or used booksellers. The rate at which we expand our student user base and increase student engagement with our connected learning platform may decline or fluctuate because of several factors, including:

## Table of Contents

- our ability and Ingram's ability to consistently provide students with a convenient, high quality experience for selecting, receiving and returning print textbooks;
- our ability and Ingram's ability to accurately forecast and respond to student demand for print textbooks;
- the pricing of our physical textbooks and eTextbooks for rental or sale in relation to other alternatives, including the prices offered by publishers or by other competing textbook rental providers;
- the quality and prices of our offerings compared to those of our competitors;
- the rate of adoption of eTextbooks and our ability to capture a significant share of that market;
- our ability to engage high school students with our College Admissions and Scholarship Services, Chegg Tutors, Chegg Test Prep and Chegg Writing Tools;
- changes in student spending levels;
- changes in the number of students attending college;
- the effectiveness of our sales and marketing efforts; and
- our ability to introduce new products and services that are favorably received by students.

If we do not attract more students to our connected learning platform and the products and services that we offer or if students do not increase their level of engagement with our platform, our revenues may grow more slowly than expected or decline. Many students use our print textbook service as a result of word-of-mouth advertising and referrals from students who have used this service in the past. If our efforts to satisfy our existing student user base are not successful, we may not be able to attract new students and, as a result, our business will be adversely affected.

If our efforts to build a strong brand are not successful, we may not be able to grow our student user base, which could adversely affect our operating results.

We believe our brand is a key asset of our business. Developing, protecting and enhancing the "Chegg" brand is critical to our ability to expand our student user base and increase student engagement with our connected learning platform. A strong brand also helps to counteract the significant student turnover we experience from year to year as students graduate and differentiates us from our competitors.

To succeed in our efforts to strengthen our brand identity, we must, among other activities:

- maintain our reputation as a trusted source of textbooks, content and services for students;
- maintain the quality of and improve our existing products and services;
- maintain and control the quality of our brand while Ingram handles our textbook fulfillment logistics;
- introduce products and services that are favorably received;
- adapt to changing technologies;
- adapt to students' rapidly changing tastes, preferences, behavior and brand loyalties;
- protect our students' data, such as passwords and personally identifiable information;
- protect our trademark and other intellectual property rights;
- continue to expand our reach to students in high school, graduate school and internationally;
  - ensure that the content posted to our website by students is reliable and does not infringe on third-party copyrights or violate other applicable laws, our terms of use or the ethical codes of those students' colleges;
- adequately address students' concerns with our products and services; and
- convert and fully integrate the brands and students that we acquire, including Imagine Easy Solutions and Internships.com, each into the Chegg brand and Chegg.com.

Our ability to successfully achieve these goals is not entirely within our control and we may not be able to maintain the strength of our brand or do so in a cost effective manner. Factors that could negatively affect our brand include:

-



- changes in student sentiment about the quality or usefulness of our connected learning platform and our products and services;
- problems that prevent Ingram, from delivering textbooks reliably or timely;
- technical or other problems that prevent us from providing our products and services reliably or otherwise negatively affect the student experience on our website or our mobile application;
- concern from colleges about the ways students use our content offerings, such as our Expert Answers service;
- brand conflict between acquired brands and the Chegg brand;
- student concerns related to privacy and the way in which we use student data as part of our products and services;
- the reputation or products and services of competitive companies;
- and

## Table of Contents

students' misuse of our products and services in ways that violate our terms of services, applicable laws or the code of conduct at their colleges.

We intend to offer new products and services to students to grow our business. If our efforts are not successful, our business and financial results would be adversely affected.

Our ability to attract and retain students and increase their engagement with our connected learning platform depends on our ability to connect them with the product, person or service they need to save time, save money, and get smarter. Part of our strategy is to offer students new products and services in an increasingly relevant and personalized way. We may develop such products and services independently, by acquisition or in conjunction with developers and other third parties. For example, in 2016, we acquired Writing Tools service in the acquisition of Imagine Easy Solutions, and we developed Chegg Test Prep internally, the paid version of which we launched in July 2016. The markets for these new products and services may be unproven, and these products may include technologies and business models with which we have little or no prior development or operating experience or may significantly change our existing products and services. In addition, we may be unable to obtain long-term licenses from third-party content providers necessary to allow a product or service, including a new or planned product or service, to function. If our new or enhanced products and services fail to engage our students or attract new students, or if we are unable to obtain content from third parties that students want, we may fail to grow our student base or generate sufficient revenues, operating margin or other value to justify our investments, and our business would be adversely affected.

In the future, we may invest in new products and services and other initiatives to generate revenues, but there is no guarantee these approaches will be successful. Acquisitions of new companies, products and services create integration risk, while development of new products and services and enhancements to existing products and services involve significant time, labor and expense and are subject to risks and challenges including managing the length of the development cycle, entry into new markets, integration into our existing business, regulatory compliance, evolution in sales and marketing methods and maintenance and protection of intellectual property and proprietary rights. If we are not successful with our new products and services, we may not be able to maintain or increase our revenues as anticipated or recover any associated development costs, and our financial results could be adversely affected. For example, in 2014 we acquired a print coupon business, which we later determined to no longer support or expand, and as a result, in 2014 recorded an impairment charge of \$1.6 million related to the write-off of intangible assets from that acquisition.

Our future revenues depend on our ability to continue to attract new students from a high school and college student population that has an inherently high rate of turnover primarily due to graduation, requiring us to invest continuously in marketing to the student population to build brand awareness and loyalty, which we may not be able to accomplish on a cost-effective basis or at all.

We are dependent on the acquisition of new students from a high school and college student population that has an inherently high rate of turnover primarily due to graduation. Most incoming college students will not have previously used products and services like the ones we provide which are geared towards the college market. We rely heavily on word-of-mouth and other marketing channels, including online advertising, search engine marketing and social media. The student demographic is characterized by rapidly changing tastes, preferences, behavior, and brand loyalty. Developing an enduring business model to serve this population is particularly challenging. Our ability to attract new students depends not only on investment in our brand and our marketing efforts, but also on the perceived value of our products and services versus competing alternatives among our extremely price conscious student user base. If our marketing initiatives are not successful or become less effective, or if the cost of such initiatives were to significantly increase, we may not be able to attract new students as successfully or efficiently and, as a result, our revenues and results of operations would be adversely affected. Even if our marketing initiatives succeed in establishing brand awareness and loyalty, we may be unable to maintain and grow our student user base if our competitors, some of

whom are substantially larger and have greater financial resources, adopt aggressive pricing strategies to compete against us. If we are unable to offer competitive prices for our products and services fewer students may use our connected learning platform, products or services.

If we are not able to manage the growth of our business both in terms of scale and complexity, our operating results and financial condition could be adversely affected.

We have expanded rapidly since we launched our online print textbook rental service in 2007. We anticipate further expanding our operations to offer additional products, services and content to help grow our student user base and to take advantage of favorable market opportunities. As we grow, our operations and the technology infrastructure we use to manage and account for our operations will become more complex, and managing these aspects of our business will become more challenging. Any future expansion will likely place significant demands on our resources, capabilities and systems, and we may need to develop new processes and procedures and expand the size of our infrastructure to respond to these demands. If we are

## Table of Contents

not able to respond effectively to new and increasingly complex demands that arise because of the growth of our business, or, if in responding to such demands, our management is materially distracted from our current operations, our operating results and financial condition may be adversely affected.

We may not realize the anticipated benefits of acquisitions, which could disrupt our business and harm our financial condition and results of operations.

As part of our business strategy, we have made and intend to make acquisitions to add specialized employees, complementary businesses, products, services, operations or technologies. Realizing the benefits of acquisitions depends, in part, on our successful integration of acquired companies including their technologies, products, services, operations and personnel in a timely and efficient manner. We may incur significant costs integrating acquired companies and if our integration efforts are not successful we may not be able to offset our acquisition costs. Acquisitions involve many risks that may negatively impact our financial condition and results of operations, including the risks that the acquisitions may:

- require us to incur charges and substantial debt or liabilities;
- cause adverse tax consequences, substantial depreciation or deferred compensation charges;
- result in acquired in-process research and development expenses or in the future may require the amortization, write-down or impairment of amounts related to deferred compensation, goodwill and other intangible assets; and
- give rise to various litigation risks, including the increased likelihood of litigation.

In addition:

- we may not generate sufficient financial return to offset acquisition costs;
- we may encounter difficulties or unforeseen expenditures in integrating the business, technologies, products, services, operations and personnel of any company that we acquire, particularly if key personnel of the acquired company decide not to work for us;
- an acquisition may disrupt our ongoing business, divert resources, increase our expenses and distract our management;
- an acquisition may delay adoption rates or reduce engagement rates for our products and services and those of the company acquired by us due to student uncertainty about continuity and effectiveness of service from either company;
- we may encounter difficulties in, or may be unable to, successfully sell or otherwise monetize any acquired products and services; and
- an acquisition may involve the entry into geographic or business markets in which we have little or no prior experience.

Acquired companies, businesses and assets can be complex and time consuming to integrate. For example, we recently expanded into internships with the acquisition of Internships.com in October 2014 and into writing tools with the acquisition of Imagine Easy Solutions in 2016. We are currently in the process of transitioning these users to the Chegg platform and integrating these brands into the Chegg platform. We may not successfully transition these users to the Chegg platform.

In addition, we have made, and may make in the future, acquisitions that we later determine are not complementary with our evolving business model. For example, in 2014 we acquired a print coupon business, which we later determined to no longer support or expand and as a result, in 2014 recorded an impairment charge of \$1.6 million related to the write-off of acquired intangible assets.

We may pursue additional acquisitions in the future to add specialized employees, complementary companies, products, services or technologies. Our ability to acquire and integrate larger or more complex companies, products, or technologies in a successful manner is unproven. We may not be able to find suitable acquisition candidates, and

we may not be able to complete acquisitions on favorable terms, if at all. To finance any future acquisitions we may issue equity, which could be dilutive, or debt, which could be costly, potentially dilutive, and require substantial restrictions on the conduct of our business. If we fail to successfully complete any acquisitions, integrate the services, products, personnel, operations or technologies associated with such acquisitions into our company, or identify and address liabilities associated with the acquired business or assets, our business, revenues and operating results could be adversely affected. Any future acquisitions we complete may not achieve our goals.

Table of Contents

We rely on third-party software and service providers, including Amazon Web Services (AWS), to provide systems, storage and services for our website. Any failure or interruption experienced by such third parties could result in the inability of students to use our products and services, result in a loss of revenues and harm our reputation.

We rely on third-party software and service providers, including AWS, to provide systems, storage and services, including user log in authentication, for our website. Any technical problem with, cyber-attack on, or loss of access to such third parties' systems, servers or technologies could result in the inability of our students to rent or purchase print textbooks, interfere with access to our digital content and other online products and services or result in the theft of end-user personal information.

Our reliance on AWS makes us vulnerable to any errors, interruptions, or delays in their operations. Any disruption in the services provided by AWS could harm our reputation or brand or cause us to lose students or revenues or incur substantial recovery costs and distract management from operating our business. AWS may terminate its agreement with us upon 30 days' notice. Upon expiration or termination of our agreement with AWS, we may not be able to replace the services provided to us in a timely manner or on terms and conditions, including service levels and cost, that are favorable to us, and a transition from one vendor to another vendor could subject us to operational delays and inefficiencies until the transition is complete.

We rely heavily on our proprietary technology to process deliveries and returns of the textbooks and to manage other aspects of our operations. The failure of this technology to operate effectively, particularly during peak periods, could adversely affect our ability to retain and attract student users.

We use complex proprietary software to process deliveries and returns of the textbooks and to manage other aspects of our operations, including systems to consider the market price for textbooks, general availability of textbook titles and other factors to determine how to buy textbooks and set prices for textbooks and other content in real time. We rely on the expertise of our engineering and software development teams to maintain and enhance the software used for our distribution operations. We cannot be sure that the maintenance and enhancements we make to our distribution operations will achieve the intended results or otherwise be of value to students. If we are unable to maintain and enhance our technology to manage the shipping and return of textbooks in a timely and efficient manner, particularly during peak periods, our ability to retain existing students and to add new students may be impaired.

Any significant disruption to our computer systems, especially during peak periods, could result in a loss of students, colleges and/or brands which could harm our business, results of operations and financial condition.

We rely on computer systems housed in six facilities, three located on the East Coast and three located on the West Coast, to manage our operations. We have experienced and expect to continue to experience periodic service interruptions and delays involving our systems. While we maintain a live fail-over capability that would allow us to switch our operations from one facility to another in the event of a service outage, that process would still result in service interruptions that could be significant in duration. These service interruptions could have a disproportionate effect on our operations if they were to occur during one of our peak periods. Our facilities are vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunications failures and similar events. Our facilities also are subject to break-ins, sabotage, intentional acts of vandalism, the failure of physical, administrative and technical security measures, terrorist acts, natural disasters, human error, the financial insolvency of our third-party vendors, and other unanticipated problems or events. The occurrence of any of these events could result in interruptions in our service and unauthorized access to, theft or alteration of, the content and data contained on our systems. We also rely on systems and infrastructure of the Internet to operate our business and provide our services. Interruptions in our own systems or in the infrastructure of the Internet could hinder our ability to operate our business, damage our reputation or brand and result in a loss of students, colleges or brands which could harm our business, results of operations and financial condition.



## Table of Contents

Increased activity during peak periods places substantially increased strain on our operations and any failure to deliver our products and services during these periods will have an adverse effect on student satisfaction and our revenues.

We historically experience a disproportionate amount of activity to occur on our website at the beginning of each academic term as students search our textbook catalog and place orders for course materials. If too many students access our website within a short period of time due to increased demand, we may experience system interruptions that make our website unavailable, slowed or prevent Ingram from efficiently fulfilling rental orders, which may reduce the volume of textbooks we are able to rent or sell and may also impact our ability to sell marketing services to colleges and brands. In addition, during peak periods, we utilize, and Ingram utilizes, independent contractors and temporary personnel to supplement the workforce primarily in our student advocacy organizations and in Ingram's warehouses. Competition for qualified personnel has historically been intense, and we or Ingram may be unable to adequately staff our student advocacy organizations or Ingram's warehouses during these peak periods. For example, during the 2014 fall rush period, our staffing agencies were not able to provide as many temporary personnel as we expected. Any understaffing could lead to an increase in both the amount of time required to ship textbooks, which could lead to student dissatisfaction, and increase the amount of time required to process a rental return, which could result in Ingram purchasing more inventory than necessary. Moreover, UPS and FedEx, the third-party carriers that Ingram primarily relies on to deliver textbooks to students, and publishers, wholesalers and distributors that ship directly to our students may be unable to meet our shipping and delivery requirements during peak periods, especially during inclement weather. Any such disruptions to our business could cause our customers to be dissatisfied with our products and services and have an adverse effect on our revenues.

Computer malware, viruses, hacking, phishing attacks and spamming could harm our business and results of operations.

Computer malware, viruses, physical or electronic break-ins and similar disruptions could lead to interruptions and delays in our services and operations and loss, misuse or theft of data. Computer malware, viruses, computer hacking and phishing attacks against online networking platforms have become more prevalent and may occur on our systems in the future. We believe that we could be a target for such attacks because of the incidence of hacking among students.

Any attempts by hackers to disrupt our website service or our internal systems, if successful, could harm our business, be expensive to remedy and damage our reputation or brand. Our network security business disruption insurance may not be sufficient to cover significant expenses and losses related to direct attacks on our website or internal systems. Efforts to prevent hackers from entering our computer systems are expensive to implement and may limit the functionality of our services. Though it is difficult to determine what, if any, harm may directly result from any specific interruption or attack, any failure to maintain performance, reliability, security and availability of our products and services and technical infrastructure may harm our reputation, brand and our ability to attract students to our website. Any significant disruption to our website or internal computer systems could result in a loss of students, colleges or brands and, particularly if disruptions occur during the peak periods at the beginning of each academic term, could adversely affect our business and results of operations.

We may not timely and effectively scale and adapt our existing technology and network infrastructure to ensure that our connected learning platform is accessible and delivers a satisfactory user experience to students.

It is important to our success that students be able to access our connected learning platform at all times. We have previously experienced, and may in the future experience, service disruptions, outages and other performance problems due to a variety of factors, including infrastructure changes, third-party service providers, human or software errors and capacity constraints due to an overwhelming number of students accessing our platform simultaneously. If our connected learning platform is unavailable when students attempt to access it or it does not load as quickly as they



expect, students may seek other services to obtain the information for which they are looking and may not return to our platform as often in the future, or at all. This would negatively impact our ability to attract students and brands and the frequency with which they use our website and mobile applications.

Our platform functions on software that is highly technical and complex and may now or in the future contain undetected errors, bugs, or vulnerabilities. Some errors in our software code may only be discovered after the code has been deployed. Any errors, bugs, or vulnerabilities discovered in our code after deployment, inability to identify the cause or causes of performance problems within an acceptable period of time or difficulty maintaining and improving the performance of our platform, particularly during peak usage times, could result in damage to our reputation or brand, loss of students, colleges and brands, loss of revenues, or liability for damages, any of which could adversely affect our business and financial results.

We expect to continue to make significant investments to maintain and improve the availability of our platform and to enable rapid releases of new features and products. To the extent that we do not effectively address capacity constraints,

## Table of Contents

upgrade our systems as needed and continually develop our technology and network architecture to accommodate actual and anticipated changes in technology, our business and operating results may be harmed.

We have a disaster recovery program to transition our operating platform and data to a failover location in the event of a catastrophe and have tested this capability under controlled circumstances, however, there are several factors ranging from human error to data corruption that could materially lengthen the time our platform is partially or fully unavailable to our student user base as a result of the transition. If our platform is unavailable for a significant period of time as a result of such a transition, especially during peak periods, we could suffer damage to our reputation or brand, loss of students, colleges and brands or loss of revenues any of which could adversely affect our business and financial results.

Our reputation and relationships with students and tutors would be harmed if our users' data, particularly billing data, were to be accessed by unauthorized persons.

We maintain personal data regarding students and tutors who use our platform, including names and, in many cases, mailing addresses, and, in the case of tutors, information necessary for payment and tax filings. We take measures to protect against unauthorized intrusion into our users' data. However, despite these measures, if we or our payment processing services experience any unauthorized intrusion into our users' data, current and potential users may become unwilling to provide the information to us necessary for them to engage with our platform, we could face legal claims and our business and reputation could be adversely affected. The breach of a third-party's website, resulting in theft of user names and passwords, could result in the fraudulent use of that user login information on our platform. In addition, we do not obtain signatures from students in connection with the use of credit cards by them. Under current credit card practices, to the extent we do not obtain cardholders' signatures, we are liable for fraudulent credit card transactions, even when the associated financial institution approves payment of the orders. From time to time, fraudulent credit cards may be used. We may experience some loss from these fraudulent transactions. As an example, we discovered in 2014 that certain individuals fraudulently obtained several thousand textbooks from us. While we do have safeguards in place, we cannot be certain that other fraudulent schemes will not be successful. A failure to adequately control fraudulent transactions would harm our business and results of operations.

Difficulties that could arise from our partnership with Ingram may have an adverse effect on our business and results of operations.

We rely on Ingram to make new investments in the textbook library and fulfill our print textbook rentals and sales orders. We purchase used books on Ingram's behalf, including books through our buyback program, and invoice Ingram at cost. As we no longer own a significant number of textbooks, we have become increasingly committed to this strategic partnership. If our continuing partnership with Ingram is interrupted or if Ingram experiences disruptions in its business or is not able to perform as anticipated, Ingram may not be able to reimburse us for the books we have procured on its behalf, especially after having moved to normal payment terms in January 2017, or we may experience operational difficulties, an inability to fulfill print textbook orders, increased costs and a loss of business, as well as a greater than expected deployment of capital for textbook acquisition, that may have a material adverse effect on our business, results of operations and financial condition. Furthermore, if we are unable to achieve the financial return targets set forth in our agreement with Ingram, we could be required to make additional payments to Ingram which could adversely affect our results of operations.

Ingram purchases, and we price, textbooks based on anticipated levels of demand and other factors that we estimate based on historical experience and various other assumptions. If actual results differ materially from our estimates, our gross margins may decline.

The print textbook rental distribution model requires our fulfillment partner, Ingram, to make substantial investments in its print textbook library based on our expectations regarding numerous factors, including ongoing demand for these titles in print form. To realize a return on its investments, we must rent each purchased textbook multiple times, and as such, we are exposed to the risk of not achieving financial return targets set forth in our agreement with Ingram, which could result in additional payments to Ingram and adversely affect our results of operations. We typically plan the textbook purchases based on factors such as pricing, our demand forecast for the most popular titles, estimated timing of edition changes, estimated utilization levels and planned liquidations of stale, old or excess titles in the print textbook library. These factors are highly unpredictable and can fluctuate substantially, especially if pricing pressure becomes more intense, as we have seen in recent rush cycles, or demand is reduced due to seasonality or other factors, including increased use of eTextbooks. We rely on a proprietary model to analyze and optimize the purchasing decisions and rely on inputs from third parties including publishers, distributors, wholesalers and colleges to make our decisions. We also rely on students to return print textbooks to Ingram in a timely manner and in good condition so that we can re-rent or sell those textbooks. If the information we receive from third parties is not accurate or reliable, if students fail to return books or return damaged books, or if we for any other reason forecast demand inaccurately and cause Ingram to acquire insufficient copies of specific textbooks, we may be unable to satisfy student

## Table of Contents

demand or we may have to incur significantly increased costs in order to do so, in which event our student satisfaction and results of operations could be affected adversely. Conversely, if we attempt to mitigate this risk and cause Ingram to acquire more copies than needed to satisfy student demand, then our textbook utilization rates would decline and we may be required to make additional payments to Ingram and our gross margins would be affected adversely.

When deciding whether to offer a textbook for rent and the price we charge for that rental, we also must weigh a variety of factors and assumptions and if our judgments or assumptions are incorrect, our gross margins may be adversely affected. Certain textbooks cost more to acquire depending on the source from which they are acquired and the terms on which they are acquired. We must factor in some projection of the number of rentals we will be able to achieve with such textbooks and at what rental price, among other factors, to determine whether we believe it will be profitable to cause Ingram to acquire such textbooks and for us to offer them for rent. If the textbooks Ingram acquires are lost, determined to be unauthorized copies, or damaged prematurely, Ingram may not be able to recover its costs or generate revenues on those textbooks. If we are unable to effectively make decisions about whether to cause Ingram to acquire textbooks and the price we charge to rent those textbooks, including if the assumptions upon which our decisions are made prove to be inaccurate, our gross margins may decline significantly and if, as a result, we are unable to achieve the financial return targets set forth in our agreement with Ingram, we could be required to make additional payments to Ingram which could adversely affect our results of operations.

If Ingram's relationships with the shipping providers that deliver textbooks directly to our students are terminated or impaired, if shipping costs increase or if these vendors are unable to timely deliver textbooks to our students, our business and results of operations could be substantially harmed.

Ingram predominantly relies on UPS to deliver textbooks from its textbook warehouse and to return textbooks to Ingram from our students. To a lesser extent Ingram relies on FedEx for delivery of print textbook rentals and on publishers, distributors and wholesalers to fulfill a certain portion of textbook sales orders and liquidations. As a result, our business could be subject to carrier disruptions and increased costs due to factors that are beyond our control, including labor difficulties, inclement weather, increased fuel costs and other rising costs of transportation and terrorist activity. If UPS were to limit its services or delivery areas, such as by the discontinuation of Saturday delivery service, Ingram's ability to timely deliver textbooks could diminish, and our student satisfaction could be adversely affected. If Ingram's relationships with its shipping vendors are terminated or impaired or if Ingram's shipping vendors are unable to deliver merchandise for us, Ingram would be required to rely on alternative carriers for delivery and return shipments of textbooks to and from students. Ingram may be unable to sufficiently engage alternative carriers on a timely basis or on terms favorable to them, if at all. If textbooks are not delivered on time to students, they could become dissatisfied and discontinue their use of our service, which could adversely affect our operating results.

We may need additional capital, and we cannot be sure that additional financing will be available or on favorable terms.

Historically, investments in our business have substantially exceeded the cash we have generated from our operations. We have funded our operating losses and capital expenditures through proceeds from equity and debt financings, equipment leases and cash flow from operations. Although we currently anticipate that our available funds and cash flow from operations will be sufficient to meet our cash needs for the foreseeable future, we may require additional financing, particularly if the investment required to fund our operations is greater than we anticipate or we choose to invest in new technologies or complementary businesses or change our business model. Our ability to obtain financing will depend, among other things, on our development efforts, business plans, operating performance and condition of the capital markets at the time we seek financing. Additional financing may not be available to us on favorable terms when required, or at all especially considering that we no longer own a print textbook library, which we previously used as collateral for our debt financings. If we raise additional funds through the issuance of equity, equity-linked or

debt securities, those securities may have rights, preferences or privileges senior to the rights of our common stock, and our stockholders may experience substantial dilution.

We face significant competition in each aspect of our business, and we expect such competition to increase, particularly in the market for textbooks.

Our products and services compete for students, colleges and advertisers and we expect such competition to increase, as described below.

Products and Services for Students. Our Chegg Services face competition from different businesses depending on the offering. For Chegg Study, our competitors primarily include publishers that provide study materials and online instructional systems. Additionally, we face competition from free services such as Yahoo! Answers and Brain.ly for our Expert Answers service. For our Chegg Tutors services, we face competition from other online tutoring services such as Tutors.com and Varsity Tutors. For our writing tools, we primarily face competition

## Table of Contents

from other citation generating services such as Noodle Tools. The market for textbooks and supplemental materials is intensely competitive and subject to rapid change. We face competition from college bookstores, some of which are operated by Follett and Barnes & Noble Education, online marketplaces such as Amazon.com and providers of eTextbooks such as Apple iTunes, and Blackboard, as well as various private textbook rental websites. Many students purchase from multiple textbook providers, are highly price sensitive and can easily shift spending from one provider or format to another. As a consequence, our Required Materials product line, which includes eTextbooks, competes primarily on price and further on selection and functionality and compatibility of our eTextbook Reader across a wide variety of desktop and mobile devices.

**Enrollment Marketing Services.** With respect to our enrollment marketing services, we compete against traditional methods of student recruitment, including student data providers such as standardized test providers, radio, television and Internet advertising and print mail marketing programs. In this area, we compete primarily on the basis of the number of high-quality connections between prospective students and colleges we are able to provide as well as on price. We are able to create these connections by providing prospective students with an easy-to-use platform to input their academic information and aspirations, learn about colleges, locate scholarships and financial aid and facilitate and streamline the application process.

**Brand Advertising.** With respect to brands, we compete with online and offline outlets that generate revenues from advertisers and marketers, especially those that target high school and college students. In this area, we seek to partner with brands that have offerings that will interest or delight students and have received very positive comments and feedback from students on these offerings. We provide these brands with preferential access to our audience, which we believe represents a highly engaged portion of the target demographic of our brand partners.

Our industry is evolving rapidly and is becoming increasingly competitive. Many of our competitors have longer operating histories, larger customer bases, greater brand recognition and significantly greater financial, marketing and other resources than we do. Some of our competitors have adopted, and may continue to adopt, aggressive pricing policies and devote substantially more resources to marketing, website and systems development than we do. In addition, a variety of business models are being pursued for the provision of print textbooks, some of which may be more profitable or successful than our business model. For example, a recent U.S. Supreme Court decision may make it easier for third parties to import low-cost “gray market” textbooks for resale in the United States, and these textbooks may compete with our offerings. In addition, Follett has partnered with some colleges through its includedED program, which allows schools to deliver required course materials directly to students by including them in the cost of college as part of tuition and fees. Such strategic alliances may eliminate our ability to compete favorably with our Required Materials product line because of the added convenience they offer to students, which may result in reduced textbook rentals, loss of market share and reduced revenues. In addition, our competitors also may form or extend strategic alliances with publishers that could adversely affect Ingram's ability to obtain textbooks on favorable terms. We face similar risks from strategic alliances by other participants in the education ecosystem with respect to our newer offerings. We may, in the future, establish alliances or relationships with other competitors or potential competitors. To the extent such alliances are terminated or new alliances and relationships are established, our business could be harmed.

Our business is seasonal and we have increased risk from disruption during peak periods which makes our operating results difficult to predict.

We derive a significant portion of our net revenues from print textbook rental and, to a lesser extent, sale transactions, which occur in large part during short periods of time around the commencement of the fall, winter and spring academic terms. In particular, we and Ingram experience the largest increase in rental and sales volumes during the last two weeks of August and first two weeks of September and to a lesser degree in December and in January. The increased volume of orders that we and Ingram have to process during these limited periods of time means that any

shortfalls or disruptions in our operations during these peak periods will have a disproportionately large impact on our annual operating results and the potential future growth of our business.

As a result of this seasonality, which corresponds to the academic calendar, our revenues fluctuate significantly quarter to quarter depending upon the timing of where we are in our “rush” cycle and sequential quarter-over-quarter comparisons of our revenues and operating results are not likely to be meaningful. In addition, our operating results for any given quarter cannot be used as an accurate indicator of our results for the year. In particular, we anticipate that our ability to accurately forecast financial results for future periods will be most limited at the time we present our second quarter financial results, which will generally occur midsummer and precede the “fall rush.” In addition, our other offerings, in particular services unrelated to textbooks, are relatively new and, as a result, we have limited experience with forecasting revenues from them.

## Table of Contents

The fourth quarter has typically been our highest performing quarter as we were recognizing a full quarter of revenues on print textbooks that we owned from peak volumes in August and September and partial revenues from peak volumes in December, while the second quarter has typically been our lowest performing quarter as students start their summer vacations and the volume of our textbook rentals and sales and purchases of supplemental materials and Chegg Study decreases. With Ingram fulfilling our print textbook rental orders, we now expect our first and third quarters to be higher as we now recognize a commission immediately on the transaction of an Ingram-owned print textbook rather than recognizing the revenues ratably over the term the student rents one of our print textbooks.

We base our operating expense budgets on expected net revenue trends. Operating expenses, similar to revenues and cost of revenues, fluctuate significantly quarter to quarter due to the seasonality of our business and are generally higher during the first and third quarters as we incur marketing expense in connection with our peak periods at the beginning of each academic term. Because our revenues were historically concentrated in the fourth quarter and expenses are concentrated in the first and third quarters, we have experienced operating losses in the first and third quarters and operating income in the fourth quarter. As a result, sequential quarterly comparison of our financial results has not been meaningful. We expect our seasonality to shift as a result of our strategic partnership with Ingram and our highest quarters for revenues and operating expense to coincide. Further, a portion of our expenses, such as office space lease obligations and personnel costs, are largely fixed and are based on our expectations of our peak levels of operations. The Ingram partnership has resulted in our operating expenses related to textbook acquisition, shipping and fulfillment and warehouse facility lease obligations either decrease or be eliminated and we expect that our overall operating expenses to be more evenly distributed throughout the year. Nonetheless, we expect to continue to incur significant marketing expenses during peak periods and to have fixed expenses for office space and personnel and as such, we may be unable to adjust spending quickly enough to offset any unexpected revenues shortfall. Accordingly, any shortfall in net revenues may cause significant variation in operating results in any quarter.

Growing our student user base and their engagement with our connected learning platform through mobile devices depends upon the effective operation of our mobile applications with mobile operating systems, networks and standards that we do not control.

There is no guarantee that students will use our mobile applications, such as the mobile version of our website, m.chegg.com, Chegg Flashcards and Chegg Textbook Solutions, rather than competing products. We are dependent on the interoperability of our mobile applications with popular mobile operating systems that we do not control, such as Google's Android and Apple's iOS, and any changes in such systems that degrade our products' functionality or give preferential treatment to competitive products could adversely affect the usage of our applications on mobile devices. Additionally, in order to deliver high quality mobile products, it is important that our products work well with a range of mobile technologies, systems, networks and standards that we do not control. We may not be successful in developing relationships with key participants in the mobile industry or in developing products that operate effectively with these technologies, systems, networks or standards. In the event that it is more difficult for students to access and use our applications on their mobile devices, or if students choose not to access or use our applications on their mobile devices or use mobile products that do not offer access to our applications, our student growth and student engagement levels could be harmed.

If we are not able to maintain the compatibility of our eTextbook Reader with third-party operating systems, demand for our eTextbooks may decline and have an adverse effect on our operating results.

Our eTextbook Reader is designed to provide students with access to eTextbooks from any device with an Internet connection and an Internet browser, including PCs, iPads, Android tablets, Kindles, Nooks and mobile phones. Our eTextbook Reader can be used across a variety of third-party operating systems. If we are not able to maintain the compatibility of our eTextbook Reader with third-party operating systems, demand for our eTextbooks could decline and revenues would be adversely affected. We may desire in the future to make our eTextbook Reader compatible



with new or existing third-party operating systems that achieve popularity within the education marketplace, and these third-party operating systems may not be compatible with our designs. Any failure on our part to modify our applications to ensure compatibility with such third-party operating systems could reduce demand for our products and services.

## Table of Contents

If the transition from print textbooks to eTextbooks does not proceed as we expect, our business and financial condition will be adversely affected.

The textbook distribution market has begun shifting toward digital distribution. If demand for eTextbooks accelerates more rapidly than we expect, we could be required to make additional payments to Ingram under our inventory purchase and consignment agreement. Conversely, if the transition to digital distribution of textbooks does not gain market acceptance as we expect, capital requirements over the long term may be greater than we expect and our opportunities for growth may be diminished. In that case, we may need to raise additional capital, which may not be available on reasonable terms, or at all, and we may not realize the potential long-term benefits of a shift to digital distribution, including greater pricing flexibility, the ability to distribute a larger library of eTextbooks compared to print textbooks and lower cost of revenues.

If publishers refuse to grant us distribution rights to digital content on acceptable terms or terminate their agreements with us, or if we are unable to adequately protect their digital content rights, our business could be adversely affected.

We rely on licenses from publishers to distribute eTextbooks to our customers and to provide some of our other products and services. We do not have long-term contracts or arrangements with most publishers that guarantee the availability of such digital content. If we are unable to secure and maintain rights to distribute, or otherwise use, the digital content upon terms that are acceptable to us, or if publishers terminate their agreements with us, we would not be able to acquire such digital content from other sources and our ability to attract new students and retain existing students could be adversely impacted. Some of our licenses give the publisher the right to withdraw our rights to distribute or use the digital content without cause and/or give the publisher the right to terminate the entire license agreement without cause. If a publisher exercises such a right, this could adversely affect our business and financial results. Moreover, to the extent we are able to secure and maintain rights to distribute eTextbooks, our competitors may be able to obtain the same rights on more favorable terms.

In addition, our ability to distribute eTextbooks depends on publishers' belief that we include effective digital rights management technology to control access to digital content. If the digital rights management technology that we use is compromised or otherwise malfunctions, we could be subject to claims, and publishers may be unwilling to include their content in our service. If users are able to circumvent the digital rights management technology that we use, they may acquire unauthorized copies of the textbooks that they would otherwise rent from us, which could decrease our textbook rental volume and adversely affect our results of operations.

If we fail to convince brands of the benefits of advertising on our platform or to use our marketing services, our business could be harmed.

Our business strategy includes increasing our revenues from brand advertising. Brands may view our connected learning platform as experimental and unproven. They may not do business with us, or may reduce the amounts they are willing to spend to advertise with us, if we do not deliver ads, sponsorships and other commercial content and marketing programs in an effective manner, or if they do not believe that their investment in advertising with us will generate a competitive return relative to other alternatives. Our ability to grow the number of brands that use our brand advertising, and ultimately to generate advertising and marketing services revenues, depends on a number of factors, including our ability to successfully:

- compete for advertising and marketing dollars from colleges, brands, online marketing and media companies and advertisers;
- penetrate the market for student-focused advertising;
-

develop a platform that can deliver advertising and marketing services across multiple channels, including print, email, Internet, mobile applications and other connected devices;

- improve our analytics and measurement solutions to demonstrate the value of our advertising and marketing services;
- maintain the retention, growth and engagement of our student user base;
- strengthen our brand and increase our presence in media reports and with publicity companies that utilize online platforms for advertising and marketing purposes;
- create new products that sustain or increase the value of our advertising and marketing services and other commercial content;
- manage changes in the way online advertising and marketing services are priced;
- weather the impact of macroeconomic conditions and conditions in the advertising industry and higher education in general; and
- manage legal developments relating to data privacy, advertising or marketing services, legislation and regulation and litigation.

## Table of Contents

If Internet search engines' methodologies are modified or our search result page rankings decline for other reasons, student engagement with our website could decline.

We depend in part on various Internet search engines, such as Google, Bing and Yahoo!, to direct a significant amount of traffic to our website. Similarly, we depend on mobile app stores such as iTunes and Google Play to allow students to locate and download Chegg mobile applications that enable our service. Our ability to maintain the number of students directed to our website is not entirely within our control. Our competitors' search engine optimization (SEO) efforts may result in their websites receiving a higher search result page ranking than ours, or Internet search engines could revise their methodologies in an attempt to improve their search results, which could adversely affect the placement of our search result page ranking. If search engine companies modify their search algorithms in ways that are detrimental to our search result page ranking or in ways that make it harder for students to find our website, or if our competitors' SEO efforts are more successful than ours, overall growth could slow, student engagement could decrease, and fewer students may use our platform. These modifications may be prompted by search engine companies entering the online networking market or aligning with competitors. Our website has experienced fluctuations in search result rankings in the past, and we anticipate similar fluctuations in the future. Any reduction in the number of students directed to our website could harm our business and operating results.

Our core value of putting students first may conflict with the short-term interests of our business.

We believe that adhering to our core value of putting students first is essential to our success and in the best interests of our company and the long-term interests of our stockholders. In the past, we have forgone, and in the future we may forgo, short-term revenue opportunities that we do not believe are in the best interests of students, even if our decision negatively impacts our operating results in the short term. For example, we offer free services to students that require investment by us, such as our Internships service, in order to promote a more comprehensive solution. We also developed the Chegg for Good program to connect students and employees with partners to engage them in causes related to education and the environment. We work with the nonprofit conservation organization American Forest to plant trees around the world and our funding has enabled the planting of more than six million trees to date. We formed the Chegg Foundation, a California nonprofit public benefit corporation, to engage in charitable and education-related activities, which we funded with one percent of the net proceeds from our IPO in November 2013. Our philosophy of putting students first may cause us to make decisions that could negatively impact our relationships with publishers, colleges and brands, whose interests may not always be aligned with ours or those of our students. Our decisions may not result in the long-term benefits that we expect, in which case our level of student satisfaction and engagement, business and operating results could be harmed.

If we are required to discontinue certain of our current marketing activities, our ability to attract new students may be adversely affected.

Laws or regulations may be enacted which restrict or prohibit use of emails or similar marketing activities that we currently rely on. For example:

the CAN-SPAM Act of 2003 and similar laws adopted by a number of states regulate unsolicited commercial emails, create criminal penalties for emails containing fraudulent headers and control other abusive online marketing practices;

the U.S. Federal Trade Commission (FTC) has guidelines that impose responsibilities on companies with respect to communications with consumers and impose fines and liability for failure to comply with rules with respect to advertising or marketing practices they may deem misleading or deceptive; and

the TCPA restricts telemarketing and the use of automated telephone equipment. The TCPA limits the use of automatic dialing systems, artificial or prerecorded voice messages and SMS text messages. It also applies to unsolicited text messages advertising the commercial availability of goods or services. Additionally, a number of

states have enacted statutes that address telemarketing. For example, some states, such as California, Illinois and New York, have created do-not-call lists. Other states, such as Oregon and Washington, have enacted “no rebuttal statutes” that require the telemarketer to end the call when the consumer indicates that he or she is not interested in the product being sold. Restrictions on telephone marketing, including calls and text messages, are enforced by the FTC, the Federal Communications Commission, states and through the availability of statutory damages and class action lawsuits for violations of the TCPA.

Even if no relevant law or regulation is enacted, we may discontinue use or support of these activities if we become concerned that students or potential students deem them intrusive or they otherwise adversely affect our goodwill and brand. If our marketing activities are curtailed, our ability to attract new students may be adversely affected.

Table of Contents

Our business and growth may suffer if we are unable to hire and retain key personnel.

We depend on the continued contributions of our senior management and other key personnel. In particular, we rely on the contributions of our Chief Executive Officer, Dan Rosensweig. All of our executive officers and key employees are at-will employees, meaning they may terminate their employment relationship at any time. We compensate our employees through a combination of salary, benefits and equity compensation. Volatility or a decline in our stock price may affect our ability to retain and motivate key employees, each of whom has been granted stock options, RSUs or both. Competition for qualified personnel can be intense, and we may not be successful in retaining and motivating such personnel, particularly to the extent our stock price remains volatile or at a depressed level, as equity compensation plays an important role in how we compensate our employees. Such individuals may elect to seek employment with other companies that they believe have better long-term prospects. If we lose the services of one or more members of our senior management team or other key personnel, or if one or more of them decides to join a competitor or otherwise compete directly or indirectly with us, we may not be able to successfully manage our business or achieve our business objectives. Our future success also depends on our ability to identify, attract and retain highly skilled technical, managerial, finance and media procurement personnel. Qualified individuals are in high demand, particularly in the San Francisco Bay Area where our executive offices are located, and we may incur significant costs to attract them. If we are unable to attract or retain the personnel we need to succeed, our business may suffer.

Government regulation of education and student information is evolving, and unfavorable developments could have an adverse effect on our operating results.

We are subject to regulations and laws specific to the education sector because we offer our products and services to students and collect data from students. Data privacy and security with respect to the collection of personally identifiable information from students continues to be a focus of worldwide legislation and regulation. This includes significant regulation in the European Union and legislation and compliance requirements in various jurisdictions around the world. Within the United States, several states have enacted legislation that goes beyond any federal requirements relating to the collection and use of personally identifiable information and other data from students. Examples include statutes adopted by the State of California and most other States that require online services to report certain breaches of the security of personal data and a California statute that requires companies to provide choice to California customers about whether their personal data is disclosed to direct marketers or to report to California customers when their personal data has been disclosed to direct marketers. In this regard, there are a large number of legislative proposals before the U.S. Congress and various state legislative bodies regarding privacy issues related to our business. It is not possible to predict whether or when such legislation may be adopted, and certain proposals, if adopted, could harm our business through a decrease in student registrations and revenues. These decreases could be caused by, among other possible provisions, the required use of disclaimers or other requirements before students can utilize our services. We post our privacy policies and practices concerning the use and disclosure of student data on our website. However, any failure by us to comply with our posted privacy policies, FTC requirements or other privacy-related laws and regulations could result in proceedings by governmental or regulatory bodies or by private litigants that could potentially harm our business, results of operations and financial condition.

Our business may also be subject to laws specific to students, such as the Family Educational Rights and Privacy Act, the Delaware Higher Education Privacy Act and a California statute which restricts the access by postsecondary educational institutions of prospective students' social media account information. Compliance levels include disclosures, consents, transfer restrictions, notice and access provisions for which we may in the future need to build further infrastructure to further support. We cannot guarantee that we have been or will be fully compliant in every jurisdiction, as it is not entirely clear how existing laws and regulations governing educational institutions affect our business. Moreover, as the education industry continues to evolve, increasing regulation by federal, state and foreign agencies becomes more likely. Recently, California adopted the Student Online Personal Information Protection Act

which prohibits operators of online services used for K-12 school purposes from using or sharing student personal information and Colorado adopted House Bill 16-1423 designed to protect the use of student personal data in elementary and secondary school. These acts do not apply to general audience Internet websites but it is not clear how these acts will be interpreted and the breadth of services that will be restricted by it. Other states may adopt similar statutes. The adoption of any laws or regulations that adversely affect the popularity or growth in the use of the Internet particularly for educational services, including laws limiting the content that we can offer, and the audiences that we can offer that content to, may decrease demand for our service offerings and increase our cost of doing business. Future regulations, or changes in laws and regulations or their existing interpretations or applications, could also hinder our operational flexibility, raise compliance costs and result in additional historical or future liabilities for us, resulting in adverse impacts on our business and our operating results.

While we expect and plan for new laws, regulations and standards to be adopted over time that will be directly applicable to the Internet and to our student-focused activities, any existing or new legislation applicable to our business could expose us to substantial liability, including significant expenses necessary to comply with such laws and regulations and

Table of Contents

potential penalties or fees for non-compliance, and could negatively impact the growth in the use of the Internet for educational purposes and for our services in particular. We may also run the risk of retroactive application of new laws to our business practices that could result in liability or losses. Due to the global nature of the Internet, it is possible that the governments of other states and foreign countries might attempt to change previous regulatory schemes or choose to regulate transmissions or prosecute us for violations of their laws. We might unintentionally violate such laws, such laws may be modified and new laws may be enacted in the future. Any such developments could harm our business, operating results and financial condition. We may be subject to legal liability for our offerings.

We collect, process, store and use personal information and data, which subjects us to governmental regulation and other legal obligations related to privacy and our actual or perceived failure to comply with such obligations could harm our business.

In the ordinary course of business, and in particular in connection with merchandising our service to students, we collect, process, store and use personal information and data supplied by students and tutors. We may enable students to share their personal information with each other and with third parties and to communicate and share information into and across our platform. Other businesses have been criticized by privacy groups and governmental bodies for attempts to link personal identities and other information to data collected on the Internet regarding users' browsing and other habits. There are numerous federal, state and local laws regarding privacy and the collection, storing, sharing, using, processing, disclosing and protecting of personal information and other user data, the scope of which are changing, subject to differing interpretations, and which may be costly to comply with and may be inconsistent between countries and jurisdictions or conflict with other rules.

We currently face certain legal obligations regarding the manner in which we treat such information. Increased regulation of data utilization practices, including self-regulation or findings under existing laws, or new regulations restricting the collection, use and sharing of information from minors under the age of 18, that limit our ability to use collected data could have an adverse effect on our business. In addition, if unauthorized access to our students' data were to occur or if we were to disclose data about our student users in a manner that was objectionable to them, our business reputation and brand could be adversely affected, and we could face legal claims that could impact our operating results. Our reputation and brand and relationships with students would be harmed if our billing data were accessed by unauthorized persons.

We strive to comply with all applicable laws, policies, legal obligations and industry codes of conduct relating to privacy and data protection. However, U.S. federal, U.S. state and international laws and regulations regarding privacy and data protection are rapidly evolving and may be inconsistent and we could be deemed out of compliance as such laws and their interpretation change. In addition, foreign privacy, data protection, and other laws and regulations, particularly in Europe, are often more restrictive than those in the United States. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to our business operations may limit the use and adoption of our services and reduce overall demand for them. Furthermore, foreign court judgments or regulatory actions could impact our ability to transfer, process and/or receive transnational data, including data relating to students or partners outside the United States. Such judgments or actions could affect the manner in which we provide our services or adversely affect our financial results if foreign students and partners are not able to lawfully transfer data to us. For example, the European Court of Justice recently invalidated the U.S.-EU Safe Harbor framework that had been in place since 2000, which allowed companies to meet certain European legal requirements for the transfer of personal data from the European Economic Area to the United States. While other adequate legal mechanisms to lawfully transfer such data remain, the invalidation of the U.S.-EU Safe Harbor framework may result in different European data protection regulators applying differing standards for the transfer of personal data, which could result in increased regulation, cost of compliance and limitations on data transfer for us and our customers. In addition, some countries are considering or have passed legislation implementing data protection requirements or requiring local



storage and processing of data or similar requirements that could increase the cost and complexity of delivering our services.

Any failure or perceived failure by us to comply with our privacy policies, our privacy or data-protection obligations to students or other third parties, our privacy or data-protection legal obligations or any compromise of security that results in the unauthorized release or transfer of sensitive information, which may include personally identifiable information or other data, may result in governmental enforcement actions, litigation or public statements against us by consumer advocacy groups or others and could cause students to lose trust in us, which could have an adverse effect on our business. Additionally, if third parties we work with, such as colleges and brands, violate applicable laws or our policies, such violations may also put our student users' information at risk and could in turn have an adverse effect on our business.

Table of Contents

Public scrutiny of Internet privacy issues may result in increased regulation and different industry standards, which could deter or prevent us from providing our current products and services to students, thereby harming our business.

The regulatory framework for privacy issues worldwide is currently in flux and is likely to remain so for the foreseeable future. Practices regarding the collection, use, storage, display, processing, transmission and security of personal information by companies offering online services have recently come under increased public scrutiny. The U.S. government, including the White House, the FTC and the U.S. Department of Commerce, are reviewing the need for greater regulation of the collection and use of information concerning consumer behavior with respect to online services, including regulation aimed at restricting certain targeted advertising practices. The FTC in particular has approved consent decrees resolving complaints and their resulting investigations into the privacy and security practices of a number of online, social media companies. Similar actions may also impact us directly, particularly because high school students who use our Writing Tools, College Admissions, College Counseling and Scholarship Services are typically under the age of 18, which subjects our business to laws covering the protection of minors. For example, various U.S. and international laws restrict the distribution of materials considered harmful to children and impose additional restrictions on the ability of online services to collect information from minors. The FTC has also revised the rules under the Children's Online Privacy Protection Act effective July 1, 2013. Although our services are not primarily directed to children under 13, our Chegg Writing Tools, in particular, could be used by students as early as in middle school, and the FTC could decide that our site now or in the future has taken inadequate precautions to prevent children under 13 from accessing our site and providing us information.

In 2012, the White House published a report calling for a consumer privacy Bill of Rights that could impact the collection of data, and the Department of Commerce seeks to establish a consensus-driven Do-Not-Track standard that could impact on-line and mobile advertising. The State of California and several other states have adopted privacy guidelines with respect to mobile applications. Our business, including our ability to operate internationally, could be adversely affected if legislation or regulations are adopted, interpreted or implemented in a manner that is inconsistent with our current business practices and that require changes to these practices, the design of our websites, mobile applications, products, features or our privacy policy. In particular, the success of our business has been, and we expect will continue to be, driven by our ability to responsibly use the data that students share with us. Therefore, our business could be harmed by any significant change to applicable laws, regulations or industry standards or practices regarding the use or disclosure of data that students choose to share with us or regarding the manner in which the express or implied consent of consumers for such use and disclosure is obtained. Such changes may require us to modify our products and services, possibly in a material manner, and may limit our ability to develop new products and services that make use of the data that we collect about our student users.

If we become subject to liability for the Internet content that we publish or that is uploaded to our websites by students, our results of operations could be adversely affected.

As a publisher and distributor of online content, we face potential liability for negligence, copyright or trademark infringement or other claims based on the nature and content of materials that we publish or distribute. We also may face potential liability for content uploaded by students in connection with our community-related content. If we become liable, then our business may suffer. Third parties may initiate litigation against us without warning. Others may send us letters or other communications that make allegations without initiating litigation. We have in the past and may in the future receive such communications, which we assess on a case-by-case basis. We may elect not to respond to the communication if we believe it is without merit or we may attempt to resolve disputes out-of-court by removing content or services we offer or paying licensing or other fees. If we are unable to resolve such disputes, litigation may result. Litigation to defend these claims could be costly and harm our results of operations. We may not be adequately insured to cover claims of these types or indemnified for all liability that may be imposed on us. Any adverse publicity resulting from actual or potential litigation may also materially and adversely affect our reputation, which in turn could adversely affect our results of operations.

In addition, the Digital Millennium Copyright Act (DMCA) has provisions that limit, but do not necessarily eliminate, our liability for caching or hosting or for listing or linking to, content or third-party websites that include materials or other content that infringe copyrights or other intellectual property or proprietary rights, provided we comply with the strict statutory requirements of the DMCA. The interpretations of the statutory requirements of the DMCA are constantly being modified by court rulings and industry practice. Accordingly, if we fail to comply with such statutory requirements or if the interpretations of the DMCA change, we may be subject to potential liability for caching or hosting, or for listing or linking to, content or third-party websites that include materials or other content that infringe copyrights or other intellectual property or proprietary rights.

We maintain content usage review systems that, through a combination of manual and automated blocks, monitors for and makes us aware of potentially infringing content on our platform. Nevertheless, claims may continue to be brought and threatened against us for negligence, intellectual property infringement, or other theories based on the nature and content of

## Table of Contents

information, its origin and its distribution and there is no guarantee that we will be able to resolve any such claims quickly and without damage to us, our business model, our reputation or our operations. From time to time, we have been subject to copyright infringement claims, some of which we have settled. While these settlements have not had a material impact on our financial condition, we may be subject to similar lawsuits in the future, including in connection with our other services. The outcome of any such lawsuits may not be favorable to us and could have a material adverse effect on our financial condition.

Failure to protect or enforce our intellectual property and other proprietary rights could adversely affect our business and financial condition and results of operations.

We rely and expect to continue to rely on a combination of trademark, copyright, patent and trade secret protection laws, as well as confidentiality and license agreements with our employees, consultants and third parties with whom we have relationships to protect our intellectual property and proprietary rights. As of December 31, 2016, we had thirteen patents and 28 patent applications pending in the United States. We own three U.S. copyright registrations and have unregistered copyrights in our eTextbook Reader software, software documentation, marketing materials and website content that we develop. We own U.S. trademark registrations for the marks “Chegg,” “Chegg.com,” “Chegg Study,” “Chegg for Good,” “Student Hub,” “internships.com,” “ResearchReady,” “InstaEDU,” “EasyBib” and “#1 In Textbook Rentals,” among others, as well twenty foreign registrations. As of December 31, 2016, we owned over 600 registered domain names. We also have a number of pending trademark applications in the United States and foreign jurisdictions and unregistered marks that we use to promote our brand. From time to time we expect to file additional patent, copyright and trademark applications in the United States and abroad. Nevertheless, these applications may not be approved or otherwise provide the full protection we seek. Third parties may challenge any patents, copyrights, trademarks and other intellectual property and proprietary rights owned or held by us. Third parties may knowingly or unknowingly infringe, misappropriate or otherwise violate our patents, copyrights, trademarks and other proprietary rights and we may not be able to prevent infringement, misappropriation or other violation without substantial expense to us.

Furthermore, we cannot guarantee that:

- our intellectual property and proprietary rights will provide competitive advantages to us;
- our competitors or others will not design around our intellectual property or proprietary rights;
- our ability to assert our intellectual property or proprietary rights against potential competitors or to settle current or future disputes will not be limited by our agreements with third parties;
- our intellectual property and proprietary rights will be enforced in jurisdictions where competition may be intense or where legal protection may be weak;
- any of the patents, trademarks, copyrights, trade secrets or other intellectual property or proprietary rights that we presently employ in our business will not lapse or be invalidated, circumvented, challenged or abandoned; or
- we will not lose the ability to assert our intellectual property or proprietary rights against or to license our intellectual property or proprietary rights to others and collect royalties or other payments.

If we pursue litigation to assert our intellectual property or proprietary rights, an adverse decision in any of these legal actions could limit our ability to assert our intellectual property or proprietary rights, limit the value of our intellectual property or proprietary rights or otherwise negatively impact our business, financial condition and results of operations. If the protection of our intellectual property and proprietary rights is inadequate to prevent use or misappropriation by third parties, the value of our brand and other intangible assets may be diminished, competitors may be able to more effectively mimic our service and methods of operations, the perception of our business and service to customers and potential customers may become confused in the marketplace and our ability to attract

customers may be adversely affected.

We are a party to a number of third-party intellectual property license agreements. For example, we have entered into agreements with textbook publishers that provide access to textbook solutions content or questions for our Chegg Study service, for which we often pay an upfront license fee. In addition, we have agreements with certain eTextbook publishers under which we incur non-refundable fees at the time we provide students access to an eTextbook. We cannot guarantee that the third-party intellectual property we license will not be licensed to our competitors or others in our industry. In the future, we may need to obtain additional licenses or renew existing license agreements. We are unable to predict whether these license agreements can be obtained or renewed on acceptable terms, or at all. Any failure to obtain or renew such third-party intellectual property license agreements on commercially competitive terms could adversely affect our business and financial results.

## Table of Contents

We are, and may in the future be, subject to intellectual property claims, which are costly to defend and could harm our business, financial condition and operating results.

From time to time, third parties have alleged and are likely to allege in the future that we or our business infringes, misappropriates or otherwise violates their intellectual property or proprietary rights. Many companies, including various “non-practicing entities” or “patent trolls,” are devoting significant resources to developing or acquiring patents that could potentially affect many aspects of our business. There are numerous patents that broadly claim means and methods of conducting business on the Internet. We have not exhaustively searched patents related to our technology. In addition, the publishing industry has been, and we expect in the future will continue to be, the target of counterfeiting and piracy. We have in the past and may continue to receive communications alleging that physical textbooks sold or rented by us are counterfeit. For example, we recently cooperated, and continue to cooperate, with a group of publishers in a series of audits which have identified several thousand potentially fraudulent textbooks which we have removed from our inventory. While our fulfillment partner, Ingram, has a system for inspecting the physical textbooks in our catalog of books, many of the books sold or rented to students are shipped directly from our suppliers, and, despite this inspection, unauthorized or counterfeit textbooks may inadvertently be included in the catalog of books we offer and may be subsequently sold or rented by us to students, or purchased by us through our buyback program, including on behalf of other buyers participating in our buyback program, and we may be subject to allegations of civil or criminal liability. We may implement measures in an effort to protect against these potential liabilities that could require us to spend substantial resources. Any costs incurred as a result of liability or asserted liability relating to sales of unauthorized or counterfeit textbooks could harm our business, reputation and financial condition.

Third parties may initiate litigation against us without warning. Others may send us letters or other communications that make allegations without initiating litigation. We have in the past and may in the future receive such communications, which we assess on a case-by-case basis. We may elect not to respond to the communication if we believe it is without merit or we may attempt to resolve disputes out-of-court by electing to pay royalties or other fees for licenses. If we are forced to defend ourselves against intellectual property claims, whether they are with or without merit or are determined in our favor, we may face costly litigation, diversion of technical and management personnel, inability to use our current website or inability to market our service or merchandise our products. As a result of a dispute, we may have to develop non-infringing technology, enter into licensing agreements, adjust our merchandising or marketing activities or take other action to resolve the claims. These actions, if required, may be unavailable on terms acceptable to us or may be costly or unavailable. If we are unable to obtain sufficient rights or develop non-infringing intellectual property or otherwise alter our business practices, as appropriate, on a timely basis, our reputation or brand, our business and our competitive position may be affected adversely and we may be subject to an injunction or be required to pay or incur substantial damages and/or fees.

In addition, we use open source software in connection with certain of our products and services. Companies that incorporate open source software into their products have, from time to time, faced claims challenging the ownership of open source software and/or compliance with open source license terms. As a result, we could be subject to suits by parties claiming ownership of what we believe to be open source software or noncompliance with open source licensing terms. Some open source software licenses require users who distribute or use open source software as part of their software to publicly disclose all or part of the source code to such software and/or make available any derivative works of the open source code on unfavorable terms or at no cost. Any requirement to disclose our proprietary source code or pay damages for breach of contract could have a material adverse effect on our business, financial condition and results of operations.

Confidentiality agreements with employees and others may not adequately prevent disclosure of trade secrets and proprietary information.

We have devoted substantial resources to the development of our intellectual property and proprietary rights. In order to protect our intellectual property and proprietary rights, we rely in part on confidentiality agreements with our employees, book vendors, licensees, independent contractors and other advisors. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. In addition, others may independently discover trade secrets and proprietary information and in such cases we could not assert any trade secret rights against such parties. Costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights and failure to obtain or maintain trade secret protection could adversely affect our competitive business position.

Table of Contents

If we are unable to protect our domain names, our reputation and brand could be adversely affected.

As of December 31, 2016, we owned over 600 registered domain names relating to our brand, including Chegg.com. Failure to protect our domain names could affect adversely our reputation and brand and make it more difficult for students to find our website, our content and our services. The acquisition and maintenance of domain names generally are regulated by governmental agencies and their designees. The regulation of domain names in the United States may change in the near future. Governing bodies may establish additional top-level domains, appoint additional domain name registrars or modify the requirements for holding domain names. As a result, we may be unable to acquire or maintain relevant domain names. Furthermore, the relationship between regulations governing domain names and laws protecting trademarks and similar intellectual property and proprietary rights is unclear. We may be unable to prevent third parties from acquiring and using domain names that are similar to, infringe upon or otherwise decrease the value of our brand name, trademarks or other intellectual property or proprietary rights.

Our wide variety of accepted payment methods subjects us to third-party payment processing-related risks.

We accept payments from students using a variety of methods, including credit cards, debit cards and PayPal. As we offer new payment options to students, we may be subject to additional regulations, compliance requirements and incidents of fraud. For certain payment methods, including credit and debit cards, we pay interchange and other fees, which may increase over time and raise our operating costs and lower our profit margins. For example, we have in the past experienced higher transaction fees from our third-party processors as a result of chargebacks on credit card transactions.

We rely on third parties to provide payment processing services, including the processing and information storage of credit cards and debit cards. If these companies become unwilling or unable to provide these services to us, our business could be disrupted. We are also subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, we may be subject to additional fines and higher transaction fees and lose our ability to accept credit and debit card payments from our students, process electronic funds transfers or facilitate other types of online payments, and our business and operating results could be adversely affected.

Worsening or stagnant economic conditions and their effect on funding levels of colleges, spending behavior by students and advertising budgets, may adversely affect our operating results and financial condition.

Our business is dependent on, among other factors, general economic conditions, which affect college funding, student spending and brand advertising. The economic downturn and slow economic recovery over the last several years has resulted in reductions in both state and federal funding levels at colleges across the United States, which has led to increased tuition and decreased amounts of financial aid offered to students. To the extent that the economy continues to stagnate or worsens, students may reduce the amount they spend on textbooks and other educational content, which could have a serious adverse impact on our business. In addition to decreased spending by students, the colleges and brands that use our marketing services have advertising budgets that are often constrained during periods of stagnant or deteriorating economic conditions. In a difficult economic environment, customer spending in each of our products and services is likely to decrease, which could adversely affect our operating results and financial condition. A deterioration of the current economic environment may also have a material adverse effect on our ability to fund our growth and strategic business initiatives.

Our international operations are subject to increased challenges and risks.



We have employees in Germany, Israel, India and the People's Republic of China (China), we indirectly contract with individuals in the Ukraine and we own a minority stake in a learning platform for high school and college students in Brazil. Although today our international operations represent approximately 5% of our total consolidated operating expenses and we currently do not expect our international operations to materially increase in the near future, we expect to continue to expand our international operations and such operations may expand more quickly than we currently anticipate. However, we have limited operating history as a company outside the United States and our ability to manage our business and conduct our operations internationally requires considerable management attention and resources and is subject to the particular challenges of supporting a rapidly growing business in an environment of multiple languages, cultures, customs, tax systems, legal systems, alternative dispute systems, regulatory systems and commercial infrastructures. Operating internationally has required and will continue to require us to invest significant funds and other resources, subjects us to new risks and may increase the risks that we currently face, including risks associated with:

recruiting and retaining talented and capable employees in foreign countries and maintaining our company culture across all of our offices;

Table of Contents

• compliance with applicable foreign laws and regulations;  
• compliance with anti-bribery laws including, without limitation, compliance with the Foreign Corrupt Practices Act;  
• currency exchange rate fluctuations;  
• political and economic instability; and  
• higher costs of doing business internationally.

As part of our business strategy, we may make our products and services available in more countries outside of the U.S. market, where we are currently focused. The markets in which we may undertake international expansion may have educational systems, technology and online industries that are different or less well developed than those in the United States, and if we are unable to address the challenges of operating in international markets, it could have an adverse effect on our results of operations and financial condition.

Colleges and certain governments may restrict access to the Internet or our website, which could lead to the loss of or slowing of growth in our student user base and their level of engagement with our platform.

The growth of our business and our brand depends on the ability of students to access the Internet and the products and services available on our website. Colleges that provide students with access to the Internet either through physical computer terminals on campus or through wired or wireless access points on campus could block or restrict access to our website, content or services or the Internet generally for a number of reasons including security or confidentiality concerns, regulatory reasons, such as compliance with the Family Educational Rights and Privacy Act, which restricts the disclosure of student information or concerns that certain of our products and services, such as Chegg Study, may contradict or violate their policies.

We depend in part on colleges to provide their students with access to the Internet. If colleges modify their policies in ways that are detrimental to the growth of our student user base or in ways that make it harder for students to use our website, or if our competitors' are able to reach more students than us, the overall growth in our student user base would slow, student engagement would decrease and we would lose revenues. Any reduction in the number of students directed to our website would harm our business and operating results.

In addition to our U.S. operations, we currently offer our college and university matching service in China. The Chinese government may seek to restrict access to the Internet or to our website specifically and our content and services could be suspended, blocked (in whole or in part) or otherwise adversely impacted in China. Any restrictions on the use of our website by students could lead to the loss or slowing of growth in the number of students who use our platform or the level of student engagement.

Our operations are susceptible to earthquakes, floods, rolling blackouts and other types of power loss. If these or other natural or man-made disasters were to occur, our operations and operating results would be adversely affected.

Our business and operations could be materially adversely affected in the event of earthquakes, blackouts or other power losses, floods, fires, telecommunications failures, break-ins, acts of terrorism, inclement weather, shelving accidents or similar events. Our executive offices are located in the San Francisco Bay Area, an earthquake-sensitive area. If floods, fire, inclement weather including extreme rain, wind, heat or cold or accidents due to human error were to occur and cause damage to a warehouse of Ingram or its textbook library, Ingram's ability to fulfill orders for textbook rental and sales transactions could be materially and adversely affected and our results of operations would suffer, especially if such events were to occur during peak periods. We may not be able to effectively shift our operations due to disruptions arising from the occurrence of such events, and our business could be affected adversely as a result. Moreover, damage to or total destruction of our executive offices resulting from earthquakes may not be covered in whole or in part by any insurance we may have.

If we are unable to implement and maintain effective internal control over financial reporting in the future, the accuracy, and timeliness of our financial reporting may be adversely affected.

The Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act) requires, among other things, that we assess the effectiveness of our internal control over financial reporting annually and the effectiveness of our disclosure controls and procedures quarterly. If we are not able to comply with the requirements of the Sarbanes-Oxley Act in a timely manner, the market price of our stock could decline and we could be subject to sanctions or investigations by the New York Stock Exchange, the SEC or other regulatory authorities, which would require additional financial and management resources.

If we conclude in future periods that our internal control over financial reporting is not effective, we may be required to expend significant time and resources to correct the deficiency and could be subject to one or more investigations or enforcement actions by state or federal regulatory agencies, stockholder lawsuits or other adverse actions requiring us to incur defense costs,

## Table of Contents

pay fines, settlements or judgments and causing investor perceptions to be adversely affected and potentially resulting in a decline in the market price of our stock.

In addition, we are an “emerging growth company” as defined in the Jumpstart Our Business Startups Act of 2012 (JOBS Act), and as such we have elected to avail ourselves of the exemption from the requirement that our independent registered public accounting firm audit our internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act until we cease to be an “emerging growth company.” See “—We are an “emerging growth company,” and we cannot be certain if the reduced disclosure requirements applicable to “emerging growth companies” will make our common stock less attractive to investors.” for additional risks relating to our “emerging growth company” status.

If we are unable to maintain effective internal control over financial reporting to meet the demands placed upon us as a public company, including the requirements of the Sarbanes-Oxley Act, we may be unable to accurately report our financial results, or report them within the timeframes required by law or exchange regulations.

We may be subject to greater than anticipated liabilities for income, property, sales and other taxes, and any successful action by federal, state, foreign or other authorities to collect additional taxes could adversely harm our business.

We are subject to regular review and audit by both U.S. federal and state and foreign tax authorities and such jurisdictions may assess additional taxes against us. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different from our historical tax provisions and accruals and could have a negative effect on our financial position and results of operations. For example, we appealed the Kentucky Tax Authority’s property tax assessment on our textbook library located in our Kentucky warehouse and the Commonwealth of Kentucky issued a ruling in favor of the Kentucky Department of Revenue in January 2014, which was reversed in our appeal to the Franklin Circuit Court in Kentucky in October 2014 before the Kentucky Court of Appeals ruled unanimously in our favor in March 2016. The Kentucky Department of Revenue petitioned the Kentucky Supreme Court for discretionary review, which was denied in September 2016. The case was determined in our favor with no property tax due related to our textbook library (see discussion above under Part I, Item 3, “Legal Proceedings”). In addition, the taxing authorities of the jurisdictions in which we operate may challenge our methodologies for valuing and allocating income from our intercompany transactions, which could increase our worldwide effective income tax rate. For example, we have been and are currently under tax audit in India for the 2014-15 fiscal year. Further, we file sales tax returns in a number of states within the United States as required by law and collect and remit sales tax for some content owners. We do not collect sales or other similar taxes in some U.S. and foreign jurisdictions, with respect to some of our sale, rental or service transactions because we believe that they do not apply to the relevant transactions. However, these and other tax laws and regulations are ambiguous or their application to our business is uncertain and the interpretation of them may be subject to change. In addition, one or more states could seek to impose new or additional sales, use or similar tax collection and record-keeping obligations on us. Any successful action by federal, state, foreign or other authorities to impose or collect additional income or property taxes, or compel us to collect and remit sales, use or similar taxes, either retroactively, prospectively or both, could harm our business, financial position and results of operations.

We may not be able to utilize a significant portion of our net operating loss or tax credit carryforwards, which could adversely affect our profitability.

At December 31, 2016, we had federal and state net operating loss carryforwards due to prior period losses of approximately \$200.7 million and \$151.5 million, respectively, which if not utilized will begin to expire in 2028 and 2017 for federal and state purposes, respectively. A portion of the state net operating loss carryforwards expired in 2016. At December 31, 2016, we also had federal tax credit carryforwards of approximately \$3.5 million, which if not utilized will begin to expire in 2030, and state tax credit carryforwards of approximately \$4.3 million, which do not expire. These net operating loss and tax credit carryforwards could expire unused and be unavailable to

offset future income tax liabilities, which could adversely affect our profitability. For example, we have net operating loss carryforwards of \$22.0 million related to our previous operations in Kentucky which will expire unused unless we have similar operations in Kentucky.

In addition, under Section 382 of the Internal Revenue Code of 1986, as amended (the Code), our ability to utilize net operating loss carryforwards or other tax attributes, such as tax credits, in any taxable year may be limited if we experience an “ownership change.” A Section 382 “ownership change” generally occurs if one or more stockholders or groups of stockholders who own at least 5% of our stock increase their ownership by more than 50 percentage points over their lowest ownership percentage within a rolling three-year period. Similar rules may apply under state tax laws. As a result of prior equity issuances and other transactions in our stock, we have previously experienced “ownership changes” under Section 382 of the Code and comparable state tax laws. We may experience ownership changes in the future as a result of future issuances and other

## Table of Contents

transactions of our stock. It is possible that any future ownership change could have a material effect on the use of our net operating loss carryforwards or other tax attributes, which could adversely affect our profitability.

Our failure to comply with the terms of our revolving line of credit could have a material adverse effect on us.

We have a revolving line of credit pursuant to a credit facility with Wells Fargo Bank, National Association (Bank) that provides an aggregate principal amount of \$30.0 million with an accordion feature that, subject to the Bank's discretion, allows us to borrow up to a total of \$50.0 million (the Line of Credit). The Line of Credit expires in September 2019. We currently have no amount drawn down under our Line of Credit. Our personal property secures the Line of Credit. If we default on our credit obligations, the Bank may, among other things, require immediate repayment of amounts drawn on the Line of Credit or terminate the Line of Credit or may foreclose on our personal property that secures the Line of Credit.

The agreements governing our indebtedness contain various covenants, including those that restrict our ability to, among other things:

- borrow money and guarantee or provide other support for indebtedness of third-parties;
- pay dividends on, redeem or repurchase our capital stock;
- acquire entities or assets;
- make investments in entities that we do not control, including joint ventures;
- consummate a merger, consolidation or sale of all or substantially all of our assets;
- enter into certain asset sale transactions; and
- enter into secured financing arrangements;

These covenants may limit our ability to effectively operate our businesses. Any failure to comply with the restrictions of any agreement governing our other indebtedness may result in an event of default under those agreements.

### Risks Related to Ownership of Our Common Stock

Our stock price has been and will likely continue to be volatile.

The trading price of our common stock has been, and is likely to continue to be, volatile. Since shares of our common stock were sold in our IPO in November 2013 at a price of \$12.50 per share, our stock price has ranged from \$3.15 to \$11.25 through December 31, 2016. In addition to the factors discussed in this Annual Report on Form 10-K, the trading price of our common stock may fluctuate significantly in response to numerous factors, many of which are beyond our control, including:

- actual or anticipated fluctuations in our financial condition and operating results, including as a result of the seasonality in our business that results from the academic calendar;
- our announcement of actual results for a fiscal period that are higher or lower than projected results or our announcement of revenues or earnings guidance that is higher or lower than expected, including as a result of difficulty forecasting seasonal variations in our financial condition and operating results or the revenues generated by our offerings;
- issuance of new or updated research or reports by securities analysts, including the publication of unfavorable reports or change in recommendation or downgrading of our common stock;
- announcements by us or our competitors of significant products or features, technical innovations, acquisitions, strategic relationships and partnerships, joint ventures or capital commitments;
- actual or anticipated changes in our growth rate relative to our competitors;

changes in the economic performance or market valuations of companies perceived by investors to be comparable to us;  
additional shares of our common stock being sold into the market by us or our existing stockholders or the anticipation of such sales;  
issuances of additional shares of our common stock in connection with acquisitions;  
share price and volume fluctuations attributable to inconsistent trading volume levels of our shares;  
lawsuits threatened or filed against us;  
regulatory developments in our target markets affecting us, students, colleges or brands, publishers or our competitors;  
political climate in the United States, with a focus on cutting or limiting budgets, higher education and taxation;  
terrorist attacks or natural disasters or other such events impacting countries where we have operations;  
international stock market conditions; and

## Table of Contents

general economic and market conditions, such as recessions, unemployment rates, the limited availability of consumer credit, interest rate changes and currency fluctuations.

Furthermore, both domestic and international stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of companies in general and technology companies in particular. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. We believe our stock price may be particularly susceptible to volatility as the stock prices of technology and Internet companies have often been subject to wide fluctuations. In the past, companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could seriously harm our business.

If securities or industry analysts do not publish research reports about our business or publish inaccurate or unfavorable research about our business, our stock price could decline.

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our common stock or publish inaccurate or unfavorable research about our business, our common stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

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

We have never declared or paid cash dividends on our capital stock. We currently intend to retain any future earnings to finance the operation and expansion of our business, and we do not expect to declare or pay any dividends in the foreseeable future. As a result, our stockholders may only receive a return on their investment in our common stock if the market price of our common stock increases. In addition, our credit facility contains restrictions on our ability to pay dividends.

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

We are an "emerging growth company," as defined under the JOBS Act. For so long as we are an "emerging growth company," we may take advantage of certain exemptions from reporting requirements that are applicable to other public companies that are not "emerging growth companies" including, but not limited to, compliance with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved.

We could be an "emerging growth company" for up to five years, although we may lose such status earlier, depending on the occurrence of certain events. We will remain an "emerging growth company" until the earliest to occur of (i) the last day of the year (a) following the fifth anniversary of our initial public offering, (b) in which we have total annual gross revenues of at least \$1.0 billion or (c) in which we are deemed to be a "large accelerated filer" under the Exchange Act, which means that the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the prior June 30, and (ii) the date on which we have issued more than \$1.0 billion in non-convertible debt securities during the prior three-year period.



We cannot predict if investors will find our common stock less attractive or our company less comparable to certain other public companies because we will rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

Under the JOBS Act, “emerging growth companies” can delay adopting new or revised accounting standards issued subsequent to the enactment of the JOBS Act until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards and will be subject to the same new or revised accounting standards as other public companies that are not “emerging growth companies.”

Delaware law and provisions in our restated certificate of incorporation and restated bylaws could make a merger, tender offer or proxy contest difficult, thereby depressing the trading price of our common stock.

Our status as a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested

## Table of Contents

stockholder for a period of three years after the person becomes an interested stockholder, even if a change of control would be beneficial to our existing stockholders. In addition, our restated certificate of incorporation and restated bylaws contain provisions that may make the acquisition of our company more difficult, including the following:

our board of directors is classified into three classes of directors with staggered three-year terms and directors can only be removed from office for cause and by the approval of the holders of at least two-thirds of our outstanding common stock;

subject to certain limitations, our board of directors has the sole right to set the number of directors and to fill a vacancy resulting from any cause or created by the expansion of our board of directors, which prevents stockholders from being able to fill vacancies on our board of directors;

only our board of directors is authorized to call a special meeting of stockholders;

certain litigation against us can only be brought in Delaware;

our restated certificate of incorporation authorizes undesignated preferred stock, the terms of which may be established and shares of which may be issued, without the approval of the holders of common stock;

- advance notice procedures apply for stockholders to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders;

our stockholders cannot act by written consent;

our restated bylaws can only be amended by our board of directors or by the approval of the holders of at least two-thirds of our outstanding common stock; and

certain provisions of our restated certificate of incorporation can only be amended by the approval of the holders of at least two-thirds of our outstanding common stock.

## ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

## ITEM 2. PROPERTIES

Our corporate headquarters are located in Santa Clara, California and consist of approximately 45,000 square feet of space under a lease that expires in February 2019. We have additional offices in California, Oregon and New York in the United States and internationally in India, Israel and Berlin, under leases that expire at varying times between 2017 and 2021. We believe our facilities are adequate for our current needs and for the foreseeable future; however, we will continue to seek additional space as needed to accommodate our growth. We also have an office space in Georgia, which we are subleasing, under a lease that expires in January 2021. We previously had an approximately 611,000 square foot warehouse in Shepherdsville, Kentucky, which we exited during 2015 as a result of our strategic partnership with Ingram and the lease expired in November 2016.

## ITEM 3. LEGAL PROCEEDINGS

From time to time, third parties may assert patent infringement claims against us in the form of letters, litigation or other forms of communication. In addition, we may from time to time be subject to other legal proceedings and claims in the ordinary course of business, including claims of alleged infringement of trademarks, copyrights and other intellectual property rights; employment claims; and general contract or other claims. We may also, from time to time be subject to various legal or government claims, disputes, or investigations. Such matters may include, but not be limited to, claims, disputes or investigations related to warranty, refund, breach of contract, employment, intellectual property, government regulation or compliance or other matters.

In July 2010, the Kentucky Tax Authority issued a property tax assessment of approximately \$1.0 million related to our textbook library located in our Kentucky warehouse for the 2009 and 2010 tax years under audit. In March 2011,

we filed a protest with the Kentucky Board of Tax Appeals that was rejected in March 2012. In September 2012, we filed a complaint seeking declaratory rights against the Commonwealth of Kentucky in the Bullitt Circuit Court of Kentucky, and that case was subsequently dismissed in favor of administration remedies with the Kentucky Tax Authority. We received a final Notice of Tax due in October 2012 from the Kentucky Tax Authority, and we appealed this notice in November 2012 with the Kentucky Board of Tax Appeals. In May 2013, we presented an Offer in Judgment to the Kentucky Tax Authority of approximately \$150,000, excluding tax and penalties, an amount that we have accrued for the two years under audit. We accrued this amount as of December 31, 2012. We appealed to the Kentucky Board of Tax Appeals in July 2013, and the Board issued a ruling in favor of the Kentucky Department of Revenue in January 2014 maintaining the property tax assessment. In February 2014, we filed an appeal to the Franklin Circuit Court in Kentucky, and in June 2014 the Circuit Court held in abeyance our motion to appeal. In October 2014 the Franklin Circuit Court in Kentucky issued its opinion and order reversing the Board of Tax

Table of Contents

Appeal's decision, setting aside the Kentucky Department of Revenue's tax assessments against us and further vacating all penalties and interest. The Kentucky Department of Revenue has appealed the Circuit Court ruling. On March 4, 2016, the Kentucky Court of Appeals ruled unanimously in our favor, affirming our position that no property tax was owed on the textbooks. The Kentucky Department of Revenue petitioned the Kentucky Supreme Court for a discretionary review, which was denied in September 2016. The case was determined in our favor with no property tax due related to our textbook library.

We are not aware of any other pending legal matters or claims, individually or in the aggregate, that are expected to have a material adverse impact on our consolidated financial position, results of operations or cash flows. However, our analysis of whether a claim may proceed to litigation cannot be predicted with certainty, nor can the results of litigation be predicted with certainty. Nevertheless, defending any of these actions, regardless of the outcome, may be costly, time consuming, distract management personnel and have a negative effect on our business. An adverse outcome in any of these actions, including a judgment or settlement, may cause a material adverse effect on our future business, operating results and/or financial condition.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

Table of Contents

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

## Market Information

Our common stock has been listed on the New York Stock Exchange under the symbol "CHGG" since November 13, 2013.

The following table sets forth for the indicated periods the high and low closing sales prices of our common stock as reported by the New York Stock Exchange.

	High	Low
Year Ended December 31, 2016		
Fourth quarter	\$8.48	\$6.54
Third quarter	\$7.21	\$4.90
Second quarter	\$5.08	\$4.27
First quarter	\$6.56	\$3.47
Year Ended December 31, 2015		
Fourth quarter	\$7.83	\$6.73
Third quarter	\$8.74	\$7.07
Second quarter	\$8.68	\$7.27
First quarter	\$8.75	\$6.44

## Stockholders of Record

As of January 31, 2017, there were 75 stockholders of record of our common stock, and the closing price of our common stock was \$7.19 per share as reported on the New York Stock Exchange. Because many of our shares of common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders.

## Dividend Policy

We have never declared or paid any cash dividend on our common stock. We intend to retain any future earnings and do not expect to pay dividends in the foreseeable future. In addition, our credit facility contains restrictions on our ability to pay dividends.

## Stock Performance Graph

This performance graph shall not be deemed "soliciting material" or to be "filed" with the SEC for purposes of Section 18 of the Exchange Act, or otherwise subject to the liabilities under that Section, and shall not be deemed to be incorporated by reference into any filing of Chegg under the Securities Act or the Exchange Act.

The following graph shows a comparison from November 13, 2013 (the date our common stock commenced trading on the New York Stock Exchange) through December 31, 2016 of the cumulative total return for our common stock, the Standard & Poor's 500 Stock Index (S&P 500) and the Russell 2000 Index (Russell 2000). The graph assumes that \$100 was invested at the market close on November 13, 2013 in the common stock of Chegg, Inc., the S&P 500 Index and the Russell 2000 Index and data for the S&P 500 Index and the Russell 2000 Index assumes reinvestments of dividends. The stock price performance of the following graph is not necessarily indicative of future stock price

performance.

37

---

Table of Contents

## ITEM 6. SELECTED FINANCIAL DATA

The selected financial data set forth below should be read together with Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and related notes included in Part II, Item 8, “Consolidated Financial Statements and Supplementary Data” of this Annual Report on Form 10-K. Our historical results are not necessarily indicative of our results in any future period.

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands, except per share amounts)				
Consolidated Statements of Operations Data:					
Net revenues	\$254,090	\$301,373	\$304,834	\$255,575	\$213,334
Gross profit	134,489	111,524	93,849	80,515	67,665
Net loss	(42,245 )	(59,210 )	(64,758 )	(55,850 )	(49,043 )
Deemed dividend to preferred stockholders <sup>(1)</sup>	—	—	—	(102,557 )	—
Net loss attributable to common stockholders	\$(42,245 )	\$(59,210 )	\$(64,758 )	\$(158,407 )	\$(49,043 )
Net loss per share attributable to common stockholders, basic and diluted	\$(0.47 )	\$(0.68 )	\$(0.78 )	\$(7.58 )	\$(4.39 )
Weighted-average shares used to compute net loss per share attributable to common stockholders, basic and diluted	90,534	86,818	83,205	20,902	11,183

(1) The completion of our IPO resulted in certain accounting effects and cash tax payments related to the issuance of 11,667,254 shares of our common stock in the form of a deemed stock dividend to the holders of our Series D and Series E convertible preferred stock valued at approximately \$102.6 million and the share-based compensation expense associated with RSUs that we had granted prior to our IPO that vested as a result of the completion of our IPO. These RSUs vested upon satisfaction of both a time-based service component and a performance condition which occurred on March 15, 2014.

Table of Contents

	December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Consolidated Balance Sheet Data:					
Total assets	\$290,652	\$291,356	\$318,127	\$327,371	\$196,367
Deferred revenue	14,836	14,971	24,591	22,804	20,032
Debt obligations, current and non-current	—	—	—	—	19,386
Convertible preferred stock	—	—	—	—	207,201
Common stock and additional paid-in capital	593,443	560,330	516,929	479,361	63,088
Total stockholders' equity (deficit)	221,939	231,075	247,043	274,240	(86,127 )



Table of Contents

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion of our financial condition and results of operations in conjunction with our audited consolidated financial statements and the related notes included in Part II, Item 8, "Consolidated Financial Statements and Supplementary Data" of this Annual Report on Form 10-K. In addition to historical consolidated financial information, the following discussion contains forward-looking statements that reflect our plans, estimates, and beliefs. Our actual results could differ materially from those discussed in the forward-looking statements. See the "Note about Forward-Looking Statements" for additional information. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Annual Report on Form 10-K, particularly in Part I, Item 1A, "Risk Factors."

Overview

Chegg is the leading student-first connected learning platform. Our goal is to help students transition from high school to college to career, with a view to improving student outcomes. We help students study more effectively for college admission exams, find the right college to accomplish their goals, get better grades and test scores while in school, and find internships that allow them to gain valuable skills to help them enter the workforce after college. We strive to improve the overall return on investment in education by helping students learn more in less time and at a lower cost.

Students subscribe to our digital products and services, which we collectively refer to as Chegg Services. These include Chegg Study, Chegg Tutors, Writing Tools (newly acquired in May 2016), Enrollment Marketing, Brand Partnership, Internships, and Test Prep. Our Chegg Study service provides step-by-step Textbook Solutions and Expert Answers, helping students with their course work. When students need additional help on a subject, they can reach a live tutor online, anytime, anywhere through Chegg Tutors. When students need help creating citations for their papers, they can use one of our Writing Tools properties, including EasyBib, Citation Machine, BibMe, CiteThisForMe, and NormasAPA. Through our strategic partnership with NRCCUA, announced in January 2017, we match domestic and international students with colleges, in the United States, to help them find the best fit school for them. We provide access to internships to help students gain skills and experiences that are critical to securing their first job. We provide high school students with an online adaptive test preparation service currently covering the ACT and SAT exams. Through our strategic partnership with Ingram Content Group (Ingram), we offer Required Materials, which includes an extensive print textbook and eTextbook library for rent and sale, helping students save money compared to the cost of buying new.

To deliver services to students, we partner with a variety of third parties. We work with colleges to help shape their incoming classes. We source print textbooks, eTextbooks, and supplemental materials directly or indirectly from thousands of publishers in the United States, including Pearson, Cengage Learning, McGraw Hill, Wiley, and MacMillan. We have a large network of students and professionals who leverage our platform to tutor in their spare time and employers who leverage our platform to post their internships and jobs. In addition, because we have a large student user base, local and national brands partner with us to reach the college and high school demographics.

During the years ended December 31, 2016, 2015 and 2014, we generated net revenues of \$254.1 million, \$301.4 million and \$304.8 million, respectively, and in the same periods had net losses of \$42.2 million, \$59.2 million and \$64.8 million, respectively. We plan to continue to invest in our long-term growth, particularly further investment in the technology that powers our connected learning platform and the development of additional products and services that serve students.

Our strategy for achieving and maintaining profitability is centered upon our ability to utilize Chegg Services to increase student engagement with our connected learning platform. We plan to continue to invest in the expansion of

our Chegg Services to provide a more compelling and personalized solution and deepen engagement with students. In May 2016, we acquired Imagine Easy Solutions, LLC, a privately held online learning company based in New York that provides a portfolio of online writing tools. We anticipate this acquisition to enhance our ability to acquire new students, increase the value to our existing students, and have a meaningful and positive impact on their outcomes. Further, we believe this expanded and deeper penetration of the student demographic will allow us to drive further growth in our existing Chegg Services. In addition, we believe that these investments we have made to achieve our current scale will allow us to drive increased operating margins over time that, together with increased contributions of Chegg Services products, will enable us to accomplish profitability and become cash-flow positive for the long-term. Our ability to achieve these long-term objectives is subject to numerous risks and uncertainties, including our ability to attract, retain, and increasingly engage the student population, intense competition in our markets, the ability to achieve sufficient contributions to revenue from Chegg Services and other factors described in greater detail in Part I, Item 1A, “Risk Factors.”

## Table of Contents

We have presented revenues for our two product lines, Chegg Services and Required Materials, based on how students view us and the utilization of our products by them. Chegg Services includes our products and services we provide to supplement the requirements and help students with their coursework. Chegg Services also includes our marketing services which help to complete our offering of services to students. Required Materials includes all products that are essential for students to meet the requirements of their coursework. More detail on our two product lines is discussed in the next two sections titled "Chegg Services" and "Required Materials."

### Chegg Services

Our Chegg Services for students primarily includes our Chegg Study service, our Chegg Tutors service, and our writing tools service. We offer enrollment marketing services to colleges, through our strategic partnership with NRCCUA announced in January 2017, allowing them to reach interested college-bound high school students that use our College Admissions and Scholarship Services. We also work with leading brands, such as Proctor & Gamble, Starbucks, The Truth, Microsoft, Best Buy, DirectTV, Bare Escentuals, and Shutterfly, to provide students with discounts, promotions, and other products that, based on student feedback, delight them. For example, for Proctor & Gamble, we inserted free laundry care samples and for Starbucks, we inserted free drinks in our textbook rental shipments to students. All of our brand advertising services and the discounts, promotions, and other products provided to students are paid for by the brands. We additionally provide internship services and our Test Prep service currently covering the ACT and SAT exams.

Students typically pay to access Chegg Services such as Chegg Study on a monthly or annual basis, while colleges subscribe to our enrollment marketing services and brands pay us depending on the nature of the campaign. In the aggregate, Chegg Services revenues were 51%, 31% and 22% of net revenues during the years ended December 31, 2016, 2015 and 2014, respectively.

### Required Materials

Our Required Materials product line includes the rental and sale of print textbooks and eTextbooks as well as the commission we receive from Ingram. As of November 2016, we no longer rent our print textbooks and therefore all revenues from print textbook rentals from this date forward are commission-based. Our web-based, multiplatform eTextbook Reader, eTextbooks and supplemental course materials are available from approximately 120 publishers as of December 31, 2016. We offer our eTextbook Reader on a standalone basis or as a rental-equivalent solution and for free to students awaiting the arrival of their print textbook rental. This product line has historically been highly capital intensive due to the resources required to maintain a print textbook rental library. However, as a result of our strategic partnership with Ingram, we have exited our warehouse facilities in Kentucky and transitioned our print textbook library to Ingram's facilities, which has helped to free up resources historically required by this product line. We have continued to liquidate our print textbook library through the normal course of our operations and maintain a minimal print textbook rental library as of December 31, 2016. We will continue to liquidate our remaining print textbook library inventory in the first half of 2017.

We have historically capitalized the investment in our print textbook library and recorded depreciation expense in cost of revenues over its useful life using an estimated liquidation value. During the years ended December 31, 2016 and 2015, our purchases of print textbooks, net of proceeds from textbook liquidation was an inflow of \$24.8 million and \$6.0 million, respectively, and an outflow during the year ended December 31, 2014 of \$54.7 million. In the years ended December 31, 2016 and 2015, our purchases of print textbooks significantly decreased, and were more than offset by the proceeds received from liquidations of textbooks from our print textbook library. This was a result of our strategic partnership with Ingram as we are no longer purchased print textbooks for rental.

We use our website to liquidate print textbooks from our remaining print textbook library, which allows us to generate greater recovery on our print textbooks compared to bulk liquidations, while at the same time providing students substantial savings over the retail price of a new book. We also use our website to source, on behalf of Ingram, both new and used print textbooks for rental or resale from wholesalers, publishers and students. Purchasing used print textbooks attracts students to our website by offering more for their textbooks than they could generally get by selling them back to their campus bookstore.

In the aggregate, Required Materials revenues were 49%, 69%, and 78% of net revenues during the years ended December 31, 2016, 2015 and 2014, respectively.

#### Strategic Partnership with Ingram

Our strategic partnership with Ingram has helped to accelerate the growth of our Chegg Services products by allowing us to utilize capital otherwise spent on the purchase of print textbooks, and at the same time allowing us to maintain our leading

## Table of Contents

position and high brand recognition through our iconic orange boxes. We entered into a definitive inventory purchase and consignment agreement with Ingram that will allow us to focus exclusively on eTextbooks and Chegg Services. Under the agreement, since May 2015, Ingram has been responsible for all new investments in the print textbook library, fulfillment logistics, and has title and risk of loss related to print textbook rentals. As a result of our strategic partnership with Ingram, our revenues include a commission on the total revenues that we earn from Ingram upon their fulfillment of a rental transaction using print textbooks for which Ingram has title and risk of loss. Additionally, we ceased making additional investments in our print textbook library during 2015 and continue to liquidate our existing inventory of print textbooks maintaining a minimal print textbook library inventory as of December 31, 2016, which we expect to be fully liquidated in the first half of 2017. This model allows us to reduce and eventually eliminate the operating expenses we historically incurred to acquire and maintain a print textbook library. We will continue to buy used books on Ingram's behalf including books through our buyback program and invoice Ingram at cost. We provided Ingram with extended payment terms throughout 2016 as we procured print textbooks on their behalf and we moved to normal payment terms commencing in January 2017.

### Seasonality of Our Business

Historically, a substantial majority of our revenues were recognized ratably over the term a student rents our print textbooks and eTextbooks or has access to our Chegg Services. This has generally resulted in our highest revenues in the fourth quarter as it reflects more days of the academic year and our lowest revenues in the second quarter as colleges conclude their academic year for summer and there are fewer days of rentals. The recognition of revenues from our eTextbooks and Chegg Services will continue to follow these trends. As a result of our strategic partnership with Ingram, however, revenues from all print textbook transactions will now be higher in the first and third quarters as we recognize a commission on the transaction immediately rather than recognizing the revenues ratably over the term the student rents the print textbooks.

The variable expenses associated with our shipments of print textbooks and marketing activities historically were highest in the first and third quarters as shipping and other fulfillment costs and marketing expenses are expensed when incurred, generally at the beginning of academic terms. However, these variable expenses related to the shipments of print textbooks have decreased during 2016 as we have completely transitioned the shipping and fulfillment activities related to print textbooks to Ingram.

As a result of these factors, the most concentrated periods for our revenues and expenses did not necessarily coincide, and comparisons of our historical quarterly operating results on a sequential basis may not provide meaningful insight into our overall financial performance. Our strategic partnership with Ingram has shifted peak revenues in the periods that a student rents a textbook as a result of the immediate revenue recognition as well as our revenue sharing agreement such we believe our revenues will provide more meaningful insight on a sequential basis going forward. Further, while our expenses associated with the print textbook rental business have decreased, our variable expenses related to marketing activities continue to remain highest in the first and third quarter such that our profitability may not provide meaningful insight on a sequential basis.

### Components of Results of Operations

#### Net Revenues

We derive our revenues from the rental or sale of print textbooks and eTextbooks, commissions earned from Ingram from the rental of their textbooks, and Chegg Services, net of allowances for refunds or charge backs from our payment processors who process payments from credit cards, debit cards and PayPal. As of November 2016, we no longer rent our print textbooks and therefore all revenues from print textbook rentals from this date forward are commission-based.

We historically generated revenues from the rental of print textbooks and to a lesser extent, through the sales of print textbooks through our website on a just-in-time basis. Rental revenues for textbooks that we own were recognized

ratably over the term of the rental period, generally two to five months. Commissions earned on rental textbooks owned by Ingram are recognized immediately when a book ships to the student. Revenues from selling textbooks on a just-in-time basis were historically recognized upon shipment and has comprised approximately 12% of our consolidated net revenues on average over the three years ended December 31, 2016. As of December 2016, revenues from selling textbooks on a just-in-time basis are commission based as a result of the transition to Ingram. Our customers pay for the rental and sale of print textbooks on our website primarily by credit card, resulting in immediate settlement of our accounts receivable. Net revenues from the rental or sale of print textbooks represented 27%, 54% and 70% of our net revenues in the years ended December 31, 2016, 2015 and 2014, respectively, reflecting increasing growth in our Chegg Services. Similar to the revenue recognition from print textbooks rentals, revenues from eTextbooks is recognized ratably over the contractual period, generally two to five months or at time of the sale, and our customers pay for these services through payment processors, resulting in immediate settlement of our accounts receivable.

## Table of Contents

As a result of our strategic partnership with Ingram, we recognize less revenues from the rental of print textbooks and our Required Materials product line. Instead, our services revenues includes a commission on the total revenues that we earn from Ingram upon their fulfillment of a rental transaction using books for which Ingram has title and risk of loss.

We also generate revenues from Chegg Services that include our Chegg Study service, our Chegg Tutors service, our online writing tools, Enrollment Marketing services to colleges, Brand Partnership services that we offer to brands, internship services and our test preparation service currently covering the ACT and SAT exams. Chegg Services are offered to students through weekly, monthly or annual subscriptions, and we recognize revenues ratably over the respective subscription period.

When deciding the most appropriate basis for presenting revenues or costs of revenues, both the legal form and substance of the agreement between us and our business partners are reviewed to determine each party's respective role in the transaction. Where our role in a transaction is that of principal, revenues are recognized on a gross basis. This requires revenue to comprise the gross value of the transaction billed to the customer, after trade discounts, with any related expenditure charged as a cost of revenues. Where our role in a transaction is that of an agent, revenues are recognized on a net basis with revenues representing the margin earned. In relation to our partnership with Ingram and the rental of their textbooks, we recognize revenues on a net basis based on our role in the transaction as an agent.

Enrollment Marketing services and Brand Partnership services are offered either on a subscription or on an a la carte basis. Enrollment Marketing services connect colleges with students seeking admission or scholarship opportunities at these institutions. Brand Partnership offers brands unique ways to connect with students. Revenues are recognized ratably or as earned over the subscription service period, generally one year. Revenues from enrollment marketing services or brand advertising delivered on an a la carte basis, without a subscription, are recognized when delivery of the respective lead or service has occurred. For these services, we bill the customer at the inception, over the term of the customer arrangement or as the services are performed. Upon satisfactory assessment of creditworthiness, we generally grant credit to our Enrollment Marketing services and Brand Partnership customers with normal credit terms, typically 30 days.

Deferred revenue primarily consists of advance payments from students related to rentals and subscriptions that have not been recognized and marketing services that have yet to be performed. Deferred revenue is recognized as revenues ratably over the term or when the services are provided and all other revenue recognition criteria have been met.

## Cost of Revenues

Our cost of revenues consists primarily of expenses associated with the delivery and distribution of our products and services. Cost of revenues historically included textbook depreciation expense, shipping and other fulfillment costs, the cost of textbooks sold, payment processing costs, write-offs and allowances related to the print textbook library and all expenses associated with our distribution and customer service centers, including personnel and warehousing costs. These variable expenses have decreased during 2016 as we have completely transitioned the shipping and fulfillment activities related to print textbooks to Ingram. The cost of textbooks sold, shipping and other fulfillment costs and payment processing expenses are recognized upon shipment, while textbook depreciation is recognized under an accelerated method over the life of the textbook. We believe this method most accurately reflects the actual pattern of decline in the economic value of the assets, resulting in higher costs earlier in the textbook lifecycle. Changes in our cost of revenues may be disproportionate to changes in our revenues because unrecoverable costs, such as outbound shipping and other fulfillment and payment processing fees, are expensed in the period they are incurred while revenues are recognized ratably over the rental term. This effect is particularly pronounced in the first and third quarters, corresponding to the beginning of academic terms. As a result, we could experience quarters in which our cost of revenues exceeds our revenues for the period. In addition, cost of revenues includes the depreciation

of our eTextbook Reader software, publisher content fees for eTextbooks and allocated information technology and facilities costs.

Cost of revenues also consists of content amortization expense related to content that we develop or license, including publisher agreements for which we pay one-time license fees for published content, enrollment marketing services leads purchased from third-party suppliers to fulfill leads that we are unable to fulfill through our internal database, personnel costs and other direct costs related to providing content or services. In addition, cost of revenues include allocated information technology and facilities costs.

We anticipate that to the extent Chegg Services revenues grow and the execution of our strategic partnership with Ingram is successful, our gross margins will generally improve over time.



## Table of Contents

### Operating Expenses

We classify our operating expenses into five categories: technology and development, sales and marketing, general and administrative, restructuring (credits) charges and gain on liquidation of textbooks. One of the most significant components of our operating expenses is employee-related costs, which include share-based compensation expenses. We expect to continue to hire new employees in order to support our current and anticipated growth. In any particular period, the timing of additional hires could materially affect our operating expenses, both in absolute dollars and as a percentage of revenues. Our costs and expenses contain information technology expenses and facilities expenses such as webhosting, depreciation on our infrastructure systems, lease expense and the employee-related costs for information technology support staff. We allocate these costs to each expense category, including cost of revenues, technology and development, sales and marketing and general and administrative. The allocation is primarily based on the headcount in each group at the end of a period. As our business grows, our operating expenses may increase over time to expand capacity and sustain our workforce.

### Technology and Development

Our technology and development expenses consist of salaries, benefits and share-based compensation expense for employees in our product and web design, engineering and technical teams who are responsible for maintaining our website, developing new products and improving existing products. Technology and development costs also include amortization of acquired intangible assets, webhosting costs, third-party development costs, research and development expenses and allocated information technology and facilities expenses. We expense substantially all of our technology and development expenses as they are incurred. In the past three years, our expenses have increased to support new products and services as well as to expand our infrastructure capabilities to support back-end processes associated with our revenue transactions and internal systems. We intend to continue making significant investments in developing new products and services and enhancing the functionality of existing products and services.

### Sales and Marketing

Our sales and marketing expenses consist of user and advertiser-facing marketing and promotional expenditures through a number of targeted online marketing channels, sponsored search, display advertising, email marketing campaigns and other initiatives. We incur salaries, benefits and share-based compensation expenses for our employees engaged in marketing, business development and sales and sales support functions required for enrollment marketing services and amortization of acquired intangible assets and allocated information technology and facilities costs. Our marketing expenses are largely variable; and we tend to incur these in the first and third quarters of the year due to our efforts to target students at the beginning of academic terms. To the extent there is increased or decreased competition for these traffic sources, or to the extent our mix of these channels shifts, we would expect to see a corresponding change in our marketing expense. Sales and marketing expenses also include lead generation services and sales commissions for our enrollment marketing services and brand advertising.

### General and Administrative

Our general and administrative expenses consist of salaries, benefits and share-based compensation expense for certain executives as well as our finance, legal, human resources and other administrative employees. In addition, general and administrative expenses include outside consulting, legal and accounting services, provision for doubtful accounts and allocated information technology and facilities costs. We expect to incur additional costs when we transition from an “emerging growth company” including increased audit, legal, regulatory and other related fees.

### Restructuring (Credits) Charges

Restructuring (credits) charges are primarily comprised of severance costs, contract and program termination costs, asset impairments and costs of facility consolidation and closure. Restructuring charges are recorded upon approval of a formal management plan and are included in the operating results of the period in which such plan is approved and the expense becomes estimable.

#### Gain on Liquidation of Textbooks

Gain on liquidation of textbooks consists of proceeds we receive from the sale of previously rented print textbooks, through our website or to wholesalers and other channels, offset by the net book value of such textbooks. Our gain on liquidation of textbooks is driven by several factors including age of the books liquidated, the volume of books liquidated at a

Table of Contents

given point in time and the channel through which we liquidate. When the proceeds received exceed the net book value of the textbooks liquidated, we record a gain on liquidation of textbooks.

Interest Expense, Net and Other (Expense) Income, Net

Interest expense, net and other (expense) income, net consists primarily of interest expense on our debt obligations and interest income on our cash and cash equivalents and investment balances.

Provision for Income Taxes

Provision for income taxes consists primarily of federal and state income taxes in the United States and income taxes in foreign jurisdictions in which we conduct business. Due to the uncertainty as to the realization of the benefits of our domestic deferred tax assets, we have recorded a full valuation allowance against such assets. We intend to continue to maintain a full valuation allowance on our domestic deferred tax assets until there is sufficient evidence to support the reversal of all or some portion of these allowances.

Table of Contents

## Results of Operations

The following table summarizes our historical consolidated statements of operations (in thousands, except percentage of total net revenues):

	Year Ended December 31,					
	2016		2015		2014	
Net revenues:						
Rental	\$39,837	16 %	\$120,365	40 %	\$181,570	60 %
Services	181,264	71	131,996	44	87,460	29
Sales	32,989	13	49,012	16	35,804	11
Total net revenues	254,090	100	301,373	100	304,834	100
Cost of revenues <sup>(1)</sup> :						
Rental	28,637	11	98,162	32	145,760	48
Services	54,767	22	43,794	15	31,158	10
Sales	36,197	14	47,893	16	34,067	11
Total cost of revenues	119,601	47	189,849	63	210,985	69
Gross profit	134,489	53	111,524	37	93,849	31
Operating expenses <sup>(1)</sup> :						
Technology and development	66,331	26	59,391	20	49,386	16
Sales and marketing	53,949	21	64,082	21	72,315	24
General and administrative	55,372	22	45,209	15	41,837	14
Restructuring (credits) charges	(423 )	—	4,868	2	—	—
Gain on liquidation of textbooks	(670 )	—	(4,326 )	(2 )	(4,555 )	(2 )
Total operating expenses	174,559	69	169,224	56	158,983	52
Loss from operations	(40,070 )	(16 )	(57,700 )	(19 )	(65,134 )	(21 )
Total interest expense, net and other (expense) income, net	(468 )	—	(31 )	—	562	—
Loss before provision for income taxes	(40,538 )	(16 )	(57,731 )	(19 )	(64,572 )	(21 )
Provision for income taxes	1,707	(1 )	1,479	(1 )	186	—
Net loss	\$(42,245)	(17 )%	\$(59,210)	(20 )%	\$(64,758)	(21 )%

<sup>(1)</sup> Includes share-based compensation expense as follows:

Cost of revenues	\$172	\$262	\$617
Technology and development	14,771	11,992	10,451
Sales and marketing	6,124	7,901	11,300
General and administrative	20,718	18,620	14,520
Total share-based compensation expense	\$41,785	\$38,775	\$36,888

Table of Contents

Year Ended December 31, 2016, 2015 and 2014

## Net Revenues

Net revenues in the year ended December 31, 2016 decreased \$47.3 million, or 16%, compared to the same period in 2015. Rental revenues decreased \$80.5 million or 67%, while services revenues increased \$49.3 million, or 37%, and sales revenues decreased \$16.0 million, or 33%.

Net revenues in the year ended December 31, 2015 decreased \$3.5 million, or 1%, compared to the same period in 2014. Rental revenues decreased \$61.2 million or 34%, while services revenues increased \$44.5 million, or 51%, and sales revenues increased \$13.2 million, or 37%.

The decrease in rental revenues during the years ended December 31, 2016 and 2015 was due to our strategic partnership with Ingram. As a result of our strategic partnership, our rental revenues are increasingly classified as services revenues to represent the commission on the total revenues that we earn from Ingram upon their fulfillment of a rental transaction using books for which Ingram has title and risk of loss rather than recognizing rental revenues from transactions using our print textbooks. The increase in services revenues during the years ended December 31, 2016 and 2015 was driven primarily from growth across our other offerings for students which included increased revenues from Chegg Study and our various acquisitions in 2014 and 2016 as well as an increase in the commissions earned from Ingram. The decrease in sales revenues during the year ended December 31, 2016 and the increase in sales revenues during the year ended December 31, 2015 was driven by sales of print textbooks through our website on a just-in-time basis.

The following table sets forth our total net revenues for the periods shown for our Chegg Services and Required Materials product lines (dollars in thousands):

	Year Ended			Change in 2016		Change in 2015	
	December 31,			\$	%	\$	%
	2016	2015	2014				
Chegg Services	\$129,335	\$94,285	\$68,117	\$35,050	37 %	\$26,168	38 %
Required Materials	124,755	207,088	236,717	(82,333 )	(40)%	(29,629 )	(13)%
Total net revenues	\$254,090	\$301,373	\$304,834	\$(47,283)	(16)%	\$(3,461 )	(1 )%

Chegg Services revenues increased \$35.1 million, or 37%, in the year ended December 31, 2016, compared to the same period in 2015 due to growth in subscribers for our Chegg Study and Chegg Tutors services as well as revenues from our acquisition of Imagine Easy in the second quarter of 2016. Chegg Services revenues represented 51% and 31% of net revenues during the years ended December 31, 2016 and 2015, respectively. Required Materials revenues decreased \$82.3 million, or 40%, in the year ended December 31, 2016 compared to the same period in 2015 primarily due to our strategic partnership with Ingram. Our Required Materials revenues are increasingly comprised of a commission earned from Ingram rather than the full revenues from a print textbook rental transaction. Required Materials revenues decreased throughout 2016 and we fully transitioned new investments in the print textbook library and logistics and fulfillment for print textbook rental and sale orders to Ingram. Required Materials revenues represented 49% and 69% of net revenues during the years ended December 31, 2016 and 2015, respectively.

Chegg Services revenues increased \$26.2 million, or 38%, in the year ended December 31, 2015, compared to the same period in 2014 due to growth in subscriptions for our Chegg Study service. Chegg Services represented 31% and 22% of net revenues during the years ended December 31, 2015 and 2014, respectively. Required Materials revenues decreased \$29.6 million, or 13%, in the year ended December 31, 2015 compared to the same period in 2014 primarily due to our partnership with Ingram. Required Materials revenues represented 69% and 78% of net revenues during the years ended December 31, 2015 and 2014, respectively.



Table of Contents

## Cost of Revenues

The following table sets forth our cost of revenues for the periods shown (dollars in thousands):

	Year Ended December 31,			Change in 2016		Change in 2015	
	2016	2015	2014	\$	%	\$	%
Cost of revenues <sup>(1)</sup>	\$ 119,601	\$ 189,849	\$ 210,985	\$(70,248)	(37)%	\$(21,136)	(10)%

<sup>(1)</sup> Includes share-based compensation expense of:

	\$ 172	\$ 262	\$ 617	\$(90 )	(34)%	\$(355 )	(58)%
--	--------	--------	--------	---------	-------	----------	-------

Cost of revenues in the year ended December 31, 2016 decreased by \$70.2 million, or 37%, compared to the same period in 2015. The decrease in absolute dollars and as a percentage of revenues for the year ended December 31, 2016 was primarily due to a decrease in textbook depreciation of \$34.3 million, lower order fulfillment costs of \$18.3 million, lower write-offs related to our print textbook library of \$4.2 million, lower warehouse personnel costs of \$3.1 million and lower cost of print textbooks sold of \$16.4 million. These savings were partially offset by higher amortization of digital content of \$5.3 million. As a result, gross margins increased to 53% in the year ended December 31, 2016, from 37% in the year ended December 31, 2015.

Cost of revenues in the year ended December 31, 2015 decreased by \$21.1 million, or 10%, compared to the same period in 2014. The decrease in absolute dollars and as a percentage of revenues for the year ended December 31, 2015 was primarily due to a decrease in textbook depreciation of \$26.6 million, write-offs related to our print textbook library of \$5.2 million and lower warehouse personnel costs of \$5.6 million. These savings were partially offset by higher cost of print textbooks sold of \$15.5 million and higher amortization of digital content of \$1.6 million. As a result, gross margins increased to 37% in the year ended December 31, 2015, from 31% in the year ended December 31, 2014.

The decreases in cost of revenues in the year ended December 31, 2016 compared to the same period in 2015 and in the year ended December 31, 2015 compared to the same period in 2014 resulted from Ingram's fulfillment of print textbook rental orders and the closure of our warehouse in Kentucky. Further, as Ingram has taken title and risk of loss for the print textbook inventory needed to fulfill all print textbooks rentals and sales, our total cost of revenues has decreased and will continue to decrease continually improving our total gross margins.

## Operating Expenses

The following table sets forth our total operating expenses for the periods shown (dollars in thousands):

	Year Ended December 31,			Change in 2016		Change in 2015	
	2016	2015	2014	\$	%	\$	%
Technology and development <sup>(1)</sup>	\$66,331	\$59,391	\$49,386	\$6,940	12 %	\$10,005	20 %
Sales and marketing <sup>(1)</sup>	53,949	64,082	72,315	(10,133)	(16 )	(8,233 )	(11 )
General and administrative <sup>(1)</sup>	55,372	45,209	41,837	10,163	22	3,372	8
Restructuring (credits) charges	(423 )	4,868	—	(5,291 )	n/m	4,868	n/m
Gain on liquidation of textbooks	(670 )	(4,326 )	(4,555 )	3,656	(85 )	229	(5 )
Total operating expenses	\$174,559	\$169,224	\$158,983	\$5,335	3 %	\$10,241	6 %

<sup>(1)</sup> Includes share-based compensation expense of:

Edgar Filing: CHEGG, INC - Form 10-K

Technology and development	\$14,771	\$11,992	\$10,451	\$2,779	23	%	\$1,541	15	%
Sales and marketing	6,124	7,901	11,300	(1,777)	(22)	)	(3,399)	(30)	)
General and administrative	20,718	18,620	14,520	2,098	11		4,100	28	
Share-based compensation expense	\$41,613	\$38,513	\$36,271	\$3,100	8	%	\$2,242	6	%

---

n/m - not meaningful



## Table of Contents

### Technology and Development

Technology and development expenses during the year ended December 31, 2016 increased \$6.9 million, or 12%, compared to the same period in 2015. During the year ended December 31, 2016, our employee-related expenses and share-based compensation expense increased \$2.7 million and \$2.8 million, respectively, compared to the same period in 2015. In addition, web hosting and software licensing fees increased \$2.0 million compared to the year ended December 31, 2015. Technology and development as a percentage of net revenues were 26% during the year ended December 31, 2016 compared to 20% of net revenues during the year ended December 31, 2015.

Technology and development expenses during the year ended December 31, 2015 increased \$10.0 million, or 20%, compared to the same period in 2014. During the year ended December 31, 2015, our employee-related expenses and share-based compensation expense increased \$5.2 million and \$1.5 million, respectively, compared to the same period in 2014. In addition, expenses for outside services increased \$1.4 million and web hosting and software licensing fees increased \$0.9 million, compared to the year ended December 31, 2014. Technology and development as a percentage of net revenues were 20% during the year ended December 31, 2015 compared to 16% of net revenues during the year ended December 31, 2014.

### Sales and Marketing

Sales and marketing expenses during the year ended December 31, 2016 decreased by \$10.1 million, or 16%, compared to the same period in 2015. The decrease was attributable to a decrease in employee-related and share-based compensation expense that decreased \$1.5 million and \$1.8 million, respectively, compared to the years ended December 31, 2015. In addition, advertising and marketing expenses decreased \$7.4 million compared to the year ended December 31, 2015. Sales and marketing expenses as a percentage of net revenues remained flat during the year ended December 31, 2016 compared the same period in 2015.

Sales and marketing expenses during the year ended December 31, 2015 decreased by \$8.2 million, or 11%, compared to the same period in 2014. The decrease was primarily attributable to a decrease in employee-related and share-based compensation expense that decreased \$5.0 million and \$3.4 million, respectively, compared to the years ended December 31, 2014. The decrease was partially offset by advertising and marketing expenses that increased \$2.5 million compared to the year ended December 31, 2014. Sales and marketing expenses as a percentage of net revenues were 21% during the year ended December 31, 2015 compared to 24% of net revenues during the year ended December 31, 2014.

### General and Administrative

General and administrative expenses in the year ended December 31, 2016 increased \$10.2 million, or 22%, compared to the same period in 2015. The increase was due to higher employee-related expenses and share-based compensation expenses that increased \$5.3 million and \$2.1 million, respectively. In addition, the increase was driven by higher technology expenses, outside services and professional fees of \$0.9 million, \$0.7 million and \$0.9 million, respectively. General and administrative expenses as a percentage of net revenues were 22% during the year ended December 31, 2016 compared to 15% of net revenues during the year ended December 31, 2015.

General and administrative expenses in the year ended December 31, 2015 increased \$3.4 million, or 8%, compared to the same period in 2014. The increase was due to higher employee-related expenses and share-based compensation expenses that increased \$1.7 million and \$4.1 million, respectively, compared to the year ended December 31, 2014, which was partially offset by a decrease in professional fees and outside services of \$1.2 million and \$0.4 million, respectively. General and administrative expenses as a percentage of net revenues were 15% during the year ended December 31, 2015 compared to 14% of net revenues during the year ended December 31, 2014.

Restructuring (Credits) Charges

Restructuring credits of \$0.4 million recorded during the year ended December 31, 2016 were primarily related to a partial reversal of previously accrued lease termination costs due to our subtenant leasing additional space.

Restructuring charges in the year ended December 31, 2015 of \$4.9 million were related to the exit from our print coupon business and closing our Kentucky warehouse. These charges included one-time employee termination benefits for approximately 71 employees of \$1.9 million and lease termination and other costs of \$3.0 million.

Table of Contents

In connection with our strategic partnership with NRCCUA, we anticipate a \$1.1 million restructuring charge for the year ended December 31, 2017.

Costs incurred to date related to the lease termination and other costs are expected to be fully paid by 2021.

## Gain on Liquidation of Textbooks

During the years ended December 31, 2016, 2015 and 2014, we recorded a gain on liquidation of print textbooks of \$0.7 million, \$4.3 million and \$4.6 million, respectively, resulting from proceeds received from liquidation of previously rented print textbooks on our website and through various other liquidation channels.

## Interest Expense, Net and Other (Expense) Income, Net

The following table sets forth our interest expense, net, and other (expense) income, net, for the periods shown (dollars in thousands):

	Year Ended			Change in		Change in 2015	
	December 31,			2016			
	2016	2015	2014	\$	%	\$	%
Interest expense, net	\$(171)	\$(247)	\$(317)	\$76	(31)%	\$70	(22)%
Other (expense) income, net	(297)	216	879	(513)	n/m	(663)	(75)
Total interest expense, net and other (expense) income, net	\$(468)	\$(31)	\$562	\$(437)	n/m	\$(593)	(106)%

n/m - not meaningful

Interest expense, net, decreased during the year ended December 31, 2016 compared to the same period in 2015. In the year ended December 31, 2016 we replaced our previous expired credit facility with a new line of credit that carries a lower interest rate. Interest expense, net, decreased during the year ended December 31, 2015 compared to the same period in 2014. In the year ended December 31, 2015, we reduced our line of credit to \$30.0 million.

Other (expense) income, net, was a net expense during the year ended December 31, 2016 compared to a net income in the same period in 2015, primarily attributable to the accretion of the deferred cash consideration as a result of our acquisition of Imagine Easy Solutions. Other income, net, decreased during the year ended December 31, 2015 compared to the same period in 2014, primarily due to the interest earned on our investments.

## Provision for Income Taxes

The following table sets forth our provision for income taxes for the periods shown (dollars in thousands):

	Year Ended			Change in		Change in	
	December 31,			2016		2015	
	2016	2015	2014	\$	%	\$	%
Provision for income taxes	\$1,707	\$1,479	\$186	\$228	15%	\$1,293	n/m

n/m - not meaningful

We recorded an income tax provision of approximately \$1.7 million and \$1.5 million for the years ended December 31, 2016 and 2015, respectively, which was primarily due to state and foreign income tax expense and federal tax expense related to the tax amortization of acquired indefinite lived intangible assets. We recorded an income tax provision of approximately \$0.2 million in the year ended December 31, 2014 primarily the result of the release of a valuation allowance of \$1.3 million resulting from our acquisition of InstaEDU, offset by foreign and state income

taxes.

50

---

Table of Contents

## Liquidity and Capital Resources

As of December 31, 2016, our principal source of liquidity was cash totaling \$77.3 million, which was held for working capital purposes. The substantial majority of our net revenues are from e-commerce transactions with students, which are settled immediately through payment processors, as opposed to our accounts payable, which are settled based on contractual payment terms with our suppliers. We also have an aggregate principal amount of \$30.0 million available under our Line of Credit with an accordion feature that, subject to the lender's discretion, allows us to borrow up to a total of \$50.0 million. The Line of Credit expires in September 2019. As of December 31, 2016, we were in compliance with the financial covenants of the Line of Credit. Further, we had no amounts outstanding and were able to borrow up to \$30.0 million under the Line of Credit.

As a result of our strategic partnership with Ingram, we will continue to buy used print textbooks on Ingram's behalf, including print textbooks through our buyback program, and invoice Ingram at cost. We provided Ingram with extended payment terms in 2015 and 2016 for the purchase of print textbooks, before moving to normal payment terms in 2017. We have a reimbursement balance included within other current assets on our consolidated balance sheets related to the purchase of these textbooks of \$18.8 million and \$28.9 million as of December 31, 2016 and 2015, respectively. As a result of our strategic partnership with Ingram, we anticipate having significantly more working capital.

During the years ended December 31, 2016 and 2015, our proceeds from print textbook liquidations exceeded our purchases of print textbooks and resulted in a cash inflow of \$24.8 million and \$6.0 million, respectively. As a result of our strategic partnership with Ingram, we no longer make new investments in the print textbook library and since May 1, 2015, Ingram has been responsible for all new investments in the print textbook library. During the year ended December 31, 2014, our purchases of print textbooks, net of proceeds from textbook liquidations was \$54.7 million.

As of December 31, 2016, we have incurred cumulative losses of \$371.3 million from our operations and we expect to incur additional losses in the future. Our operations have been financed primarily by our IPO and cash generated from operations.

We believe that our existing sources of liquidity will be sufficient to fund our operations and debt service obligations for at least the next 12 months. Our future capital requirements will depend on many factors including our rate of revenue growth, our investments in technology and development activities, our acquisition of new products and services and our sales and marketing activities. To the extent that existing cash and cash from operations are insufficient to fund our future activities, we may need to raise additional funds through public or private equity or debt financing. Additional funds may not be available on terms favorable to us or at all. If adequate funds are not available on acceptable terms, or at all, we may be unable to adequately fund our business plans and it could have a negative effect on our business, operating cash flows and financial condition.

Most of our cash is held in the United States. As of December 31, 2016 our foreign subsidiaries held an insignificant amount of cash in foreign jurisdictions. We currently do not intend or foresee a need to repatriate these funds. In addition, based on our current and future needs, we believe our current funding and capital resources for our international operations are adequate.

The following table sets forth our cash flows (in thousands):

	Year Ended		
	December 31,		
	2016	2015	2014
Consolidated Statements of Cash Flows Data:			
Net cash provided by (used in) operating activities	\$24,938	\$(82 )	\$68,475

Edgar Filing: CHEGG, INC - Form 10-K

Net cash (used in) provided by investing activities	\$(5,963 )	\$8,271	\$(87,350)
Net cash (used in) provided by financing activities	\$(8,675 )	\$2,723	\$(1,872 )

Cash Flows from Operating Activities

Although we incurred net losses during the years ended December 31, 2016, 2015 and 2014, our net losses were fully or partially offset by non-cash expenditures such as print textbook library depreciation expense, other depreciation and amortization expense and share-based compensation expense.

Net cash provided by operating activities during the year ended December 31, 2016 was \$24.9 million. Our net loss of \$42.2 million was offset by significant non-cash operating expenses, including print textbook library depreciation expense of

51

---

## Table of Contents

\$9.3 million, other depreciation and amortization expense of \$14.6 million, share-based compensation expense of \$41.8 million and loss from write-offs of print textbooks of \$1.1 million.

Net cash used in operating activities during the year ended December 31, 2015 was \$0.1 million. Our net loss of \$59.2 million was increased by the change in our prepaid expenses and other current assets of \$27.9 million and partially offset by significant non-cash operating expenses, including print textbook library depreciation expense of \$43.6 million, other depreciation and amortization expense of \$11.7 million, share-based compensation expense of \$38.8 million and loss from write-offs of print textbooks of \$5.3 million. During the year ended December 31, 2015, we saw a decline in our textbook depreciation expense and an increase in the change of our prepaid expenses and other current assets, which was a result of our strategic partnership with Ingram, where we are no longer making investments in our print textbook library yet continue to buy books on Ingram's behalf, while providing them with extended payment terms. The effects of these two items were the primary reasons we had net cash used in operating activities for the year ended December 31, 2015.

Net cash provided by operating activities during the year ended December 31, 2014 was \$68.5 million. Although we incurred a net loss of \$64.8 million, our net loss was more than offset by significant non-cash operating expenses, including print textbook library depreciation expense of \$70.1 million, other depreciation and amortization expense of \$11.3 million, share-based compensation expense of \$36.9 million and loss from write-offs of print textbooks of \$10.5 million.

### Cash Flows from Investing Activities

Cash flows from investing activities have been primarily related to the purchase of print textbooks, marketable securities, acquisition of businesses, and property and equipment, offset by proceeds from the sale and maturity of marketable securities and the proceeds from the liquidation of print textbooks.

Net cash used in investing activities during the year ended December 31, 2016 was \$6.0 million and was primarily used for the purchases of marketable securities of \$7.6 million, purchases of property and equipment of \$24.7 million, acquisition of businesses of \$27.1 million, and the purchase of a strategic equity investment in a third party of \$1.0 million, partially offset by proceeds from the sale or maturity of marketable securities of \$29.7 million and proceeds from the liquidation of print textbooks of \$25.6 million.

Net cash provided by investing activities during the year ended December 31, 2015 was \$8.3 million and was primarily used for the purchases of print textbooks of \$32.3 million, purchases of marketable securities of \$35.6 million, purchases of property and equipment of \$8.3 million, and the purchase of a strategic equity investment in a third party of \$2.0 million, partially offset by proceeds from the sale or maturity of marketable securities of \$48.2 million and proceeds from the liquidation of print textbooks of \$38.3 million.

Net cash used in investing activities during the year ended December 31, 2014 was \$87.4 million and was primarily used for the acquisition of businesses of \$53.9 million, purchases of print textbooks of \$112.8 million, purchases of marketable securities of \$70.7 million and purchases of property and equipment of \$5.1 million, partially offset by proceeds from the sale or maturity of marketable securities of \$97.1 million and proceeds from the liquidation of print textbooks of \$58.1 million.

### Cash Flows from Financing Activities

Net cash used in financing activities during the year ended December 31, 2016 was \$8.7 million and was related to the payment of \$10.8 million in taxes related to the net share settlement of restricted stock units (RSUs) which became fully vested during the period partially offset by the proceeds from the issuance of common stock under stock plans

totaling \$2.1 million.

Net cash provided by financing activities during the year ended December 31, 2015 was \$2.7 million and was related to the proceeds from the issuance of common stock under stock plans totaling \$13.7 million partially offset by the payment of \$8.7 million in taxes related to the net share settlement of RSUs which became fully vested during the period, as well as the repurchase of common stock of \$2.3 million associated with a put option granted in connection with a prior acquisition.

Net cash used in financing activities during the year ended December 31, 2014 was \$1.9 million and was related to the payment of \$4.0 million in taxes related to the net share settlement of RSUs which became fully vested during the period offset by the issuance of common stock under stock plans totaling \$2.7 million, as well as the repurchase of common stock of \$0.6 million associated with a put option granted in connection with a prior acquisition.



Table of Contents

## Contractual Obligations and Other Commitments

The following is a summary of the contractual commitments associated with our lease obligations as of December 31, 2016 (in thousands):

	Less than		More than		
	Total	1 Year	1-3 Years	3-5 Years	5 Years
Purchase obligations	\$15,600	\$5,000	\$10,600	\$—	\$—
Operating lease obligations <sup>(1)</sup>	6,231	2,001	3,026	1,066	138
Total contractual obligations	\$21,831	\$7,001	\$13,626	\$1,066	\$138

(1) Our offices are leased under operating leases, which expire at various dates through 2021.

In addition, our other liabilities include \$2.1 million related to uncertain tax positions as of December 31, 2016. The timing of the resolution of these positions is uncertain and we are unable to make a reasonably reliable estimate of the timing of payments in individual years beyond one year. As a result, this amount is not included in the above table.

## Off-Balance Sheet Arrangements

Through December 31, 2016, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities that would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

## Critical Accounting Policies, Significant Judgments and Estimates

Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP). The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses and related disclosures. These estimates form the basis for judgments we make about the carrying values of our assets and liabilities, which are not readily apparent from other sources. We base our estimates and judgments on historical experience and on various other assumptions that we believe are reasonable under the circumstances. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, if different estimates reasonably could have been used, or if changes in the estimate that are reasonably possible could materially impact the financial statements. We believe that assumptions and estimates of the following accounting policies involve a greater degree of judgment and complexity. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our financial condition and results of operations. For further information on all of our significant accounting policies, see Note 2 of our accompanying Notes to Consolidated Financial Statements included in Part II, Item 8, "Consolidated Financial Statements and Supplementary Data" of this Annual Report on Form 10-K.

## Revenue Recognition and Deferred Revenue

We evaluate whether we are acting as a principal or an agent, and therefore whether we would record the gross sales amount and related costs as revenues or the net amount earned as commissions from the sale of third-party products.

Our determination is based on our evaluation of certain indicators including whether we are the principal in the transaction, are subject to inventory risk, have latitude in establishing prices and selecting suppliers, none of which is presumptive or determinative. Our evaluation requires management to make a judgment based on the terms of arrangement in our determination of whether we act as a principal or an agent. If our evaluation of an arrangement was incorrect, this could impact our revenue recognition and cost of revenues amount in a given period.

Some of our customer arrangements for marketing services include multiple deliverables, which include the delivery of student leads as well as other services to the end customer. We have determined these deliverables qualify as separate units of accounting, as they have value to the customer on a standalone basis and our arrangements do not contain a right of return. For

## Table of Contents

these arrangements that contain multiple deliverables, we allocate the arrangement consideration based on the relative selling price method in accordance with the selling price hierarchy, which includes: (i) vendor-specific objective evidence of fair value (VSOE), when available; (ii) third-party evidence of selling price (TPE), if VSOE does not exist; and (iii) estimated selling price (ESP), if neither VSOE nor TPE is available.

We determine VSOE based on our historical pricing and discounting practices for the specific solution when sold separately and when a substantial majority of the selling prices for these services fall within a narrow range. TPE is determined based on competitor prices for similar deliverables when sold separately. Generally our go-to-market strategy differs from that of our peers, and our offerings contain a significant level of differentiation such that the comparable pricing of services with similar functionality cannot be obtained.

As we have not established VSOE or TPE for our marketing services, we have used ESP in our allocation of arrangement consideration. We have determined ESP by considering multiple factors including, but not limited to, prices charged for similar offerings, sales volume, geographies, market conditions, the competitive landscape and pricing practices. Our determination of ESP requires management to make a judgment in which factors to consider when determining ESP. If different factors were considered we could conclude a different determination of ESP and this could have a material impact to the amount of revenues recognized. We believe the factors considered best represent the price at which we would transact a sale if the services were sold on a standalone basis, and we regularly assess the method used to determine ESP.

## Textbook Library

Factors considered in the determination of print textbook allowances impacting cost of revenues and our consolidated statements of operations include historical experience, management's knowledge of current business conditions and expectations of future demand. The consideration of these factors requires management to make judgments in the determination of our allowance for lost or damaged books in any given period.

We depreciate our print textbooks, less an estimated salvage value, over an estimated useful life of three years using an accelerated method of depreciation, as we estimate this method most accurately reflects the actual pattern of decline in the economic value of the assets as described below. The salvage value considers the historical trend and projected liquidation proceeds for textbooks. The useful life is determined based on the time period in which the textbooks are held and rented before liquidation. In accordance with our policy, we review the estimated useful lives of our textbook library on an ongoing basis.

We believe that a print textbook has more value to our customers and us early in its useful life and therefore an accelerated depreciation method reflects the actual pattern of decline in economic value and aligns with the textbook's condition, which may deteriorate over time. In addition, we consider the utilization of the textbooks and the rental revenues we can earn, recognizing that a used textbook rents for a lower amount than a new textbook. Should the actual rental activity or deterioration of books differ from our estimates, our loss (gain) on liquidation of textbooks or write-offs of textbooks could differ.

In addition, our evaluation of the appropriateness of the estimated salvage value and estimated useful life based on historical liquidation transactions with both vendors and customers and reviewing a blend of actual and estimates of the lifecycle of each book and the number of times rented before it is liquidated, respectively. Our estimates utilize data from historical experience, including actual proceeds from liquidated textbooks as a percentage of original sourcing costs, channel mix of liquidations and consideration of the estimated sales price, largely driven by the average market price data of used books and the projected values of a book in relation to the original source cost over time. Changes in the estimated salvage value, method of depreciation or useful life can have a significant impact on

our depreciation expense, write-offs liquidations and gross margins.

Depreciation expense and write-offs of print textbooks are recorded in cost of revenues in our consolidated statements of operations. During the years ended December 31, 2016, 2015 and 2014, our print textbook library depreciation expense was approximately \$9.3 million, \$43.6 million and \$70.1 million, respectively, and write-offs of print textbooks were approximately \$1.1 million, \$5.3 million and \$10.5 million, respectively.

#### Impairment of Acquired Intangible Assets and Other Long-Lived Assets

We assess the impairment of acquired intangible assets and other long-lived assets at least annually and whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Factors that we consider in determining when to perform an impairment review include significant negative industry or economic trends or significant

## Table of Contents

changes or planned changes in the use of the assets. When measuring the recoverability of these assets, we will make assumptions regarding our estimated future cash flows expected to be generated by the assets. If our estimates or related assumptions change in the future, we may be required to impair these assets. During the fourth quarter of 2014, we determined that we would not continue to support or look to expand our print coupon business, resulting in a significant decrease in the expected future cash flows. As a result an impairment analysis was performed based on a discounted cash flow analysis with key assumptions based on the future revenues expected until the services were removed from our website. The analysis indicated that the carrying amounts of the intangible assets acquired will not be fully recoverable, resulting in an impairment charge totaling \$1.6 million, which is included in sales and marketing operating expenses on our consolidated statements of operations. As of December 31, 2016 and 2015, we had intangible assets, net, of \$20.7 million and \$8.9 million, respectively.

## Goodwill

Goodwill is tested for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. In our qualitative assessment, we consider factors including economic conditions, industry and market conditions and developments, overall financial performance and other relevant entity-specific events in determining whether it is more likely than not that the fair value of our reporting unit is less than the carrying amount. Our qualitative assessment requires management to make a judgment based on the factors listed above in our determination. Should we conclude that it is more likely than not that our recorded goodwill amounts have been impaired, we would perform a two-step impairment test. The two-step impairment test requires us to perform a valuation of our goodwill. When performing the valuation of our goodwill, we make assumptions regarding our estimated future cash flows to determine the fair value of our business. If our estimates or related assumptions change in the future, we may be required to record impairment loss related to our goodwill. We have not recognized any impairment of goodwill since our inception. As of December 31, 2016 and 2015, we had goodwill of \$116.2 million and \$91.3 million, respectively.

## Indefinite Lived Intangibles

We make judgments about the recoverability of purchased indefinite-lived intangible assets whenever events or changes in circumstances indicate that an impairment may exist. We perform an annual impairment assessment on October 1 of each year for indefinite-lived intangible assets, or more frequently if indicators of potential impairment exist, to determine whether it is more likely than not that the carrying value of the assets may not be recoverable. The assumptions and estimates used to determine future values and remaining useful lives of our intangible and other long-lived assets are complex and subjective. They can be affected by various factors, including external factors such as industry and economic trends, and internal factors such as changes in our business strategy and our forecasts for specific product lines.

## Share-based Compensation

We measure and recognize share-based compensation expense for all awards made to employees, directors and consultants, including stock options, RSUs, performance-based RSUs (PSUs) and our employee stock purchase plan (ESPP) based on estimated fair values.

The fair value of stock options and shares to be purchased under our ESPP is estimated at the date of grant using the Black-Scholes-Merton option pricing model which includes assumptions for the expected term, risk-free interest rate, expected volatility and expected dividends.

The Black-Scholes-Merton option pricing model utilizes the fair value of our common stock based on an active market and requires the input of subjective assumptions, including the expected term and the price volatility of the underlying stock. These assumptions represent management's best estimates. These estimates involve inherent uncertainties and the application of management's judgment. If factors change and different assumptions are used, our share-based compensation expense could be materially different in the future. The assumptions required are estimated as follows:

**Expected term.** The expected term for options granted to employees, officers and directors is calculated as the midpoint between the vesting date and the end of the contractual term of the options. The expected term for options granted to consultants is determined using the remaining contractual life. The expected term for shares to be purchased under our ESPP is calculated as the length of the offering period which is generally six months.

**Risk-free interest rate.** The risk-free interest rate is the implied yield currently available on the United States treasury zero-coupon issues, with a remaining term equal to the expected term.

## Table of Contents

Expected volatility. The expected volatility historically was based on the average volatility of similar public entities within our peer group. Starting in the fourth quarter of 2015, we have utilized the average volatility of our share price as we now have over two years of trading history.

Expected dividends. The dividend assumption is based on our historical experience. To date we have not paid any dividends on our common stock and do not expect to pay dividends in the foreseeable future.

In addition to assumptions used in the Black-Scholes-Merton option pricing model, we must also estimate a forfeiture rate to calculate the share-based compensation expense related to our awards. Estimated forfeitures are determined based on historical data and management's expectation of exercise behaviors. We will continue to evaluate the appropriateness of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover and other factors. Quarterly changes in the estimated forfeiture rate can have a significant impact on our share-based compensation expense as the cumulative effect of adjusting the rate is recognized in the period the forfeiture estimate is changed. If a revised forfeiture rate is higher than the previously estimated forfeiture rate, an adjustment is made that will result in a decrease to the share-based compensation expense recognized in the financial statements. If a revised forfeiture rate is lower than the previously estimated forfeiture rate, an adjustment is made that will result in an increase to the share-based compensation expense recognized in the financial statements.

Share-based compensation expense recognized related to PSUs is subject to the achievement of performance objectives and requires significant judgment by management in determining the current level of attainment of such performance objectives. Management may consider factors such as the latest revenue forecasts and general business trends in the assessment of whether or not a PSU award will be obtained. Subsequent changes to these considerations may have a material impact on the amount of share-based compensation expense recognized in the period related to PSU awards, which may lead to volatility of share-based compensation expense period-to-period.

We will continue to use judgment in evaluating the assumptions related to our share-based compensation expense on a prospective basis. As we continue to accumulate additional data related to our common stock, we may refine our estimates, which could materially impact our future share-based compensation expense.

## Income Taxes

We account for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. We currently are providing a valuation allowance on domestic deferred tax assets. If or when recognizing deferred tax assets in the future, we will consider all available positive and negative evidence including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies, and results of recent operations.

We record uncertain tax positions on the basis of a two-step process in which (1) we determine whether it is more likely than not that the tax positions will be sustained on the basis of technical merits of the position and (2) for those tax positions that meet the more likely than not recognition threshold, we recognize the tax benefit as the largest amount that is cumulative more than 50 percent likely to be realized upon ultimate settlement with the related tax authority.

## Recent Accounting Pronouncements

For relevant recent accounting pronouncements, see Note 2-Significant Accounting Policies of our accompanying Notes to Consolidated Financial Statements included in Part II, Item 8, "Consolidated Financial Statements and

Supplementary Data" of this Annual Report on Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk, including changes to foreign currency exchange rates, interest rates and inflation.

Foreign Currency Exchange Risk

International revenues as a percentage of net revenues is not significant and our sales contracts are denominated primarily in U.S. dollars. A portion of our operating expenses are incurred outside the United States and are denominated in foreign currencies, which are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Chinese Renminbi and Indian Rupee. To date, we have not entered into derivatives or hedging strategies as our exposure to

56

---



Table of Contents

foreign currency exchange rates has not been material to our historical operating results. There were no significant foreign exchange gains or losses in the years ended December 31, 2016, 2015 and 2014.

Interest Rate Sensitivity

We had cash and cash equivalents totaling \$77.3 million and \$67.0 million as of December 31, 2016 and 2015, respectively. Additionally, we had investments of \$22.0 million as of December 31, 2015 which were liquidated during the year ended December 31, 2016. Our cash and cash equivalents consist of cash and money market funds. Changes in U.S. interest rates affect the interest earned on our cash and cash equivalents. A hypothetical 100 basis point increase in interest rates would not result in a material impact in the interest earned during the year ended December 31, 2016. We were not exposed to material risks to changes in market interest rates given the liquidity of the cash and money market funds in which we invested our cash.

Interest rate risk also reflects our exposure to movements in interest rates associated with our Line of Credit. The interest bearing credit facility is denominated in U.S. dollars and the interest expense is based on the LIBOR interest rate. As of December 31, 2016, we did not have an outstanding balance on our Line of Credit.

Table of Contents

ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements

	Page
<u>Report of Independent Registered Public Accounting Firm</u>	<u>59</u>
<u>Consolidated Balance Sheets</u>	<u>60</u>
<u>Consolidated Statements of Operations</u>	<u>61</u>
<u>Consolidated Statements of Comprehensive Loss</u>	<u>62</u>
<u>Consolidated Statements of Stockholders' Equity</u>	<u>63</u>
<u>Consolidated Statements of Cash Flows</u>	<u>64</u>
<u>Notes to Consolidated Financial Statements</u>	<u>65</u>

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Chegg, Inc.

We have audited the accompanying consolidated balance sheets of Chegg, Inc. as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive loss, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2016. Our audits also included the financial statement schedule listed in the Index at Item 15(2). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Chegg, Inc. at December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/S/ Ernst & Young LLP

San Jose, California  
February 22, 2017

Table of Contents

CHEGG, INC.

## CONSOLIDATED BALANCE SHEETS

(in thousands, except for number of shares and par value)

	December 31, 2016	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	\$ 77,329	\$ 67,029
Short-term investments	—	17,800
Accounts receivable, net of allowance for doubtful accounts of \$436 and \$378 at December 31, 2016 and December 31, 2015, respectively	9,206	13,157
Prepaid expenses	2,579	3,117
Other current assets	22,259	31,732
Total current assets	111,373	132,835
Long-term investments	—	4,229
Textbook library, net	2,575	29,728
Property and equipment, net	35,305	19,971
Goodwill	116,239	91,301
Intangible assets, net	20,748	8,865
Other assets	4,412	4,427
Total assets	\$ 290,652	\$ 291,356
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable	\$ 5,175	\$ 5,860
Deferred revenue	14,836	14,971
Accrued liabilities	44,319	35,280
Total current liabilities	64,330	56,111
Long-term liabilities		
Total other long-term liabilities	4,383	4,170
Total liabilities	68,713	60,281
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock, \$0.001 par value – 10,000,000 shares authorized, no shares issued and outstanding at December 31, 2016 and December 31, 2015	—	—
Common stock, \$0.001 par value – 400,000,000 shares authorized; 91,708,839 and 88,099,983 shares issued and outstanding at December 31, 2016 and December 31, 2015, respectively	92	88
Additional paid-in capital	593,351	560,242
Accumulated other comprehensive loss	(176	) (172
Accumulated deficit	(371,328	) (329,083
Total stockholders' equity	221,939	231,075
Total liabilities and stockholders' equity	\$ 290,652	\$ 291,356
See Notes to Consolidated Financial Statements.		

Table of Contents

CHEGG, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Year Ended December 31,		
	2016	2015	2014
Net revenues:			
Rental	\$39,837	\$120,365	\$181,570
Services	181,264	131,996	87,460
Sales	32,989	49,012	35,804
Total net revenues	254,090	301,373	304,834
Cost of revenues:			
Rental	28,637	98,162	145,760
Services	54,767	43,794	31,158
Sales	36,197	47,893	34,067
Total cost of revenues	119,601	189,849	210,985
Gross profit	134,489	111,524	93,849
Operating expenses:			
Technology and development	66,331	59,391	49,386
Sales and marketing	53,949	64,082	72,315
General and administrative	55,372	45,209	41,837
Restructuring (credits) charges	(423 )	4,868	—
Gain on liquidation of textbooks	(670 )	(4,326 )	(4,555 )
Total operating expenses	174,559	169,224	158,983
Loss from operations	(40,070 )	(57,700 )	(65,134 )
Interest expense, net and other (expense) income, net:			
Interest expense, net	(171 )	(247 )	(317 )
Other (expense) income, net	(297 )	216	879
Total interest expense, net and other (expense) income, net	(468 )	(31 )	562
Loss before provision for income taxes	(40,538 )	(57,731 )	(64,572 )
Provision for income taxes	1,707	1,479	186
Net loss	\$(42,245)	\$(59,210)	\$(64,758)
Net loss per share, basic and diluted	\$(0.47 )	\$(0.68 )	\$(0.78 )
Weighted average shares used to compute net loss per share, basic and diluted	90,534	86,818	83,205
See Notes to Consolidated Financial Statements.			

Table of Contents

CHEGG, INC.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands)

	Year Ended December 31,		
	2016	2015	2014
Net loss	\$ (42,245)	\$ (59,210)	\$ (64,758)
Other comprehensive loss:			
Change in unrealized gain (loss) on available for sale investments	25	(8)	2
Change in foreign currency translation adjustments, net of tax	(29)	(151)	(9)
Other comprehensive loss	(4)	(159)	(7)
Total comprehensive loss	\$ (42,249)	\$ (59,369)	\$ (64,765)

See Notes to Consolidated Financial Statements.

Table of Contents

CHEGG, INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

	Common Stock	Par Value	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity
Balances at December 31, 2013	81,708	\$ 82	\$ 479,279	\$ (6 )	\$ (205,115 )	\$ 274,240
Issuance of common stock upon exercise of stock options and ESPP	1,004	1	2,712	—	—	2,713
Net issuance of common stock for settlement of restricted stock units (RSUs)	873	1	(3,980 )	—	—	(3,979 )
Warrant exercises	104	—	—	—	—	—
Issuance of common stock in connection with acquisition	408	—	2,585	—	—	2,585
Repurchase of common stock	(89 )	—	(604 )	—	—	(604 )
Share-based compensation expense	—	—	36,853	—	—	36,853
Other comprehensive loss	—	—	—	(7 )	—	(7 )
Net loss	—	—	—	—	(64,758 )	(64,758 )
Balances at December 31, 2014	84,008	84	516,845	(13 )	(269,873 )	247,043
Issuance of common stock upon exercise of stock options and ESPP	2,165	2	13,694	—	—	13,696
Net issuance of common stock for settlement of RSUs	1,624	2	(8,712 )	—	—	(8,710 )
Warrant exercises	368	—	—	—	—	—
Issuance of common stock in connection with acquisition	125	—	825	—	—	825
Repurchase of common stock	(190 )	—	(1,185 )	—	—	(1,185 )
Share-based compensation expense	—	—	38,775	—	—	38,775
Other comprehensive loss	—	—	—	(159 )	—	(159 )
Net loss	—	—	—	—	(59,210 )	(59,210 )
Balances at December 31, 2015	88,100	88	560,242	(172 )	(329,083 )	231,075
Issuance of common stock upon exercise of stock options and ESPP	590	1	2,103	—	—	2,104
Net issuance of common stock for settlement of RSUs	3,019	3	(10,779 )	—	—	(10,776 )
Share-based compensation expense	—	—	41,785	—	—	41,785
Other comprehensive loss	—	—	—	(4 )	—	(4 )
Net loss	—	—	—	—	(42,245 )	(42,245 )
Balances at December 31, 2016	91,709	\$ 92	\$ 593,351	\$ (176 )	\$ (371,328 )	\$ 221,939

See Notes to Consolidated Financial Statements.

Table of Contents

CHEGG, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands)

	Year Ended December 31,		
	2016	2015	2014
Cash flows from operating activities			
Net loss	\$(42,245)	\$(59,210)	\$(64,758)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Textbook library depreciation expense	9,267	43,553	70,147
Amortization of warrants and deferred loan costs	105	151	187
Other depreciation and amortization expense	14,520	11,511	11,159
Share-based compensation expense	41,785	38,775	36,888
Provision (release) for bad debts	58	(77)	) 234
Gain on liquidation of textbooks	(670)	) (4,326)	) (4,555)
Loss from write-offs of textbooks	1,090	5,297	10,534
Deferred income taxes	—	—	(1,291)
Realized gain on sale of securities	(11)	) —	(21)
Loss from disposal of property and equipment	—	967	—
Impairment of intangible assets	—	—	1,552
Change in assets and liabilities net of effect of acquisition of businesses:			
Accounts receivable	(127)	) 712	(1,709)
Prepaid expenses and other current assets	10,039	(27,878)	) (2,981)
Other assets	1,437	(592)	) (155)
Accounts payable	(728)	) (4,236)	) 5,037
Deferred revenue	(272)	) (9,620)	) 1,657
Accrued liabilities	(9,499)	) 5,237	7,448
Other liabilities	189	(346)	) (898)
Net cash provided by (used in) operating activities	24,938	(82)	) 68,475
Cash flows from investing activities			
Purchases of textbooks	(886)	) (32,297)	) (112,814)
Proceeds from liquidations of textbooks	25,646	38,260	58,119
Purchases of marketable securities	(7,633)	) (35,610)	) (70,706)
Proceeds from sale of marketable securities	22,830	350	46,358
Maturities of marketable securities	6,844	47,840	50,700
Purchases of property and equipment	(24,689)	) (8,253)	) (5,083)
Acquisition of businesses, net of cash acquired	(27,055)	) —	(53,872)
Release of cash from escrow	—	—	(52)
Purchase of strategic equity investment	(1,020)	) (2,019)	) —
Net cash (used in) provided by investing activities	(5,963)	) 8,271	(87,350)
Cash flows from financing activities			
Common stock issued under stock plans, net	2,104	13,696	2,712
Payment of taxes related to the net share settlement of RSUs	(10,779)	) (8,710)	) (3,980)
Repurchase of common stock	—	(2,263)	) (604)
Net cash (used in) provided by financing activities	(8,675)	) 2,723	(1,872)
Net increase (decrease) in cash and cash equivalents	10,300	10,912	(20,747)
Cash and cash equivalents, beginning of period	67,029	56,117	76,864
Cash and cash equivalents, end of period	\$77,329	\$67,029	\$56,117



## Supplemental cash flow data:

## Cash paid during the period for:

Interest	\$50	\$95	\$114
Income taxes	\$1,094	\$827	\$625
Non-cash investing and financing activities:			
Accrued purchases of long-lived assets	\$2,333	\$1,771	\$5,132
Issuance of common stock related to prior acquisition	\$—	\$825	\$2,585
Accrued deferred cash consideration related to acquisition	\$17,378	\$—	\$—

See Notes to Consolidated Financial Statements.

Table of Contents

CHEGG, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Background and Basis of Presentation

Company and Background

Chegg, Inc. (Chegg, the Company, we, us, or our), headquartered in Santa Clara, California, was incorporated as a Delaware corporation in July 2005. Chegg is the leading student-first connected learning platform. Our goal is to help students transition from high school to college to career, with a view to improving student outcomes. We help students study more effectively for college admission exams, find the right college to accomplish their goals, get better grades and test scores while in school, and find internships that allow them to gain valuable skills to help them enter the workforce after college. Our student-first connected learning platform offers products and services that help students transition from high school to college to career.

Basis of Presentation

Our fiscal year ends on December 31 and in this report we refer to the year ended December 31, 2016, December 31, 2015, and December 31, 2014 as 2016, 2015, and 2014, respectively.

Note 2. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States (U.S. GAAP) requires management to make estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities; the disclosure of contingent liabilities at the date of the financial statements; and the reported amounts of revenues and expenses during the reporting periods. Significant estimates, assumptions, and judgments are used for, but not limited to: revenue recognition, recoverability of accounts receivable, determination of the useful lives and salvage value assigned to our textbook library, restructuring charges, share-based compensation expense including estimated forfeitures, accounting for income taxes, useful lives assigned to long-lived assets for depreciation and amortization, impairment of goodwill and long-lived assets, and the valuation of acquired intangible assets. We base our estimates on historical experience, knowledge of current business conditions, and various other factors we believe to be reasonable under the circumstances. These estimates are based on management's knowledge about current events and expectations about actions we may undertake in the future. Actual results could differ from these estimates, and such differences could be material to our financial position and results of operations.

Principles of Consolidation

The consolidated financial statements include the accounts of Chegg and our wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. The consolidated financial statements have been prepared in accordance with U.S. GAAP.

Cash and Cash Equivalents and Restricted Cash

We consider all highly liquid investments with an original maturity date of three months or less from the date of purchase to be cash equivalents. Cash and cash equivalents, which consist of cash, money market accounts, commercial paper, corporate securities and agency bonds at financial institutions, are stated at cost, which approximates fair value.

We classify certain restricted cash balances within other current assets and other assets on the accompanying consolidated balance sheets based upon the term of the remaining restrictions.

As of December 31, 2016, we had approximately \$0.1 million of restricted cash that consisted of a security deposit for our offices in Oregon and New York. As of December 31, 2015, we had approximately \$0.8 million of restricted cash that consisted of a deposit pledged as security for our corporate credit cards and a letter of credit pledged as a security deposit for our headquarters and a sales office. The deposit pledged as security for our corporate credit cards of approximately \$0.3 million as of December 31, 2015 is classified in other current assets in our consolidated balance sheets due to the short-term nature of the restriction. The amounts related to the security deposits of approximately \$0.1 million and \$0.5 million as

## Table of Contents

of December 31, 2016 and 2015, respectively, are classified in other assets in our consolidated balance sheets as these amounts are restricted for periods that exceed one year from the balance sheet dates.

### Investments

We hold investments in marketable securities, consisting of corporate securities, commercial paper and agency bonds. We classify our marketable securities as available-for-sale investments that are either short or long-term based on the nature of each security based on the contractual maturity of the investment when purchased. Our available-for-sale investments are carried at estimated fair value with any unrealized gains and losses, net of taxes, included in accumulated other comprehensive loss in stockholders' equity. Unrealized losses are charged against other (expense) income, net when a decline in fair value is determined to be other-than-temporary. We did not record any such impairment charges in the periods presented. We determined realized gains or losses on the sale of marketable securities on a specific identification method, and recorded such gains or losses as other (expense) income, net. For the years ended December 31, 2015 and 2014, the Company's gross realized gains and losses on short-term investments were not significant.

### Accounts Receivable

Accounts receivable are recorded at the invoiced amount and are non-interest bearing. We generally grant uncollateralized credit terms to our customers, which include textbook wholesalers, and marketing services customers, and maintain an allowance for doubtful accounts to account for potentially uncollectible receivables.

### Allowance for Doubtful Accounts

We assess the creditworthiness of our customers based on multiple sources of information, and analyze such factors as our historical bad debt experience, industry and geographic concentrations of credit risk, economic trends, and customer payment history. This assessment requires significant judgment. Because of this assessment, we maintain an allowance for doubtful accounts for estimated losses resulting from the inability of certain customers to make all of their required payments. In making this estimate, we analyze historical payment performance and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. Accounts receivable are written off as a decrease to the allowance for doubtful accounts when all collection efforts have been exhausted and an account is deemed uncollectible.

### Concentration of Credit Risk

Financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash and cash equivalents, restricted cash, and marketable securities invested in highly liquid instruments in accordance with our investment policy. We place the majority of our cash and cash equivalents and restricted cash with financial institutions in the United States that we believe to be of high credit quality, and accordingly minimal credit risk exists with respect to these instruments. Certain of our cash balances held with financial institutions are in excess of Federal Deposit Insurance Corporation limits. Our investment portfolio consists of investment-grade marketable securities diversified among security types, industries and issuers. Our investments were held and managed by recognized financial institutions that followed our investment policy with the main objective of preserving capital and maintaining liquidity.

Concentrations of credit risk with respect to trade receivables exist to the full extent of amounts presented in the financial statements. We had no textbook wholesalers that represented greater than 10% of our net accounts receivable balance as of December 31, 2016 and two textbook wholesalers that represented 16% and 11% of our net accounts receivable balance as of December 31, 2015, respectively. No customers represented over 10% of net revenues

in 2016, 2015 or 2014.

#### Textbook Library

We consider our print textbook library to be a long-term productive asset and, as such, classify it as a non-current asset in our consolidated balance sheets. Cash outflows for the acquisition of our print textbook library, net of changes in related accounts payable and accrued liabilities historically was classified as cash flows from investing activities in our consolidated statements of cash flows. As a result of our strategic partnership with Ingram, since May 1, 2015, Ingram has made all new investments in the print textbook library and we also provided Ingram with extended payment terms through 2016 for the purchase of textbooks, before moving to normal payment terms in January 2017. As such, we have recorded any cash outflows as a result of this partnership as an operating activity in our consolidated statements of cash flows as we are no longer purchasing print textbooks but rather providing extended payments terms to Ingram to facilitate their purchase of new textbooks. Cash inflows received from the liquidation of print textbooks are classified as cash flows from investing activities in our consolidated statements of cash flows, consistent with other long-term asset classification of our existing print textbook

66

---

Table of Contents

library. The gain or loss from the liquidation of print textbooks previously rented is recorded as a component of operating expenses in our consolidated statement of operations and is classified as cash flow from operating activities.

All print textbooks in our textbook library are stated at cost, which includes the purchase price less accumulated depreciation. We record allowances for lost or damaged print textbooks in cost of revenues in our consolidated statements of operations based on our assessment of our print textbook library on a book-by-book basis. Write-offs result from lost or damaged books, books no longer considered to be rentable, or when books are not returned to us after the rental period by our customers.

We depreciate our print textbooks, less an estimated salvage value, over an estimated useful life of three years using an accelerated method of depreciation, as we estimate this method most accurately reflects the actual pattern of decline in the economic value of the assets. The salvage value considers the historical trend and projected liquidation proceeds for print textbooks. The useful life is determined based on the time period in which the print textbooks are held and rented before liquidation. In accordance with our policy, we review the estimated useful lives of our print textbook library on an ongoing basis.

Depreciation expense and write-offs of print textbooks are recorded in cost of revenues in our consolidated statements of operations. During 2016, 2015 and 2014, print textbook depreciation expense was approximately \$9.3 million, \$43.6 million and \$70.1 million, respectively, and write-offs were approximately \$1.1 million, \$5.3 million and \$10.5 million, respectively.

#### Property and Equipment

Property and equipment are recorded at cost less accumulated depreciation and amortization. Depreciation and amortization are computed using the straight-line method over the following estimated useful lives of the assets:

Classification	Useful Life
Computers and equipment	3 years
Software	3 years
Furniture and fixtures	5 years
Leasehold improvements	Shorter of the remaining lease term or the estimated useful life of 5 years
Content	5 years

We capitalize costs related to the purchase or development of Chegg Study and Test Prep content and amortize these costs over a period of five years.

Depreciation and amortization expense are generally classified within the corresponding cost of revenues and operating expenses categories in our consolidated statements of operations. Depreciation and amortization expense during the years ended December 31, 2016, 2015 and 2014 were approximately \$9.9 million, \$6.8 million and \$6.2 million, respectively.

The cost of maintenance and repairs is expensed as incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation and amortization are removed from their respective accounts, and any gain or loss on such sale or disposal is reflected in loss from operations.

#### Software Development Costs

We capitalize costs related to software developed or obtained for internal use when certain criteria have been met. Costs incurred during the application development stage for internal-use software are capitalized in property and

equipment and amortized over the estimated useful life of the software, generally up to three years.

We had no capitalized software development costs as of December 31, 2016 or 2015. During the year ended December 31, 2016, we had no amortization of capitalized software development costs and during the years ended December 31, 2015 and 2014, the amortization of capitalized software development costs totaled approximately \$0.5 million in each year.

## Table of Contents

### Goodwill

Goodwill represents the excess of the fair value of consideration paid over the estimated fair value of assets acquired and liabilities assumed in a business acquisition. Goodwill is not amortized but rather tested for impairment at least annually on October 1, or more frequently if certain events or indicators of impairment occur between annual impairment tests. We first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. In our qualitative assessment, we consider factors including economic conditions, industry and market conditions and developments, overall financial performance and other relevant entity-specific events in determining whether it is more likely than not that the fair value of our reporting unit is less than the carrying amount. We completed our annual impairment test on October 1 of 2016 and 2015, each of which did not result in any impairment as our qualitative assessment did not indicate that it is more likely than not that the fair value of our reporting unit is less than the carrying amount.

### Acquired Intangible Assets and Other Long-Lived Assets

Acquired intangible assets with finite useful lives, which include developed technology, customer lists, trade names and non-compete agreements, are amortized over their estimated useful lives. We assess the impairment of acquired intangible assets and other long-lived assets when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable.

### Indefinite-Lived Intangibles

We make judgments about the recoverability of purchased indefinite-lived intangible assets at least annually on October 1 or more frequently whenever events or changes in circumstances indicate that an impairment may exist to determine whether it is more likely than not that the carrying value of the assets may not be recoverable. Recoverability of indefinite-lived intangible assets is measured by comparing the carrying amount of the asset to the future undiscounted cash flows that the asset is expected to generate. If we determine that an individual asset is impaired, the amount of any impairment is measured as the difference between the carrying value and the fair value of the impaired asset. We completed our annual impairment test on October 1 of 2016 and 2015, each of which did not result in any impairment.

### Revenue Recognition and Deferred Revenue

We derive our revenues, net of allowances, for refunds or charge backs from our payment processors who process payments from credit cards, debit cards and PayPal. Revenues are recognized when the four basic criteria for revenue recognition have been met as follows: persuasive evidence of an arrangement exists, delivery has occurred and title has transferred, the sale price is fixed or determinable, and collection is reasonably assured.

Revenues are presented net of sales tax collected from customers to be remitted to governmental authorities and net of allowances for estimated cancellations and customer returns, which are based on historical data. Customer refunds from cancellations and returns are recorded as a reduction to revenues.

We generate revenues from our Required Materials product line including the rental of print textbooks and eTextbooks and, to a lesser extent, through the sales of print textbooks through our website purchased by us on a just-in-time basis. Rental revenues were historically recognized ratably over the term of the rental period, generally two to five months, for the print textbooks that we owned. As of November 2016, we no longer rent our print textbooks and therefore all revenues from print textbook rentals from this date forward are commission-based.

Commission-based print textbook rental revenues are recognized immediately in the period the transaction occurs. Revenues from selling textbooks on a just-in-time basis are recognized upon shipment. We do not hold an inventory



of textbooks for sale. Our customers pay for the rental and sale of print textbooks on our website primarily by credit card, resulting in immediate settlement of our accounts receivable. Shipping costs charged to customers in the sale or rental of textbooks are recorded in revenues and the related expenses are recorded as cost of revenues.

We generate revenues from our Chegg Services product line including our Chegg Study service, our Chegg Tutors service, and our writing tools service that we offer to students. These services are offered to students through monthly or annual subscriptions and we recognize revenues ratably over the respective subscription period. Our Chegg Services also include enrollment marketing services and brand advertising, which we offer either on a subscription or on an a la carte basis. Enrollment marketing services connect colleges and graduate schools with students seeking admission or scholarship opportunities at these institutions. Brand advertising offers brands unique ways to connect with students. Finally, Chegg Services includes our internship services and our Test Prep service currently covering the ACT and SAT exams. Revenues are recognized ratably or as earned over the subscription service, generally one year. Revenues from enrollment marketing services

## Table of Contents

or brand advertising delivered on an a la carte basis, without a subscription, is recognized when delivery of the respective lead or service has occurred. For these services, we bill the customer at the inception, over the term of the customer arrangement or as the services are performed. Upon satisfactory assessment of creditworthiness, we generally grant credit to our enrollment marketing services and brand advertising customers with normal credit terms, typically 30 days.

Some of our customer arrangements for enrollment marketing services include multiple deliverables, which include the delivery of student leads as well as other services to the end customer. We have determined these deliverables qualify as separate units of accounting, as they have value to the customer on a standalone basis and our arrangements do not contain a right of return. For these arrangements that contain multiple deliverables, we allocate the arrangement consideration based on the relative selling price method in accordance with the selling price hierarchy, which includes: (1) vendor-specific objective evidence of fair value (VSOE), when available; (2) third-party evidence of selling price (TPE), if VSOE does not exist; and (3) estimated selling price (ESP), if neither VSOE nor TPE is available.

We determine VSOE based on our historical pricing and discounting practices for the specific solution when sold separately and when a substantial majority of the selling prices for these services fall within a narrow range. TPE is determined based on competitor prices for similar deliverables when sold separately. Generally our go-to-market strategy differs from that of our peers, and our offerings contain a significant level of differentiation such that the comparable pricing of services with similar functionality cannot be obtained. If we have not established VSOE or TPE for our enrollment marketing services, we have used ESP in our allocation of arrangement consideration.

Additionally, we limit the amount of revenues recognized for delivered elements to the amount that is not contingent on future delivery of services or other future performance obligations.

Deferred revenue primarily consists of advanced payments from students related to rentals and subscriptions that have not been recognized, and marketing services that have yet to be performed. Deferred revenue is recognized as revenues ratably over the term or when the services are provided and all other revenue recognition criteria have been met.

We evaluate whether we are acting as a principal or an agent, and therefore would record the gross sales amount and related costs as revenues or the net amount earned as commissions from the sale of third party products. Our determination is based on our evaluation of certain indicators including whether we are the principal in the transaction, are subject to inventory risk, have latitude in establishing prices and selecting suppliers, none of which is presumptive or determinative. We generally operate as the principal and so in those instances revenues are recorded at the gross sale price. We generally record the net amounts as commissions earned when such amounts are determined using a fixed percentage of the transaction price, we are not subject to inventory risk or responsible for the fulfillment of the textbooks. We operate as an agent in our strategic partnership with Ingram and therefore our revenues include a commission on the total revenues that we earn from Ingram upon their fulfillment of a rental transaction using books for which Ingram has title and risk of loss.

We also present our revenues separately for rental, services and sales. Rental revenue includes the rental of print textbooks for which we take title and bear the risk of loss; service revenue includes Chegg Study, Chegg Tutors, our writing tools service, enrollment marketing, brand advertising, eTextbooks, and commissions we earn from Ingram and other e-commerce partners; sale revenue includes just-in-time sale of print textbooks and the sale of other required materials.

## Cost of Revenues

Our cost of revenues consists primarily of expenses associated with the delivery and distribution of our products and services. Cost of revenues related to our print textbook rentals included print textbook depreciation expense, shipping and other fulfillment costs, the cost of textbooks sold, payment processing costs, write-offs and allowances related to the print textbook library, and all expenses associated with our distribution and customer service centers, including personnel and warehousing costs. The cost of textbooks sold, shipping and other fulfillment costs and payment processing expenses are recognized upon shipment, while print textbook depreciation is recognized under an accelerated method over the life of the textbook. We believe this method most accurately reflects the actual pattern of decline in the economic value of the assets, resulting in higher costs earlier in the textbook lifecycle. Cost of revenues also includes the depreciation of our eTextbook Reader software, publisher content fees for eTextbooks, content amortization expense related to content that we develop or license, including publisher agreements for which we pay one-time license fees for published content, enrollment marketing services leads purchased from third-party suppliers to fulfill leads that we are unable to fulfill through our internal database, personnel costs and other direct costs related to providing the content or services. In addition, cost of revenues includes allocated information technology and facilities costs.

## Table of Contents

### Technology and Development Costs

Technology and development expenses consist primarily of salaries, benefits and share-based compensation expense for employees on our product and web design, engineering and technical teams who are maintaining our website, developing new products and improving existing products. Technology and development costs also include web hosting costs, third-party development costs and allocated information technology and facilities costs. We expense substantially all of our technology and development costs as they are incurred.

### Advertising Costs

Advertising costs are expensed as incurred and consist primarily of online advertising and marketing promotional expenditures. During years ended December 31, 2016, 2015 and 2014, advertising costs were approximately \$18.4 million, \$25.0 million, and \$22.4 million, respectively.

### Share-based Compensation

Share-based compensation expense for stock options, restricted stock units (RSUs), performance-based restricted stock units (PSUs), and employee stock purchase plan (ESPP) are accounted for under the fair value method, which requires us to measure the cost of employee share-based compensation awards based on the grant-date fair value of the award. Share-based compensation expense for stock options and our ESPP is estimated at the date of grant using the Black-Scholes-Merton option pricing model while expense for RSUs and PSUs is measured based on the closing fair market value of the Company's common stock on the date of grant. We recognize compensation cost for all share-based compensation awards that are expected to vest on a straight-line basis over the requisite service period of the awards, which is generally the option vesting period. These amounts are reduced by estimated forfeitures, which are estimated at the time of the grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

Equity awards issued to non-employees are recorded at their fair value on the measurement date and are subject to adjustment each period as the underlying awards vest or consulting services are performed.

### Income Taxes

We account for income taxes under an asset and liability method whereby deferred tax asset and liability account balances are determined based on differences between the financial reporting and the tax basis of assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Valuation allowances are established, when necessary, to reduce deferred tax assets to an amount that is more likely than not to be realized. We recognize the benefit from a tax position only if it is more likely than not that the position would be sustained upon audit based solely on the technical merits of the tax position. Our policy is to include interest and penalties related to unrecognized tax benefits as a component of income tax expense.

### Restructuring Charges

Restructuring charges are primarily comprised of severance costs, contract and program termination costs, asset impairments and costs of facility consolidation and closure. Restructuring charges are recorded upon approval of a formal management plan and are included in the operating results of the period in which such plan is approved and the expense becomes estimable. To estimate restructuring charges, management utilizes assumptions of the number of employees that would be involuntarily terminated and of future costs to operate and eventually vacate duplicate facilities. Severance and other employee separation costs are accrued when it is probable that benefits will be paid and the amount is reasonably estimable. The rates used in determining severance accruals are based on our policies and

practices and negotiated settlements. Restructuring charges for employee workforce reductions are recorded upon employee notification for employees whose required continuing service period is 60 days or less and ratably over the employee's continuing service period for employees whose required continuing service period is greater than 60 days.

#### Strategic Investment

We have entered into an equity investment in a privately-held business to achieve certain strategic business objectives. Our investment in equity securities of this privately-held business is accounted for under the cost method. We periodically review this investment for other-than-temporary declines in fair value based on the specific identification method and write down investments when an other-than-temporary decline has occurred. Any fair value estimates are made based on consideration of the current cash position, recent operational performance, and forecasts of the investees.

Table of Contents

## Net Loss Per Share

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period, less the weighted-average unvested common stock subject to repurchase or forfeiture. Diluted net loss per share is computed by giving effect to all potential shares of common stock, including stock options, warrants, restricted stock units (RSUs), and performance-based restricted stock units (PSUs), to the extent dilutive. Basic and diluted net loss per share was the same for each period presented as the inclusion of all potential common shares outstanding would have been anti-dilutive.

The following table sets forth the computation of historical basic and diluted net loss per share (in thousands, except per share amounts):

	Year Ended December 31,		
	2016	2015	2014
Numerator:			
Net loss	\$(42,245)	\$(59,210)	\$(64,758)
Denominator:			
Weighted-average common shares outstanding	90,534	86,818	83,241
Less: Weighted-average unvested common shares subject to repurchase or forfeiture	—	—	(36)
Weighted average shares used to compute net loss per share, basic and diluted	90,534	86,818	83,205
Net loss per share, basic and diluted	\$(0.47)	\$(0.68)	\$(0.78)

The following potential weighted-average shares of common stock outstanding were excluded from the computation of diluted net loss per share attributable to common stockholders because including them would have been anti-dilutive (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Options to purchase common stock	10,799	11,446	14,253
RSUs and PSUs	1,239	200	289
Employee stock purchase plan	15	—	—
Warrants to purchase common stock	200	299	996
Total common stock equivalents	12,253	11,945	15,538

## Foreign Currency Translation

The functional currency of our foreign subsidiaries is the local currency. Adjustments resulting from the translation of foreign currencies into U.S. dollars for balance sheet amounts are based on the exchange rates as of the consolidated balance sheet date. Non-monetary balance sheet items denominated in a currency other than the applicable functional currency are translated using the historical rate. Revenues and expenses are translated at average exchange rates during the period. Foreign currency translation gains or losses are included in accumulated other comprehensive loss as a component of stockholders' equity on the consolidated balance sheets. Gains or losses resulting from foreign currency transactions, which are denominated in currencies other than the entity's functional currency, are included in other income (expense), net in the consolidated statements of operations and were not material during 2016, 2015 or 2014.



Table of Contents

## Recent Accounting Pronouncements

In December 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-20 Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers. ASU 2016-20 provides for corrections and improvements for specific areas of Topic 606. In May 2016, the FASB issued ASU No. 2016-12 Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients. ASU 2016-12 provides for improvements and practical expedients for specific areas of Topic 606. In April 2016, the FASB issued ASU No. 2016-10 Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing. ASU 2016-10 provides for clarification of two aspects of Topic 606: identifying performance obligations and the licensing implementation guidance. In March 2016, the FASB issued ASU No. 2016-08 Revenue from Contracts with Customers (Topic 606) - Principal versus Agent Considerations (Reporting Revenue Gross versus Net). ASU No. 2016-08 requires an entity to determine whether the nature of its promise to provide goods or services to a customer is performed in a principal or agent capacity and to recognize revenue in a gross or net manner based on its principal/agent designation. In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This standard outlines a single comprehensive model for entities to use in accounting for revenues arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance.

ASUs 2016-20, 2016-12, 2016-10, 2016-08, and 2014-09 allow for companies to choose to apply the standard retrospectively to each prior reporting period presented (full retrospective application) or retrospectively with the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings of the annual reporting period that includes the date of initial application (modified retrospective application). We plan to adopt the standard under the modified retrospective application. Each guidance is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. We plan to adopt the guidance starting in the first quarter of 2018. We are currently in the process of evaluating the impact this guidance may have on our consolidated financial statements and related disclosures and have initially determined that a potential area of impact subject to further evaluation is our revenue recognition as it relates to our commissions based revenue streams and performance related obligations. We will continue to evaluate the guidance updates as we near our adoption date.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash. ASU 2016-18 requires an entity to explain the change during a period in restricted cash equivalents on the consolidated statements of cash flows and include such amounts when reconciling beginning-of-period and end-of-period total amounts shown on the consolidated statements of cash flows. Early adoption is permitted, and the guidance requires a retrospective adoption. The guidance is effective for annual periods after December 15, 2017, and we are currently in the process of evaluating the impact of this new guidance.

In August 2016, the FASB issued ASU No. 2016-15 Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force). ASU 2016-15 provides for specific guidance on eight cash flow issues where the previously U.S. GAAP was either unclear or did not include specific guidance. The guidance requires a retrospective application and is effective for annual periods after December 15, 2017, with earlier application permitted as of the beginning of an interim or annual reporting period. We have elected to early adopt this standard which did not result in any changes to the presentation of our consolidated statements of cash flows for the years ended December 31, 2016, 2015, and 2014.

In March 2016 the FASB issued ASU No. 2016-09 Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. ASU 2016-09 provides for simplification involving several aspects of the accounting for share-based payment transactions, including the income tax consequences, an option to recognize



gross share-based compensation expense with actual forfeitures recognized as they occur, and classification on the statement of cash flows. In addition to these simplifications, ASU 2016-09 also eliminates the guidance in Topic 718 that was indefinitely deferred shortly after the issuance of FASB Statement No. 123 (revised 2004), Share-Based Payment. Early adoption is permitted and the application of the guidance is different for each update included within ASU 2016-09. The guidance is effective for annual periods after December 15, 2016. We plan to adopt the guidance starting in the first quarter of 2017 and we do not anticipate the provisions in this update to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). ASU 2016-02 requires an entity to recognize a right-of-use asset and lease liability for all leases with terms of more than 12 months. Recognition, measurement, and presentation of expenses will depend on classification as a finance or operating lease. The amendments in this update also require certain quantitative and qualitative disclosures about leasing arrangements. Early adoption is permitted, and the

Table of Contents

guidance requires a modified retrospective adoption. The guidance is effective for annual periods after December 15, 2018, and we are currently in the process of evaluating the impact of this new guidance.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 requires all financial assets and liabilities not accounted for under the equity method to be measured at fair value with the changes in fair value recognized in net income. The amendments in this update also require an entity to separately present in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, the amendments in this update supersede the requirement to disclose the methods and significant assumptions used in calculating the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet for public business entities. Early adoption is not permitted except for the comprehensive income presentation requirement, and the updated guidance requires a prospective application with a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The guidance is effective for annual periods after December 15, 2017, and we are currently in the process of evaluating the impact of this new guidance.

## Note 3. Cash and Cash Equivalents, Investments and Restricted Cash

The following table shows our cash and cash equivalents, restricted cash and investments' adjusted cost, net unrealized loss and fair value as of December 31, 2016 and December 31, 2015 (in thousands):

	December 31, 2016			December 31, 2015		
	Cost	Net Unrealized Loss	Fair Value	Cost	Net Unrealized Loss	Fair Value
Cash and cash equivalents:						
Cash	\$77,329	\$	—\$77,329	\$52,905	\$ —	\$52,905
Money market funds	—	—	—	6,672	—	6,672
Commercial paper	—	—	—	5,453	—	5,453
Corporate securities	—	—	—	600	(1 )	599
Agency bond	—	—	—	1,400	—	1,400
Total cash and cash equivalents	\$77,329	\$	—\$77,329	\$67,030	\$ (1 )	\$67,029
Short-term investments:						
Commercial paper	\$—	\$	—\$—	\$3,746	\$ —	\$3,746
Corporate securities	—	—	—	10,572	(12 )	10,560
Agency bonds	—	—	—	3,494	—	3,494
Total short-term investments	\$—	\$	—\$—	\$17,812	\$ (12 )	\$17,800
Long-term investments:						
Corporate securities	\$—	\$	—\$—	\$3,241	\$ (10 )	\$3,231
Agency bond	—	—	—	1,001	(3 )	998
Long-term corporate securities	\$—	\$	—\$—	\$4,242	\$ (13 )	\$4,229
Short-term restricted cash	\$—	\$	—\$—	\$300	\$ —	\$300
Long-term restricted cash	104	—	104	478	—	478
Total restricted cash	\$104	\$	—\$104	\$778	\$ —	\$778

As of December 31, 2016, we did not carry a balance of cash equivalents, short-term or long-term investments. Our investment policy generally limits the amount of credit exposure to any one issuer. The policy requires investments

generally to be investment grade, with the primary objective of preserving capital and maintaining liquidity. Fair values were determined for each individual security in the investment portfolio. When evaluating an investment for other-than-temporary impairment, we review factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates and our intent to sell or whether it is more likely than not it will be required to sell, and the investment before recovery of the investment's cost basis. During the year ended December 31, 2016, we did not recognize any impairment charges.

73

---

Table of Contents

## Strategic Investment

During the years ended December 31, 2016 and 2015, we invested \$1.0 million and \$2.0 million, respectively, in a third party to expand our customer reach. Our total investment of \$3.0 million is included in other assets on our consolidated balance sheets. We did not record other-than-temporary impairment charges on this investment during the years ended December 31, 2016 and 2015 as there were no significant identified events or changes in circumstances that would be considered an indicator for impairment.

## Note 4. Fair Value Measurement

We have established a fair value hierarchy used to determine the fair value of our financial instruments as follows:

Level 1—Inputs are unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2—Inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the assets or liabilities, either directly or indirectly through market corroboration, for substantially the full term of the financial instruments.

Level 3—Inputs are unobservable inputs based on our own assumptions used to measure assets and liabilities at fair value; the inputs require significant management judgment or estimation.

A financial instrument's classification within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

We had no financial instruments measured and recorded at fair value on a recurring basis as of December 31, 2016 and amounts as of December 31, 2015 are classified based on the valuation technique level in the table below (in thousands):

	December 31, 2015		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Assets:			
Cash equivalents:			
Money market funds	\$6,672	\$ 6,672	\$ —
Commercial paper	5,453	—	5,453
Corporate securities	599	—	599
Agency bond	1,400	—	1,400
Short-term investments:			
Commercial paper	3,746	—	3,746
Corporate securities	10,560	—	10,560
Agency bonds	3,494	—	3,494
Long-term investments:			
Corporate securities	3,231	—	3,231
Agency bond	998	—	998

Edgar Filing: CHEGG, INC - Form 10-K

Total assets measured and recorded at fair value \$36,153 \$ 6,672 \$ 29,481

We value our marketable securities based on quoted prices in active markets for identical assets (Level 1 inputs) or inputs other than quoted prices that are observable either directly or indirectly (Level 2 inputs) in determining fair value. We classify all of our fixed income available-for-sale securities as having Level 2 inputs. The valuation techniques used to measure the fair value of our financial instruments having Level 2 inputs were derived from non-binding market consensus prices that are corroborated by observable market data, quoted market prices for similar instruments, or pricing models such as discounted cash flow techniques.

74

---

Table of Contents

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while we believe our valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

## Note 5. Long-Lived Assets

## Textbook Library, Net

Textbook library, net consisted of the following (in thousands):

	December 31,	
	2016	2015
Textbook library	\$33,980	\$100,783
Less accumulated depreciation	(31,405 )	(71,055 )
Textbook library, net	\$2,575	\$29,728

## Property and Equipment, Net

Property and equipment, net consisted of the following (in thousands):

	December 31,	
	2016	2015
Computer and equipment	\$1,597	\$1,313
Software	4,324	2,591
Furniture and fixtures	2,148	1,652
Leasehold improvements	5,342	4,983
Content	49,725	27,359
Property and equipment	63,136	37,898
Less accumulated depreciation and amortization	(27,831 )	(17,927 )
Property and equipment, net	\$35,305	\$19,971

## Note 6. Acquisitions

## Fiscal Year 2016 Acquisitions

In May 2016, we acquired all of the outstanding interests of Imagine Easy Solutions, LLC (Imagine Easy), a privately held online learning company based in New York that provides a portfolio of online writing tools. We anticipate this acquisition will enhance our ability to acquire new students, increase the value of our platform to our existing students, and have a meaningful and positive impact on their outcomes. The total fair value of the purchase consideration was \$42.3 million. The purchase consideration included deferred cash consideration of \$17.0 million, of which the present value of \$16.8 million was recorded as accrued liabilities on our consolidated balance sheet as of December 31, 2016. We will accrete into the deferred cash consideration of \$17.0 million until it is paid to the sellers in April 2017. During the year ended December 31, 2016, we recorded accretion expense of \$0.4 million through other (expense), income, net on our consolidated statement of operations. Further, the consideration included an escrow and a hold-back amount of \$4.2 million and \$0.5 million, respectively, for general representations and warranties and potential post-closing adjustments. The escrow amount will be released in July 2017, and the hold-back amount was released during the third quarter of 2016.

In December 2016, we acquired certain assets of RefME Ltd., a privately held online learning company based in London, England, to enhance our already existing portfolio of writing tools. The total fair value of the purchase consideration was \$1.8 million. The purchase consideration included deferred cash consideration of \$0.8 million, of which \$0.2 million was

75

---

Table of Contents

paid out during the year ended December 31, 2016 and the remaining \$0.6 million was recorded as accrued liabilities on our consolidated balance sheet as of December 31, 2016 and will be paid out in three quarterly installments in 2017.

The acquisition date fair value of the purchase consideration for the above transactions consisted of the following (in thousands):

Initial cash consideration	\$22,007
Net working capital adjustment	200
Fair value of deferred cash consideration	17,127
Escrow	4,200
Hold-back	500
Fair value of purchase consideration	\$44,034

Included in the purchase agreement for the acquisition of Imagine Easy are additional contingent payments of up to \$18.0 million, of which \$3.0 million relates to the achievement of performance conditions for the fiscal year ended 2016. These performance conditions were achieved therefore these payments will be made over the next three years, subject to continued employment of the sellers, and will be expensed ratably as technology and development and general and administrative expense on our consolidated statements of operations. These contingent payments may be settled by us, at our sole discretion, either in cash or shares of our common stock. We have accrued \$1.0 million as of December 31, 2016 for these contingent payments which is included within accrued liabilities on our condensed consolidated balance sheet.

The fair value of the intangible assets acquired was determined under the acquisition method of accounting for business combinations. The excess of the purchase consideration paid over the fair value of net identifiable assets acquired was recorded as goodwill. Goodwill is primarily attributable to the potential for future product offerings as well as our expanded student reach. The amounts recorded for goodwill are expected to be deductible for tax purposes.

The following table presents the total allocation of purchase consideration recorded in our consolidated balance sheets as of the acquisition date (in thousands):

Cash	\$59
Accounts receivable	2,610
Favorable lease acquired	300
Other acquired assets	212
Acquired intangible assets:	
Trade names	1,840
Domain names	1,330
Advertiser relationships	6,600
User base	550
Non-compete agreements	508
Developed technology	5,660
Total acquired intangible assets	16,488
Total identifiable assets acquired	19,669
Liabilities assumed	(573 )
Net identifiable assets acquired	19,096
Goodwill	24,938
Total fair value of purchase consideration	\$44,034

During the year ended December 31, 2016, we incurred \$1.1 million of acquisition-related expenses associated with the above acquisitions which have been included in general and administrative expenses in our consolidated



statements of operations.

76

---

Table of Contents

## Fiscal Year 2014 Acquisitions

On October 1, 2014, we acquired 100% of the business of internships.com, a division of CareerArc Group, headquartered in Burbank, California. With this acquisition, we aimed to expand our user base and expose new users to our services. We see the acquisition of internships.com as a method to connect the ending of the student life cycle to the beginning of their career. The total fair value of the purchase consideration was \$10.0 million in cash, and \$1.0 million in stock that was placed into escrow, for indemnification against breaches of general representations and warranties, and was released in the year ended December 31, 2016.

On June 5, 2014, we acquired 100% of the outstanding shares and voting interest of InstaEDU, Inc. (InstaEDU), headquartered in San Francisco, California. With this acquisition, we aimed to expand our digital offerings to help students excel in school by including real time tutoring services. We see the acquisition of InstaEDU as a method to connect the textbook offering and service offerings of Chegg together. The total fair value of the purchase consideration was \$31.1 million in cash. This included \$4.5 million that was placed into escrow for indemnification against breaches of general representations and warranties, and was released during the year ended December 31, 2015.

On April 9, 2014, we acquired 100% of the outstanding shares and voting interest of The Campus Special, LLC and The Campus Special Food, LLC (together, the Campus Special), headquartered in Duluth, Georgia for a total fair value purchase consideration of \$16.0 million, consisting of \$14.0 million in cash and 250,000 shares of our common stock, and all of such shares of our common stock were placed in escrow for indemnification against breaches of general representations and warranties that were released during the year ended December 31, 2015, and a fair value contingent consideration of additional shares of common stock, which is payable on the attainment of certain performance metrics in 2014 and 2015. The metrics related to 2014 were not met and as such those shares were not released. The shares associated with the 2015 metrics were released as a result of our exit from the print coupon business.

On March 7, 2014, we acquired certain assets from Bookstep LLC, (Bookstep) to expand our technical resources and research and development capabilities. The total fair value of the purchase consideration was \$0.5 million. The acquisition agreement requires us to pay approximately \$2.5 million in cash, payable over two years, contingent upon the continuation of services by a certain number of consultants during the period after acquisition. The fair value of these subsequent payments was \$2.5 million, which was accounted for as post-combination compensation expense.

The acquisition date fair value of the consideration for the above four transactions consisted of the following as of December 31, 2014 (in thousands):

Cash consideration	\$55,537
Fair value of stock escrow consideration	2,585
Fair value of stock contingent consideration	193
Fair value of purchase consideration	\$58,315

The fair value of the intangible assets acquired was determined under the acquisition method of accounting for business combinations. The excess of purchase consideration paid over the fair value of identifiable intangible assets acquired was recorded as goodwill.

Table of Contents

The following table summarizes the fair value of the net identifiable assets acquired in the year ended December 31, 2014 (in thousands):

Cash	\$1,665
Other acquired assets	595
Acquired intangible assets:	
Developed technology	4,174
Customer lists	3,770
Trade names	5,990
Non-compete agreements	1,630
Corporate partnerships	243
Master services agreements	1,030
Total acquired intangible assets	16,837
Total identifiable assets acquired	19,097
Liabilities assumed	(2,538 )
Net identifiable assets acquired	16,559
Goodwill	41,756
Net assets acquired	\$58,315

During the fourth quarter of 2014, we determined that we would not continue to support or look to expand our print coupon business, resulting in a significant decrease in the expected future cash flows. As a result an impairment analysis was performed based on a discounted cash flow analysis with key assumptions based on the future revenues expected until the services were removed from our website. The analysis indicated that the carrying amounts of the intangible assets acquired will not be fully recoverable, resulting in an impairment charge totaling \$1.6 million, which is included as an operating expense within sales and marketing on our consolidated statements of operations.

For the year ended December 31, 2014, we incurred \$0.7 million of acquisition-related expenses associated with the four acquisitions which have been included in general and administrative expenses in the consolidated statements of operations.

The amounts recorded for goodwill related to the Bookstep, Campus Special and internships.com transactions are deductible for tax purposes. The amount recorded for goodwill related to the InstaEDU transaction is not deductible for tax purposes.

The pro forma results of operations of the above acquisitions have not been presented as the financial impact to our consolidated statements of operations is not material.

#### Note 7. Goodwill and Intangible Assets

Goodwill consists of the following (in thousands):

	December 31, December 31,	
	2016	2015
Beginning balance	\$ 91,301	\$ 91,301
Additions due to acquisitions	24,938	—
Ending balance	\$ 116,239	\$ 91,301

Table of Contents

Intangible assets as of December 31, 2016 and December 31, 2015 consist of the following (in thousands, except weighted-average amortization period):

	December 31, 2016			
	Weighted-Average			
	Amortization	Carrying	Accumulated	Net
	Period	Amount	Amortization	Carrying
	(in Amount			Amount
	months)			
Developed technologies	60	\$ 15,077	\$ (8,245	) \$ 6,832
Customer lists	47	9,970	(3,673	) 6,297
Trade names	47	5,513	(1,998	) 3,515
Non-compete agreements	30	1,728	(1,249	) 479
Master service agreements	21	1,030	(1,005	) 25
Indefinite-lived trade name	—	3,600	—	3,600
Total intangible assets		\$ 36,918	\$ (16,170	) \$ 20,748

	December 31, 2015			
	Weighted-Average			
	Amortization	Carrying	Accumulated	Net
	Period	Amount	Amortization	Carrying
	(in Amount			Amount
	months)			
Developed technologies	52	\$ 9,417	\$ (6,702	) \$ 2,715
Customer lists	20	2,820	(2,239	) 581
Trade names	48	2,343	(920	) 1,423
Non-compete agreements	28	1,220	(832	) 388
Master service agreements	21	1,030	(872	) 158
Indefinite-lived trade name	—	3,600	—	3,600
Total intangible assets		\$ 20,430	\$ (11,565	) \$ 8,865

During the years ended December 31, 2016, 2015 and 2014, amortization expense related to our acquired intangible assets totaled approximately \$4.6 million, \$4.8 million and \$5.0 million, respectively.

As part of our acquisition of internships.com in October 2014, we acquired an indefinite-lived trade name intangible asset valued at \$3.6 million. We will assess this asset for impairment annually during the fourth quarter or whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

As of December 31, 2016, the estimated future amortization expense related to our finite-lived intangible assets is as follows (in thousands):

2017	\$ 5,350
2018	4,446
2019	3,510
2020	2,153
2021	815
Thereafter	874
Total	\$ 17,148



Table of Contents

## Note 8. Balance Sheet Details

## Other Current Assets

Other current assets consist of the following (in thousands):

	December 31,	
	2016	2015
Reimbursement from Ingram	\$ 18,759	\$ 28,875
Other	3,500	2,857
Other Current Assets	\$ 22,259	\$ 31,732

## Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	December 31,	
	2016	2015
Accrued shipping for cycle returns	\$ 1,334	\$ 3,355
Refund reserve	487	4,538
Taxes payable	2,927	3,913
Accrued deferred cash consideration related to acquisition	17,378	—
Payable to Ingram	8,237	9,965
Other	13,956	13,509
Accrued Liabilities	\$ 44,319	\$ 35,280

## Note 9. Debt Obligations

In September 2016, we entered into a revolving line of credit with an aggregate principal amount of \$30.0 million (the Line of Credit) with an accordion feature that, subject to the lender's discretion, allows us to borrow up to a total of \$50.0 million. This new line of credit replaced the previous line of credit that expired in August 2016. The Line of Credit matures September 2019 and requires us to repay the outstanding balance upon maturity. We will pay a fee equal to 0.25% per year on the average daily unused amount of the Line of Credit and a base interest rate equal to the LIBOR. In addition, we will pay a fee for each issued letter of credit which will be determined based on our current leverage ratio at the time the letter of credit is issued. If our leverage ratio is less than 1.00%, we will pay a fee equal to 1.50% per year and if our leverage ratio is greater than or equal to 1.00%, we will pay a fee equal to 2.50% per year. Our leverage ratio is a ratio of all obligations owed to the bank divided by our consolidated EBITDA. EBITDA for the purposes of calculating our leverage ratio is defined as net profit (loss) before tax, plus interest expense, plus non-cash stock compensation (net of capitalized interest expense), depreciation expense, amortization expense and other non-cash expenses (assuming there are no future cash costs), plus expenses incurred in connection with permitted acquisitions (including without limitation accrued acquisition-related contingent expenses) in an amount not to exceed \$6.0 million per calendar year, plus non-recurring expenses in an amount not to exceed \$2.0 million per calendar year. We must maintain financial covenants under the Line of Credit as follows: (1) maintain a balance of unrestricted cash at the Bank of not less than \$30.0 million at all times, other than the three months ending March 31, 2017 and June 30, 2017, and not less than \$25.0 million during the three months ending March 31, 2017 and June 30, 2017; and (2) achieve EBITDA, on a trailing 12 month basis, of not less than (i) \$25.0 million for the period of time from September 30, 2016 through June 30, 2017, (ii) \$30.0 million for the period of time from September 30, 2017 through June 30, 2018, and (iii) \$35.0 million for the period of time from September 30, 2018 through the maturity of the Line of Credit.

As of December 31, 2015, we had a revolving credit facility with an aggregate principal amount of \$30.0 million (the Revolving Credit Facility) with an accordion feature that, subject to certain financial criteria, allowed us to borrow up to a total of \$65.0 million beginning the quarter ended December 31, 2015. The Revolving Credit Facility carried, at our election, a base interest rate of the greater of the Federal Funds Rate plus 0.5% or one-month LIBOR plus 1% or a LIBOR based interest rate plus additional interest of up to 4.5% depending on our leverage ratio. The Revolving Credit Facility expired in August 2016.

Table of Contents

As of December 31, 2016, we were in compliance with the financial covenants of the Line of Credit. Further, we had no amounts outstanding and were able to borrow up to \$30.0 million under the Line of Credit.

## Note 10. Commitments and Contingencies

We lease our offices under operating leases, which expire at various dates through 2022. Our primary operating lease commitments at December 31, 2016 related to our headquarters in Santa Clara, California and our office in San Francisco, California. We recognize rent expense on a straight-line basis over the lease period. Where leases contain escalation clauses, rent abatements, or concessions, such as rent holidays and landlord or tenant incentives or allowances, we apply them in the determination of straight-line rent expense over the lease term. Rental expense, net of sublease income, was approximately \$1.9 million, \$2.5 million and \$3.3 million in the years ended December 31, 2016, 2015 and 2014, respectively.

The aggregate future minimum lease payments as of December 31, 2016, are as follows (in thousands):

2017	\$2,001
2018	1,927
2019	1,099
2020	749
2021	317
Thereafter	138
Total	\$6,231

From time to time, third parties may assert patent infringement claims against us in the form of letters, litigation, or other forms of communication. In addition, we may from time to time be subject to other legal proceedings and claims in the ordinary course of business, including claims of alleged infringement of trademarks, copyrights and other intellectual property rights; employment claims; and general contract or other claims. We may also, from time to time, be subject to various legal or government claims, disputes, or investigations. Such matters may include, but not be limited to, claims, disputes, or investigations related to warranty, refund, breach of contract, employment, intellectual property, government regulation, or compliance or other matters.

In July 2010, the Kentucky Tax Authority issued a property tax assessment of approximately \$1.0 million related to our textbook library located in our Kentucky warehouse for the 2009 and 2010 tax years under audit. In March 2011, we filed a protest with the Kentucky Board of Tax Appeals that was rejected in March 2012. In September 2012, we filed a complaint seeking declaratory rights against the Commonwealth of Kentucky in the Bullitt Circuit Court of Kentucky, and that case was subsequently dismissed in favor of administration remedies with the Kentucky Tax Authority. We received a final Notice of Tax due in October 2012 from the Kentucky Tax Authority and we appealed this notice in November 2012 with the Kentucky Board of Tax Appeals. In May 2013, we presented an Offer in Judgment to the Kentucky Tax Authority of approximately \$150,000, excluding tax and penalties, an amount that we have accrued for the two years under audit. We accrued this amount as of December 31, 2012. We appealed to the Kentucky Board of Tax Appeals in July 2013 and the Board issued a ruling in favor of the Kentucky Department of Revenue in January 2014 maintaining the property tax assessment. In February 2014, we filed an appeal to the Franklin Circuit Court in Kentucky and in June 2014 the Circuit Court held in abeyance our motion to appeal. In October 2014 the Franklin Circuit Court in Kentucky issued its opinion and order reversing the Board of Tax Appeal's decision, setting aside the Kentucky Department of Revenue's tax assessments against us and further vacating all penalties and interest. The Kentucky Department of Revenue has appealed the Circuit Court ruling. On March 4, 2016, the Kentucky Court of Appeals ruled unanimously in our favor, affirming our position that no property tax was owed on the textbooks. The Kentucky Department of Revenue petitioned the Kentucky Supreme Court for a



discretionary review, which was denied in September 2016. The case was determined in our favor with no property tax due related to our textbook library.

We are not aware of any other pending legal matters or claims, individually or in the aggregate, that are expected to have a material adverse impact on our consolidated financial position, results of operations, or cash flows. However, our determination of whether a claim will proceed to litigation cannot be made with certainty, nor can the results of litigation be predicted with certainty. Nevertheless, defending any of these actions, regardless of the outcome, may be costly, time consuming, distract management personnel, and have a negative effect on our business. An adverse outcome in any of these actions, including a judgment or settlement, may cause a material adverse effect on our future business, operating results, and/or financial condition.

Table of Contents

## Note 11. Guarantees and Indemnifications

We have agreed to indemnify our directors and officers for certain events or occurrences, subject to certain limits, while such persons are or were serving at our request in such capacity. We may terminate the indemnification agreements with these persons upon termination of employment, but termination will not affect claims for indemnification related to events occurring prior to the effective date of termination. We have a directors' and officers' insurance policy that limits our potential exposure up to the limits of our insurance coverage. In addition, we also have other indemnification agreements with various vendors against certain claims, liabilities, losses, and damages. The maximum amount of potential future indemnification is unlimited.

We believe the fair value of these indemnification agreements is minimal. We have not recorded any liabilities for these agreements as of December 31, 2016.

## Note 12. Common Stock

We are authorized to issue 400 million shares of common stock, with a par value per share of \$0.001. As of December 31, 2016, we have reserved the following shares of common stock for future issuance:

	December 31, 2016
Warrants to purchase common stock	200,000
Outstanding stock options	11,333,624
Outstanding RSUs	14,142,109
Shares available for grant under the stock plans	9,574,896
Shares available for issuance under employee stock purchase plan	5,310,428
Total common shares reserved for future issuance	40,561,057

## Stock Plans

## 2013 Equity Incentive Plan

On June 6, 2013, the Board of Directors adopted our 2013 Equity Incentive Plan (the 2013 Plan), which was subsequently approved by our stockholders on August 29, 2013. The 2013 Plan became effective on November 11, 2013 and replaced the 2005 Plan. On the effective date of the 2013 Plan, 12,000,000 shares of our common stock were reserved for issuance, plus an additional 3,838,985 shares reserved but not issued or subject to outstanding awards under our 2005 Plan on the effective date of the 2013 Plan, plus, on and after the effective date of the 2013 Plan, (i) shares that are subject to outstanding awards under the 2005 Plan which cease to be subject to such awards, (ii) shares issued under the 2005 Plan that are forfeited or repurchased at their original issue price and (iii) shares subject to awards under the 2005 Plan that are used to pay the exercise price of an option or withheld to satisfy the tax withholding obligations related to any award. As of December 31, 2016 there were 9,574,896 shares available for grant under the 2013 Plan. The 2013 Plan permits the granting of incentive stock options, non-qualified stock options, RSUs, stock appreciation rights, restricted shares of common stock and performance share awards. The exercise price of stock options may not be less than the 100% of the fair market value of the common stock on the date of grant. Options granted pursuant to the 2013 Plan generally expire no later than ten years.

## 2013 Employee Stock Purchase Plan

On June 6, 2013, our board of directors adopted our 2013 Employee Stock Purchase Plan (the 2013 ESPP) and our stockholders subsequently approved the 2013 ESPP Plan on August 29, 2013. The 2013 ESPP permits eligible employees to acquire shares of our common stock by accumulating funds through periodic payroll deductions of up to 15% of base salary. Our 2013 ESPP is intended to qualify as an ESPP under Section 423 of the Code and employees will receive a 15% discount to the lesser of the fair market value of our common stock on (i) the first trading day of the applicable offering period or (ii) the last day of each purchase period in the applicable offering period. Each offering period may run for no more than six months. We have reserved 4,000,000 shares of our common stock under our 2013 ESPP. The aggregate number of shares issued over the term of our 2013 ESPP will not exceed 20,000,000 shares of our common stock. As of December 31, 2016, there were 5,310,428 shares of common stock available for future issuance under the 2013 ESPP.

Table of Contents

## Note 13. Stockholders' Equity

## Share-based Compensation

Total share-based compensation expense recorded for employees and non-employees, is as follows (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Cost of revenues	\$ 172	\$ 262	\$ 617
Technology and development	14,771	11,992	10,451
Sales and marketing	6,124	7,901	11,300
General and administrative	20,718	18,620	14,520
Total share-based compensation expense	\$ 41,785	\$ 38,775	\$ 36,888

Total share-based compensation expense for consultants was \$0.5 million, \$0.4 million and \$0.7 million in the years ended December 31, 2016, 2015 and 2014, respectively. There was no capitalized share-based compensation expense as of December 31, 2016, 2015 or 2014.

## Fair Value of Stock Options

We estimate the fair value of each stock option award using the Black-Scholes-Merton option-pricing model, which utilizes the fair value of our common stock based on active market and requires input on the following subjective assumptions:

**Expected Term.** The expected term for options granted to employees, officers, and directors is calculated as the midpoint between the vesting date and the end of the contractual term of the options. The expected term for options granted to consultants is determined using the remaining contractual life.

**Expected Volatility.** The expected volatility was historically based on the average volatility of public companies within our peer group as our common stock had previously not been publicly trading for a long enough period to rely on our own expected volatility. Beginning with stock options granted during the fourth quarter of 2015, we have based the expected volatility on the average volatility of our stock price as we now have over two years of trading history.

**Expected Dividends.** The dividend assumption is based on our historical experience. To date we have not paid any dividends on our common stock.

**Risk-Free Interest Rate.** The risk-free interest rate used in the valuation method is the implied yield currently available on the United States treasury zero-coupon issues, with a remaining term equal to the expected life term of our options.

The following table summarizes the key assumptions used to determine the fair value of our stock options granted to employees, officers and directors:

	Year Ended December 31,		
	2016	2015	2014
Expected term (years)	5.50	5.50-6.00	6.07
Expected volatility	56.94 %	50.68%-51.69%	55.91%-56.83%
Dividend yield	— %	— %	— %
Risk-free interest rate	1.43 %	1.75%-1.86%	1.88%-2.02%
Weighted-average grant-date fair value per share	\$ 2.58	\$ 3.54	\$ 3.82



Table of Contents

## Fair Value of Restricted Stock Units (RSUs) and of Performance-Based Restricted Stock Units (PSUs)

RSUs and PSUs are converted into shares of our common stock upon vesting on a one-for-one basis. Vesting of RSUs is subject to the employee's continuing service to us, while vesting of PSUs is subject to our achievement of specified corporate financial performance objectives in addition to the employee's continuing service to us. The compensation expense related to RSUs and PSUs is determined using the fair value of our common stock on the date of grant and the expense is recognized on a straight-line basis over the vesting period. RSUs are typically fully vested at the end of three or four years while PSUs vest subject to the achievement of performance objectives and if achieved, typically vest over two to three years. We assess the achievement of performance objectives on a quarterly basis and adjust our share-based payment expense as appropriate.

## Fair Value of 2013 ESPP

Under the 2013 ESPP, rights to purchase shares are generally granted during the second and fourth quarter of each year. We estimate the fair value of rights granted under the 2013 ESPP at the date of grant using the Black-Scholes-Merton option-pricing model. The following table summarizes the key assumptions used to determine the fair value of rights granted under the 2013 ESPP:

	Year Ended December 31,		
	2016	2015	2014
Expected term (years)	0.50	0.50	0.50
Expected volatility	35.10%- <del>35.72%</del>	40.54%-49.59%	40.54%-46.42%
Dividend yield	— %	— %	— %
Risk-free interest rate	0.38%- <del>0.62%</del>	0.29%-0.31%	0.05%-0.07%
Weighted-average grant-date fair value per share	\$ 1.79	\$ 1.98	\$ 1.68

There were 467,979 shares purchased under the 2013 ESPP for the year ended December 31, 2016 at an average price per share of \$3.76 with cash proceeds from the issuance of shares of \$1.8 million.

There were 419,137 shares purchased under the 2013 ESPP for the year ended December 31, 2015 at an average price per share of \$5.81 with cash proceeds from the issuance of shares of \$2.4 million.

## Stock Option Activity

Stock option activity under our equity incentive plans was as follows:

	Options Outstanding		Weighted-Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
	Number of Options Outstanding	Weighted-Average Exercise Price per Share		
Balance at December 31, 2015	12,415,492	\$ 8.68	6.24	\$5,082,489
Granted	232,700	5.00		
Exercised	(121,538 )	2.81		
Canceled	(1,193,030 )	9.31		
Balance at December 31, 2016	11,333,624	\$ 8.60	5.22	\$6,608,611
As of December 31, 2016				
Options exercisable	10,818,738	\$ 8.64	5.07	\$6,004,970

Options vested and expected to vest	11,299,893	\$ 8.60	5.21	\$6,569,584
-------------------------------------	------------	---------	------	-------------

The total intrinsic value of options exercised during 2016, 2015 and 2014, was approximately \$0.6 million, \$3.2 million and \$3.1 million, respectively.

Table of Contents

As of December 31, 2016, our total unrecognized compensation expense for stock options granted to employees, officers, directors, and consultants was approximately \$1.6 million, which will be recognized over a weighted-average vesting period of approximately 0.7 years.

We recognize only the portion of the stock options granted to employees that is ultimately expected to vest as compensation expense. Estimated forfeitures are determined based on historical data and management's expectation of exercise behaviors. Forfeiture rates and the resulting compensation expense are revised in subsequent periods if actual forfeitures differ from the estimate.

## RSU and PSU Activity

	RSUs and PSUs Outstanding Number of	Weighted Average Grant Date Fair Value
Balance at December 31, 2015	13,270,650	\$ 6.38
Granted	10,307,836	4.62
Released	(5,104,641 )	6.37
Canceled	(4,331,736 )	6.06
Balance at December 31, 2016	14,142,109	\$ 5.20

## 2014 PSU Grants

In February 2014, we granted PSUs under the 2013 Plan to certain of our executive officers. The PSUs entitle the executives to receive a certain number of shares of our common stock based on our satisfaction of certain financial and strategic performance targets during 2014 (the 2014 Performance Period). Based on the achievement of the performance conditions during the 2014 Performance Period for the February grants, the final settlement of the PSU awards was 120% of the target shares underlying the PSU awards based on a specified objective formula approved by the Compensation Committee. These PSUs will vest annually over a three year period, with the first year vesting in February 2015. The target number of shares underlying the 2014 Performance Period PSUs that were granted to certain executive officers during the year ended December 31, 2014 totaled 1,208,560 shares and had a weighted average grant date fair value of \$6.37 per share. As of December 31, 2014, 120% of the PSUs vested.

In June 2014, we granted PSUs under the 2013 Plan to the employees of InstaEDU, which were based on achieving certain revenue targets in 2014 and 2015. The target number of shares underlying the PSUs that were granted to certain employees of our InstaEDU acquisition during the year ended December 31, 2014 totaled 2,280,081 and had a weighted average grant date fair value of \$6.00 per share. As of December 31, 2015, metrics related to the 2014 and 2015 periods were not achieved and the shares were canceled following the attainment certification by our compensation committee.

## 2015 PSU Grants

In February 2015, we granted PSUs under the 2013 Plan to certain of our key employees (the February 2015 grants). The PSUs entitle the employees to receive a certain number of shares of our common stock based on our satisfaction of certain financial and strategic performance targets during 2015 (the 2015 Performance Period) and 2016 (the 2016 Performance Period). Based on the achievement of the performance conditions during the 2015 Performance Period for the February 2015 grants, the final settlement met the minimum threshold for the 2015 Performance Period based



on a specified objective formula approved by the Compensation Committee of the Board of Directors (the Compensation Committee). The PSUs related to the 2015 Performance Period vest annually over a one or three year period depending on the employee, with the initial vesting occurring in February 2016. In March 2016, the financial and strategic performance targets were set by the Compensation Committee for the 2016 Performance Period for the February 2015 grants. Based on the achievement of the performance conditions during the 2016 Performance Period for the February 2015 grants, the final settlement met the minimum threshold for the 2016 Performance Period based on a specified objective formula approved by the Compensation Committee. The PSUs related to the 2016 Performance Period vest over a one year period with vesting occurring in March 2017.

## Table of Contents

During the year ended December 31, 2016, the Compensation Committee approved a modification of the performance targets related to the 2015 Performance Period of the February 2015 grant for 26 employees. As a result of the modification, we recorded an expense of \$1.5 million during the year ended December 31, 2016.

The number of shares underlying the PSUs granted during the year ended December 31, 2015 totaled 2,300,824 shares and had a weighted average grant date fair value of \$6.59 per share. During the year ended December 31, 2016, 688,464 shares were released relating to the 2015 Performance Period. As of December 31, 2016, we expect a significant portion of the remaining PSUs related to the 2016 Performance Period to vest.

### 2016 PSU Grants

In March 2016, we granted PSUs under the 2013 Plan to certain of our key executives. The PSUs entitle the executives to receive a certain number of shares of our common stock based on our satisfaction of certain financial and strategic performance targets during 2016. Based on the achievement of the performance conditions for the March 2016 grant, the final settlement met the minimum threshold based on a specified objective formula approved by the Compensation Committee. These PSUs will vest over a three year period depending on the employee, with the initial vesting occurring in March 2018.

The number of shares underlying the PSUs granted during the year ended December 31, 2016 totaled 2,377,842 shares and had a weighted average grant date fair value of \$4.32 per share. As of December 31, 2016, we expect a significant portion of these PSUs to vest.

As of December 31, 2016, we had a total of approximately \$36.2 million of unrecognized compensation costs related to RSUs and PSUs that is expected to be recognized over the remaining weighted average period of 1.9 years.

### Stock Warrants

As of December 31, 2016, we had a total of 200,000 common stock warrants exercisable at a weighted average exercise price of \$12.00.

No common stock warrants were exercised in the year ended December 31, 2016. During the year ended December 31, 2015, 795,549 common stock warrants were exercised at a weighted average exercise price of \$4.12. During the year ended December 31, 2014, 122,733 common stock warrants were exercised at a weighted average exercise price of \$0.82.

### Note 14. Income Taxes

We recorded an income tax provision of approximately \$1.7 million, \$1.5 million and \$0.2 million for the years ended December 31, 2016, 2015 and 2014, respectively. The income tax provision for the year ended December 31, 2016 was primarily due to state and foreign income tax expense and federal tax expense related to tax amortization of acquired indefinite lived intangible assets. The income tax provision for year ended December 31, 2015 was primarily due to state and foreign income tax expense and federal tax expense related to tax amortization of acquired indefinite lived intangible assets. The income tax provision for the year ended December 31, 2014 was primarily the result of foreign and state income taxes offset by the release of valuation allowance of \$1.3 million resulting from our acquisition of InstaEDU.



Table of Contents

Our income tax provision consisted of the following (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Current income taxes:			
Federal	\$(18 )	\$—	\$—
State	321	263	304
Foreign	959	778	871
Total current income taxes	1,262	1,041	1,175
Deferred income taxes:			
Federal	503	484	(1,003)
State	48	56	33
Foreign	(106 )	(102 )	(19 )
Total deferred income taxes	445	438	(989 )
Total income tax provision	\$1,707	\$1,479	\$186

Loss before provision for income taxes consisted of the following (in thousands):

	Year Ended December 31,		
	2016	2015	2014
United States	\$(42,687)	\$(59,376)	\$(65,930)
Foreign	2,149	1,645	1,358
Total	\$(40,538)	\$(57,731)	\$(64,572)

The differences between our income tax provision as presented in the accompanying consolidated statements of operations and the income tax expense computed at the federal statutory rate consists of the items shown in the following table as a percentage of pretax loss (in percentages):

	Year Ended December 31,		
	2016	2015	2014
Income tax at U.S. statutory rate	34.0 %	34.0 %	34.0 %
State, net of federal benefit	1.7	3.7	5.1
Share-based compensation	(9.1 )	(7.0 )	(6.5 )
Non-deductible expenses	(0.2 )	(0.2 )	(0.4 )
Other	(1.4 )	—	(0.5 )
Change in valuation allowance	(29.2)	(33.1)	(32.0)
Total	(4.2 )%	(2.6 )%	(0.3 )%

Table of Contents

A summary of our deferred tax assets is as follows (in thousands):

	Year Ended	
	December 31,	
	2016	2015
Deferred tax assets:		
Accrued expenses and reserves	\$5,069	\$7,351
Share-based compensation	23,864	21,676
Deferred revenue	1,085	1,488
Net operating loss carryforwards	73,708	58,664
Property and equipment, textbooks and intangibles assets	5,168	7,577
Other items	1,407	1,612
Gross deferred tax assets	110,301	98,368
Valuation allowance	(110,045)	(98,209)
Total deferred tax assets	256	159
Deferred tax liabilities:		
Intangible asset	(1,413 )	(862 )
Total deferred tax liabilities	(1,413 )	(862 )
Net deferred tax liability	\$(1,157)	\$(703 )

At December 31, 2016 and 2015 the deferred tax liability is created by the tax amortization of acquired indefinite lived intangible assets. Under the accounting guidance this deferred tax liability cannot be used as a source of income for recognition of deferred tax assets when determining the amount of valuation allowance to be recorded.

Realization of the deferred tax assets is dependent upon future taxable income, the amount and timing of which are uncertain. Accordingly, the federal and state gross deferred tax assets have been fully offset by a valuation allowance. The net valuation allowance increased by approximately \$11.8 million and \$19.1 million during 2016 and 2015, respectively.

As of December 31, 2016, we had net operating loss carryforwards for federal and state income tax purposes of approximately \$200.7 million and \$151.5 million, respectively, which will begin to expire in years beginning 2028 and 2017, respectively.

As of December 31, 2016, we had tax credit carryforwards for federal and state income tax purposes of approximately \$3.5 million and \$4.3 million, respectively. The federal credits expire in various years beginning in 2030. The state credits do not expire.

Utilization of our net operating losses and tax credit carryforwards may be subject to substantial annual limitations due to ownership change limitations provided by the Internal Revenue Code of 1986, as amended (IRC), and similar state provisions. Such annual limitations could result in the expiration of the net operating losses and tax credit carryforwards before utilization.

As of December 31, 2016 and 2015, we have permanently reinvested approximately \$6.0 million and \$4.4 million of earnings from our international subsidiaries, respectively, and have not provided for U.S. federal income and foreign withholding taxes. If we were to distribute these earnings, such earnings could be subject to income or other taxes upon repatriation. Determination of the amount of unrecognized deferred tax liability related to these earnings is not practicable.

During the year ended December 31, 2016, we settled an audit relating to an examination by the tax authorities in India for the fiscal filing period ending March 31, 2012 for which we had received a notice of adjustment relating to our transfer pricing between the US and our Indian subsidiary. Also, the fiscal filing periods ending March 31, 2013 and 2014 were settled with no adjustment. Additionally, during the year ended December 31, 2016 we were informed that we would be under examination by the tax authorities in India for the fiscal filing period ending March 31, 2015.

Table of Contents

We recognize interest and penalties related to uncertain tax positions as a component of income tax expense. During 2016 we recognized a decrease of \$18 thousand and an increase during 2015 and 2014 of \$0.1 million and \$0.1 million of interest and penalties, respectively. Accrued interest and penalties as of December 31, 2016 and 2015 were approximately \$0.6 million and \$0.7 million, respectively.

We file tax returns in U.S. federal, state, and certain foreign jurisdictions with varying statutes of limitations. Due to net operating loss and credit carryforwards, all of the tax years since inception through the 2016 tax year remain subject to examination by the U.S. federal and some state authorities. Foreign jurisdictions remain subject to examination up to approximately seven years from the filing date.

A reconciliation of the beginning and ending balances of the total amount of unrecognized tax benefits, excluding accrued interest and penalties, is as follows (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Beginning balance	\$4,849	\$4,272	\$2,994
Increase in tax positions for prior years	478	82	406
Decrease in tax positions for prior years	(855 )	(416 )	(284 )
Decrease in tax positions for prior year settlement	(32 )	(61 )	—
Decrease in tax positions for prior years due to statutes lapsing	(76 )	—	—
Increase in tax positions for current year	595	948	1,172
Change due to translation of foreign currencies	(77 )	24	(16 )
Ending balance	\$4,882	\$4,849	\$4,272

The actual amount of any taxes due could vary significantly depending on the ultimate timing and nature of any settlement. We believe that the amount by which the unrecognized tax benefits may increase or decrease within the next 12 months is not estimable. The amount of unrecognized tax benefits, if recognized, that would affect the effective tax rate is \$1.5 million for the year ended December 31, 2016. One or more of these unrecognized tax benefits could be subject to a valuation allowance if and when recognized in a future period, which could impact the timing of any related effective tax rate benefit.

#### Note 15. Restructuring (Credits) Charges

##### 2015 Restructuring Plan

During the year ended December 31, 2016, we recorded restructuring credits of \$0.4 million primarily related to a partial reversal of previously accrued lease termination costs due to our subtenant leasing additional space. During the year ended December 31, 2015, we recorded restructuring charges of \$4.9 million related to our exits from our print coupon business and our Kentucky warehouse. The charges during the year ended December 31, 2015 included one-time employee termination benefits for 71 employees of \$1.9 million and lease termination and other costs of \$3.0 million. As a result of our strategic partnership with Ingram, we have successfully exited our warehouse facilities in the year ended December 31, 2015. Costs incurred to date related to the lease termination and other costs are expected to be fully paid by 2021.

Table of Contents

The following table summarizes the activity related to the accrual for restructuring charges (in thousands):

	Workforce Reduction Costs	Lease Termination and Other Costs	Total
Balance at January 1, 2015	\$ —	\$ —	\$—
Restructuring charges	1,885	2,983	4,868
Cash payments	(1,830 )	(675 )	(2,505 )
Write-offs	—	(317 )	(317 )
Other	—	472	472
Balance at December 31, 2015	\$ 55	\$ 2,463	\$2,518
Restructuring credits	—	(423 )	(423 )
Cash payments	(55 )	(1,734 )	(1,789 )
Balance at December 31, 2016	\$ —	\$ 306	\$306

As of December 31, 2016, the \$0.3 million liability was comprised of a short-term accrual of \$0.1 million included within accrued liabilities and a long-term accrual of \$0.2 million included within other liabilities on the consolidated balance sheet.

## Note 16. Related-Party Transactions

Our Chief Executive Officer is a member of the Board of Directors of Adobe Systems Incorporated (Adobe). During the years ended December 31, 2016, 2015 and 2014, we had purchases of \$3.1 million, \$2.9 million and \$0.9 million, respectively, from Adobe. We had no revenues in the year ended December 31, 2016 and \$0.1 million and \$1.0 million in revenues in the years ended December 31, 2015 and 2014, respectively, from Adobe. We had \$0.3 million and \$0.4 million in payables as of December 31, 2016 and 2015, respectively, to Adobe. We had no outstanding accounts receivables as of December 31, 2016 and 2015 from Adobe.

One of our board members is also a member of the Board of Directors of Cengage Learning, Inc. (Cengage). During the years ended December 31, 2016, 2015 and 2014, we had purchases of \$10.2 million, \$11.5 million and \$12.4 million, respectively, from Cengage. We had \$0.6 million and \$0.1 million in revenues from Cengage in the years ended December 31, 2016 and 2015, respectively, and no revenues in 2014. We had an immaterial amount in payables as of December 31, 2016 and 2015 to Cengage. We had \$0.1 million in outstanding accounts receivables as of December 31, 2016 and no outstanding accounts receivables as of December 31, 2015 from Cengage.

One of our board members is also a member of the Board of Directors of Groupon, Inc. (Groupon). During the years ended December 31, 2016 and 2015, we had purchases of \$0.6 million and \$0.1 million, respectively, from Groupon and an immaterial amount in 2014. We had no revenues in the years ended December 31, 2016, 2015 and 2014 from Groupon. We had an immaterial amount in payables as of December 31, 2016 and 2015 to Groupon. We had no outstanding accounts receivables as of December 31, 2016 and 2015 from Groupon.

One of our board members is also a member of the Board of Directors of Synack, Inc. (Synack). During the years ended December 31, 2016 and 2015, we had purchases of \$0.2 million and \$0.1 million, respectively, of services from Synack.

Transactions with the above related parties have been conducted on an arms-length basis and the terms of our contracts are consistent with our contracts with other independent parties.

## Note 17. Employee Benefit Plan



We sponsor a 401(k) savings plan for eligible employees and their beneficiaries. Contributions by us are discretionary. Participants may contribute, on a pretax basis, a percentage of their annual compensation, but not to exceed a maximum contribution amount pursuant to Section 401(k) of the IRC. During 2016, 2015 and 2014, our matching contributions totaled approximately \$0.9 million, \$0.8 million, and \$0.8 million, respectively.

Table of Contents

## Note 18. Segment Information

Our chief operating decision-maker is our Chief Executive Officer who makes resource allocation decisions and reviews financial information presented on a consolidated basis. Accordingly, we have determined that we have a single operating and reporting segment and operating unit structure.

## Product Information

We derive our revenues from our Chegg Services and Required Materials product lines. Chegg Services includes our products and services we provide to supplement the requirements and help students with their coursework as well as our marketing services which help to complete our offering of services to students. Required Materials includes all products that are essential for students to meet the requirements of their coursework. Chegg Services includes Chegg Study, Chegg Tutors, Writing Tools (newly acquired in May 2016), Enrollment Marketing, Brand Partnership, Internships, and Test Prep. Required Materials includes the rental and sale of print textbooks, our web-based, multiplatform eTextbook Reader, eTextbooks and supplemental course materials and the commissions earned through our Ingram partnership.

The following table sets forth our total net revenues for the periods shown for our Chegg Services and Required Materials product lines (in thousands):

	December 31,		
	2016	2015	2014
Chegg Services	\$ 129,335	\$94,285	\$68,117
Required Materials	124,755	207,088	236,717
Total net revenues	\$254,090	\$301,373	\$304,834

## Geographic Information

Our headquarters and most of our operations are located in the United States. We conduct our sales, marketing and customer service activities primarily in the United States. Geographic revenues information is based on the location of the customer. In 2016, 2015 and 2014, substantially all of our revenues and long-lived assets are located in the United States.

Table of Contents

## Note 19. Selected Quarterly Financial Data (unaudited)

	Three Months Ended			
	March 31, 2016	June 30, 2016	September 30, 2016	December 31, 2016
Total net revenues	\$66,654	\$53,036	\$ 71,343	\$ 63,057
Gross profit	\$27,731	\$31,629	\$ 32,644	\$ 42,485
Net loss	\$(15,685)	\$(9,008)	\$(16,063)	\$(1,489)
Weighted average shares used to compute net loss per share, basic and diluted	89,118	90,416	91,059	91,526
Net loss per share, basic and diluted	\$(0.18)	\$(0.10)	\$(0.17)	\$(0.02)

	Three Months Ended			
	March 31, 2015	June 30, 2015	September 30, 2015	December 31, 2015
Total net revenues	\$84,872	\$67,061	\$ 81,286	\$ 68,154
Gross profit	\$19,379	\$30,805	\$ 19,566	\$ 41,774
Net (loss) income	\$(28,542)	\$(10,131)	\$(24,167)	\$ 3,630
Weighted average shares used to compute net (loss) income per share:				
Basic	84,794	86,741	87,706	87,993
Diluted	84,794	86,741	87,706	93,225
Net (loss) income per share:				
Basic	\$(0.34)	\$(0.12)	\$(0.28)	\$ 0.04
Diluted	\$(0.34)	\$(0.12)	\$(0.28)	\$ 0.04

We recorded restructuring credits of \$0.1 million, \$0.1 million, \$0.2 million and \$44 thousand in the three months ended December 31, 2016, September 30, 2016, June 30, 2016 and March 31, 2016, respectively. We recorded restructuring charges of \$1.6 million, \$0.3 million, \$0.5 million and \$2.5 million in the three months ended December 31, 2015, September 30, 2015, June 30, 2015 and March 31, 2015, respectively.

Table of Contents

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the period covered by this report.

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on management's evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are designed to, and are effective to, provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

(b) Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) of the Securities Exchange Act of 1934, as amended). Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control—Integrated Framework (2013 framework). The Company has excluded from its evaluation the internal control over financial reporting of all current year acquisitions, which are included in the December 31, 2016 consolidated financial statements and constituted approximately 1% of total assets as of December 31, 2016, and approximately 4% of total net revenues for the year then ended December 31, 2016. All control systems are subject to inherent limitations. Our management has concluded that, as of December 31, 2016, our internal control over financial reporting is effective based on these criteria. This Annual Report on Form 10-K does not include an attestation report of our registered public accounting firm because, as an "emerging growth company" under the JOBS Act, we are exempt from the requirement to obtain an attestation report from our registered public accounting firm.

(c) Changes in Internal Control over Financial Reporting

During the fourth quarter of fiscal 2016, there were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during our most recently completed fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

93

---

Table of Contents

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information concerning our directors, compliance with Section 16(a) of the Exchange Act, our Audit Committee and any changes to the process by which stockholders may recommend nominees to the Board required by this Item are incorporated herein by reference to information contained in the Proxy Statement, including “Proposal No. 1 Election of Directors”, “Committees of our Board of Directors”, “Section 16(a) Beneficial Ownership Reporting Compliance” and “Stockholder Proposals to Be Presented at Next Annual Meeting.”

The information concerning our executive officers required by this Item is incorporated herein by reference to information contained in the Proxy Statement, including “Our Management.”

We have adopted a code of ethics, our Code of Business Conduct and Ethics, which applies to all employees, including our principal executive officer, our principal financial officer, and all other executive officers, and our board of directors. The Code of Business Conduct and Ethics is available on our web-site at investor.chegg.com under “Corporate Governance.” We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding amendment to, or waiver from, a provision of our Code of Business Conduct and Ethics by posting such information on our website at the address and location specified above.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item is incorporated herein by reference to information contained in the Proxy Statement, including “Compensation Committee Interlocks and Insider Participation” and “Executive Compensation.”

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item is incorporated herein by reference to information contained in the Proxy Statement, including “Transactions with Related Parties, Founders and Control Persons” and “Independence of Directors.”

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item is incorporated herein by reference to information contained in the Proxy Statement, including “Corporate Governance Standards and Director Independence” “Transactions with Related Parties, Founders and Control Persons” and “Termination and Change of Control Arrangements.”

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this Item is incorporated herein by reference to information contained in the Proxy Statement, including “Proposal No. 2 Ratification of Independent Registered Public Accounting Firm”.

Table of Contents

## PART IV

## ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

We have filed the following documents as part of this Annual Report on Form 10-K:

## 1. Consolidated Financial Statements

	Page
Report of Independent Registered Public Accounting Firm	<u>59</u>
Consolidated Balance Sheets	<u>60</u>
Consolidated Statements of Operations	<u>61</u>
Consolidated Statements of Comprehensive Loss	<u>62</u>
Consolidated Statements of Stockholders' Equity	<u>63</u>
Consolidated Statements of Cash Flows	<u>64</u>
Notes to Consolidated Financial Statements	<u>65</u>

## 2. Financial Statement Schedules

Schedule II-Valuation and Qualifying Accounts (in thousands):

	Years Ended December 31, 2016, 2015 and 2014			
	Balance at Beginning of Year	Provision (Release) for Bad Debts	Net (Write-offs) Recoveries	Balance at End of Year
Allowance for doubtful accounts				
2016	\$378	\$ 58	\$ —	\$ 436
2015	\$559	\$ (77 )	\$ (104 )	\$ 378
2014	\$317	\$ 234	\$ 8	\$ 559

	Years Ended December 31, 2016, 2015 and 2014			
	Balance at Beginning of Year	Provision for Refunds	Refunds Issued	Balance at End of Year
Refund Reserve				
2016	\$4,538	\$ 26,373	\$(30,424)	\$ 487
2015	\$6,174	\$ 39,919	\$(41,555)	\$ 4,538
2014	\$330	\$ 54,434	\$(48,590)	\$ 6,174

All other financial statement schedules are omitted because they are not applicable or the information is included in the Registrant's consolidated financial statements or related notes.

## 3. Exhibits

See the Index to Exhibits immediately following the signature page of this Annual Report on Form 10-K.

## ITEM 16. FORM 10-K SUMMARY

None.

95

---



Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CHEGG, INC.

February 22, 2017 By: /S/ DAN ROSENSWEIG

Dan Rosensweig

President, Chief Executive Officer and Chairman

Table of Contents

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS that each individual whose signature appears below constitutes and appoints Dan Rosensweig, Andrew Brown and Dave Borders Jr., and each of them, his or her true and lawful attorneys-in-fact and agents with full power of substitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any amendments to this Annual Report on Form 10-K and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or his, her or their substitute or substitutes, may lawfully do or cause to be done or by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

Name	Title	Date
/S/ DAN ROSENSWEIG Dan Rosensweig	President, Chief Executive Officer and Chairman (Principal Executive Officer)	February 22, 2017
/S/ ANDREW BROWN Andrew Brown	Chief Financial Officer (Principal Financial Officer)	February 22, 2017
/S/ ROBIN TOMASELLO Robin Tomasello	Vice President, Corporate Controller (Principal Accounting Officer)	February 22, 2017
/S/ JEFFREY HOUSENBOLD Jeffrey Housenbold	Director	February 22, 2017
/S/ RENEE BUDIG Renee Budig	Director	February 22, 2017
Marne Levine	Director	February 22, 2017
/S/ RICHARD SARNOFF Richard Sarnoff	Director	February 22, 2017
Ted Schlein	Director	February 22, 2017
/S/ JOHN YORK John York	Director	February 22, 2017

Table of Contents

## Index to Exhibits

Exhibit No.	Exhibit	Incorporated by Reference			Exhibit No.	Filed Herewith
		Form	File No	Filing Date		
3.01	Restated Certificate of Incorporation of the Registrant effective November 18, 2013	10-K	001-36180	3/4/16	3.01	
3.02	Restated Bylaws of the Registrant effective November 13, 2013	10-K	001-36180	3/4/16	3.02	
4.01	Form of Registrant's Common Stock Certificate Amended and Restated Investors' Rights Agreement, dated as of March 7, 2012, by and among the Registrant and certain investors of the Registrant	S-1/A	333-190616	10/01/13	4.01	
4.02	Form of Indemnification Agreement entered into between the Registrant and each of its directors and executive officers	S-1	333-190616	08/14/13	4.02	
10.01*	2005 Stock Incentive Plan, as amended, and forms of agreement thereunder	S-1/A	333-190616	10/01/13	10.01	
10.02*	2013 Equity Incentive Plan, and forms of agreement thereunder	S-1	333-190616	08/14/13	10.02	
10.03*	2013 Employee Stock Purchase Plan	S-1/A	333-190616	10/25/13	10.04	
10.04*	Offer Letter between Dan Rosensweig and the Registrant, dated December 3, 2009	S-1	333-190616	08/14/13	10.05	
10.05*	Amendment to Offer Letter between Dan Rosensweig and the Registrant, dated November 29, 2012	S-1	333-190616	08/14/13	10.06	
10.06*	Offer Letter between Andy Brown and the Registrant, dated September 2, 2011	S-1	333-190616	08/14/13	10.07	
10.07*	Amendment to Offer Letter between Andy Brown and the Registrant, dated November 29, 2012	10-K	001-36180	3/6/14	10.07	
10.08*	Offer Letter between Jenny Brandemuehl and the Registrant, dated January 9, 2013	10-K	001-36180	3/6/14	10.08	
10.10*	Lease between Silicon Valley CA-I, LLC and the Registrant, dated as of May 14, 2012					X
10.13	Commencement Date Memorandum between Silicon Valley CA-I, LLC and the Registrant, dated as of October 12, 2012	S-1	333-190616	08/14/13	10.14	
10.14	Standard Industrial Lease Agreement between Pattillo Industrial Partners, LLC and the Registrant, dated as of October 17, 2009	S-1	333-190616	08/14/13	10.15	
10.15	Amendment to Lease, dated as of May 13, 2011, amended the Standard Industrial Lease Agreement between Pattillo Industrial Partners, LLC and the Registrant, dated as of October 17, 2009	S-1	333-190616	08/14/13	10.16	
10.16	2015 Inventory Purchase and Consignment Agreement dated April 3, 2015, by and among Ingram Hosting Holdings Inc., the Company and Ingram Book Group Inc.	S-1	333-190616	08/14/13	10.17	
10.17†		10-Q	001-36180	08/06/15	10.01	

Edgar Filing: CHEGG, INC - Form 10-K

10.19	Interest Purchase Agreement by and among Chegg Inc., and Imagine Easy Solutions, LLC and the Sellers, dated as of April 28, 2016.	8-K	001-36180	5/2/16	99.03
10.20	Credit Agreement dated September 21, 2016 by and between Chegg, Inc. and Wells Fargo Bank, National Association.	8-K	001-36180	9/22/16	99.1
21.01	List of subsidiaries				X

Table of Contents

23.01	Consent of Independent Registered Public Accounting Firm	X
24.01	Power of Attorney (included on signature page hereto)	X
31.01	Certification of Dan Rosensweig, Chief Executive Officer, pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X
31.02	Certification of Andrew Brown, Chief Financial Officer, pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X
32.01**	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X
101.INS	XBRL Instance	X
101.SCH	XBRL Taxonomy Extension Schema	X
101.CAL	XBRL Taxonomy Extension Calculation	X
101.LAB	XBRL Taxonomy Extension Labels	X
101.PRE	XBRL Taxonomy Extension Presentation	X
101.DEF	XBRL Taxonomy Extension Definition	X
†	Confidential treatment has been granted for portions of this exhibit by the SEC.	
*	Indicates a management contract or compensatory plan.	
**	This certification is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended (Exchange Act), or otherwise subject to the liability of that section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended or the Exchange Act.	