

**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 001-36280

SharpSpring, Inc.

(Exact name of Registrant as specified in its charter)

Delaware

*(State or other jurisdiction of
incorporation or organization)*

**550 SW 2nd Avenue
Gainesville, FL**

(Address of principal executive offices)

05-0502529

*(I.R.S. employer
identification number)*

32601

(Zip Code)

888-428-9605

(Registrant's telephone number)

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 NASDAQ Stock Market LLC

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 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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 of 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 the 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

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

The aggregate market value of the voting common equity held by non-affiliates of the registrant was \$25,845,316 as of June 30, 2016.

As of March 27, 2017, there were 8,371,547 outstanding shares of the registrant's common stock, \$.001 par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed in conjunction with the registrant's 2017 annual meeting of stockholders are incorporated by reference in Part III of this Annual Report on Form 10-K. The proxy statement will be filed by the registrant with the Securities and Exchange Commission not later than 120 days after the end of the registrant's fiscal year ended December 31, 2016.

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PART I

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report on Form 10-K contains forward-looking statements. Forward-looking statements involve risks and uncertainties, such as statements about our plans, objectives, expectations, assumptions or future events. In some cases, you can identify forward-looking statements by terminology such as “anticipate,” “estimate,” “plan,” “project,” “continuing,” “ongoing,” “expect,” “we believe,” “we intend,” “may,” “should,” “will,” “could” and similar expressions denoting uncertainty or an action that may, will or is expected to occur in the future. These statements involve estimates, assumptions, known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from any future results, performances or achievements expressed or implied by the forward-looking statements.

Examples of forward-looking statements include:

- the timing of the development of future products;
- projections of costs, revenue, earnings, capital structure and other financial items;
- statements of our plans and objectives;
- statements regarding the capabilities of our business operations;
- statements of expected future economic performance;
- statements regarding competition in our market; and
- assumptions underlying statements regarding us or our business.

Forward-looking statements are neither historical facts nor assurances of future performance. Instead, they are based only on our current beliefs, expectations and assumptions regarding the future of our business, future plans and strategies, projections, anticipated events and trends, the economy and other future conditions. Because forward-looking statements relate to the future, they are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict and many of which are outside of our control. Our actual results and financial condition may differ materially from those indicated in the forward-looking statements. Therefore, you should not rely on any of these forward-looking statements. Important factors that could cause our actual results and financial condition to differ materially from those indicated in the forward-looking statements include, among others, the following:

- strategic actions, including acquisitions and dispositions and our success in integrating acquired businesses;
- the extent to which we continue to experience attrition related to the migration of customers from our legacy GraphicMail platform;
- the occurrence of hostilities, political instability or catastrophic events;
- changes in customer demand;
- the extent to which we are successful in gaining new long-term relationships with customers or retaining existing ones and the level of service failures that could lead customers to use competitors’ services;
- developments and changes in laws and regulations, including increased regulation of our industry through legislative action and revised rules and standards; and
- disruptions to our technology network including computer systems and software, as well as natural events such as severe weather, fires, floods and earthquakes or man-made or other disruptions of our operating systems, structures or equipment.

The ultimate correctness of these forward-looking statements depends upon a number of known and unknown risks and events. We discuss our known material risks under Item 1.A “Risk Factors.” Many factors could cause our actual results to differ materially from the forward-looking statements. In addition, we cannot assess the impact of each factor 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.

The forward-looking statements speak only as of the date on which they are made, and, except as required by law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

ITEM 1. BUSINESS

Overview

SharpSpring, Inc. (the “Company”) is a cloud-based marketing technology company. The Company’s products are designed to improve the way that businesses communicate with their prospects and customers to increase sales. The Company’s flagship SharpSpring marketing automation platform uses advanced features such as web tracking, lead scoring and automated workflow to help businesses deliver the right message to the right customer at the right time. All of our products are designed and built as Software as Service (or SaaS) offerings. We provide our products primarily on a subscription basis, with additional fees charged if specified volume limits are exceeded by our customers.

We operate globally through SharpSpring, Inc., a Delaware corporation, and our wholly owned subsidiaries that consist of (i) SharpSpring Technologies, Inc., a Delaware corporation; (ii) InterInbox SA, a Swiss corporation; (iii) ERNEPH 2012A (Pty) Ltd. dba ISMS, a South African limited company; (iv) ERNEPH 2012B (Pty) Ltd. dba GraphicMail South Africa, a South African limited company; (v) Quattro Hosting LLC, a Delaware limited liability company; (vi) SMTP Holdings S.a.r.l., a Luxembourg S.a.r.l.; and (vii) InterCloud Ltd, a Gibraltar Limited Company. Unless the context otherwise requires, all references to the “Company,” “we,” “our” or “us” and other similar terms means SharpSpring, Inc., and its subsidiaries.

On June 27, 2016, we sold the assets related to our SMTP email relay product to the Electric Mail Company, a Nova Scotia company.

Products and Services

SharpSpring Marketing Automation

Our SharpSpring marketing automation solution brings powerful digital marketing tools to small and medium-sized businesses and is primarily sold to marketing agencies who use the platform on behalf of their clients. SharpSpring’s powerful features, flexible platform, and ease-of-use allow customers to increase leads into their business, convert more leads to sales and measure the effectiveness of all their marketing campaigns. At the end of 2016, we had over 1,400 marketing automation customers and over 5,000 businesses using the platform, including agencies, agency clients and direct end users. SharpSpring provides this powerful, but simple-to-use marketing automation platform at a lower price than its competitors and in a framework that is especially appealing because of its inherently flexible architecture. The solution also offers a built-in CRM tool and call tracking functionality.

Email Marketing

During 2015 and the first half of 2016, the Company offered the GraphicMail email campaign management solution to customers globally. In late 2015, the Company announced that it would discontinue selling and offering the GraphicMail email solution and migrate existing GraphicMail customers to the SharpSpring platform, onto a new product named SharpSpring Mail+. SharpSpring Mail+ provides customers with some marketing automation functionality along with traditional email marketing capabilities. Prior to the migration of customers to SharpSpring Mail+, the GraphicMail platform focused on email, social and mobile marketing and was typically used by companies wishing to communicate with a list of subscribers or customers. Email marketing remains an effective form of digital marketing today and provides users with a high ROI on their marketing budget, which continues to drive email marketing industry growth. SharpSpring Mail+ customers have tools such as automated workflows, triggered emails and dynamic list segmentation to improve the effectiveness of their marketing programs.

SMTP Email Relay Services

On June 27, 2016, we sold the assets related to our SMTP email relay product to the Electric Mail Company, a Nova Scotia company. Prior to that, the Company offered a proprietary SMTP relay product, which was designed to send high volumes of email messages in an efficient manner and increase the delivery rate of email messages. For over a decade, customers turned to SMTP to ensure their emails were delivered to the inbox of their intended recipients. Companies sending large volumes of permission-based, opt-in email (email that a person has agreed to receive) often have difficulty getting those emails into the recipient's inbox. In recent years, Internet Service Providers (ISPs) have been forced to tighten email filters resulting in billions of legitimate emails never reaching their intended recipients. SMTP's deliverability expertise and technology platform allowed customers to achieve higher rates of receipt, thus improving their marketing campaigns and communication efforts. This product is treated as a discontinued operation in the consolidated financial statements.

Markets & Competition

We operate in the marketing technology market, with a focus on marketing automation which enables businesses to improve the number of leads they generate for their products, convert more leads to sales and measure the return on all their marketing programs. Although we are now focused nearly 100% on marketing automation, the company historically has offered products that perform traditional email marketing services and email relay (delivery) services. The Company's email delivery services were sold in June 2016. The three markets served in 2016 include:

- 1) Marketing automation products (highly targeted one-to-one messaging with sophisticated analytics);
- 2) Traditional email marketing services (newsletters and one-to-many communications); and
- 3) Email delivery services (robust infrastructure for the delivery of high volumes of email)

Marketing Automation: Our SharpSpring product competes primarily in the marketing automation market. Based on industry reports, our growth rate and the growth rate of our competitors, we believe the market for marketing automation technology is growing at approximately 60% per year currently. The market for marketing automation software and related solutions is new and evolving, with high barriers to entry due to the complex nature of the technology. SharpSpring entered the market in 2014 with a highly competitive offering that achieved meaningful customer adoption in its first three years after launch. At the end of 2016, SharpSpring had over 1,400 paying customers and approximately 5,000 businesses using the SharpSpring marketing automation platform, including agencies, agency clients and direct end-user customers. We face competition from cloud-based software and SaaS companies including HubSpot, Act-On, Pardot (acquired by Salesforce.com in July 2013) and Active Campaign. We differentiate ourselves from the competition with SharpSpring's advanced features, ease of use, platform flexibility, and value compared to other competitive offerings. SharpSpring is designed as a solution for small or mid-sized businesses, but also focuses on selling to marketing agencies, who serve as partners providing a distribution channel to end customers. The Company's SharpSpring Mail+ product provides customers an entry point into using marketing automation technology for customers that have historically used traditional email marketing solutions.

Traditional Email Marketing: Until the middle of 2016, the Company offered traditional email marketing capabilities through its GraphicMail product. During the second quarter of 2016, customers of the GraphicMail product were migrated to SharpSpring Mail+. GraphicMail historically competed in the email marketing space, with a product focused on the small and medium-size business market (SMB). GraphicMail was designed to provide customers with an easy-to-use email campaign management solution that includes design capabilities, reporting tools and list management functionality. GraphicMail competed with companies such as Constant Contact, iContact Corporation, The Rocket Science Group LLC (MailChimp), and VerticalResponse, Inc., a subsidiary of Deluxe Corporation, and others. GraphicMail, and most other vendors, typically charge a monthly fee or a fee per number of emails sent and, in some cases, have a free offering for low-volume or non-profit customers. GraphicMail's local language and support had historically been market differentiators.

Email Delivery Services: Until the product's sale in June 2016, the Company offered stand-alone SMTP relay services to customers seeking the highest levels of marketing and transactional email deliverability. Those customers may have in-house design teams, and internal analytics capabilities, so are typically less concerned with some of the "front end" capabilities of a full-service email marketing system. They often send significantly higher volumes of email and are therefore subject to higher risks of having their legitimate opt-in email inadvertently intercepted by SPAM filters. As a result, SMTP relay customers are typically far more concerned with successful email delivery than with the design and creation of email content. For this reason, SMTP's relay services for improving deliverability are typically significantly lower in cost than sending via integrated packages. Until the sale of the product in June 2016, we competed with companies such as SendGrid, Mandrill, JangoMail, Amazon SES and others.

We are part of a constantly evolving and highly competitive marketplace. Some of our competitors have more extensive customer bases and broader customer relationships than we have, and have longer operating histories and greater name recognition than we have. Additionally, some of our current and potential competitors have significantly more financial, technical, marketing and other resources than we have, and are able to devote greater resources to the development, promotion, sale and support of their products and services. Barriers to entry are relatively high in the marketing automation market due to complexity of systems.

Sales and Marketing

We sell our products globally, through our internal sales teams, and to a lesser extent, third party resellers. Before the discontinuation of GraphicMail and the sale of our SMTP email relay product, our products had separate and mostly distinct sales processes, which are described below. We use and rely on our own SharpSpring marketing automation platform to help our business generate leads, convert more leads to sales and monitor the effectiveness of all our marketing campaigns. Our website www.sharpspring.com serves as a lead generation source and we use a variety of other digital marketing tools to attract new customers.

Our SharpSpring product sales process involves targeting customers, completing product demos and advancing customers through our marketing and sales pipeline to conversion using our SharpSpring marketing automation product. Since SharpSpring was launched fairly recently in 2014, brand recognition today is growing, but still fairly limited. Therefore, we are more reliant on outbound marketing and search engine traffic to attract potential leads. Our marketing efforts to date have been nearly 100% focused on digital marketing agencies, and we have had success signing up over 1,100 marketing agency partners as of December 31, 2016. These agencies become customers of ours and are able to resell SharpSpring to their clients, while paying increased fees to us as their client count expands beyond the base license. This allows the agency to provide services and first level support for their clients, which increases their own revenues from the end client and creates a longer-lasting relationship overall between the agency and client. We also sell SharpSpring directly to end-users and have over 270 direct end user customers on the platform. The Company's sales are done primarily through internal resources, but a small number of third-party resellers were also used during 2016.

Since creating the SharpSpring Mail+ product to migrate the GraphicMail customers onto during the middle of 2016, we have spent limited resources marketing and selling SharpSpring Mail+ as a standalone product. During the second half of 2016, we did a small amount of prospecting for new SharpSpring Mail+ clients, and make the product available for demos and free trials for new customers. After the free trial, customers can select either a send plan, which incurs charges based on the number of emails sent through the platform, or a contact plan, which incurs charges based on the number of contacts (or leads) in the system. We intend to continue to devote limited resources to the sales and marketing process for SharpSpring Mail+ as a standalone product in the future.

Prior to its discontinuation in the middle of 2016, our GraphicMail sales and marketing efforts were designed to attract potential customers to our website, enroll them in a free trial, encourage them to engage with our products, convert them to paying customers and retain them as ongoing customers. We employed strategies to acquire customers by using a variety of sources, including online advertising and partner relationships and referrals. We advertised online through pay-per-click advertising with search engines, including Google, Yahoo!, Bing and others. We deployed banner advertising with online advertising networks and other websites likely to be frequented by SMB organizations. Additionally, GraphicMail used a network of third party resellers who distributed and sold GraphicMail in 14 countries. These resellers acted as local sales resources, performed marketing for the product and provided first level support, and received a large portion of the revenue related to sales of GraphicMail through those organizations. The Company discontinued the GraphicMail product and ended any reselling arrangements for GraphicMail with third parties.

Prior to its sale in June 2016, SMTP relay services were sold and leads were largely generated by the SMTP.com website. SMTP stands for "Simple Mail Transfer Protocol", which is the internet protocol by which all email is sent globally. Despite the fact that we did not own the protocol, the SMTP name provided us immediate name recognition and domain context worldwide. In addition, the services we provided may be searched for online as "SMTP", "SMTP relay services", "SMTP services", "SMTP providers", or using similar terms. Our website may have appeared in search engine results for these and other queries in common search engines, such as Google, Yahoo!, Bing, and others. In addition, SMTP purchased online search advertising and other forms of online advertising to drive traffic to the website and referring partners provided us with leads. Referring partners were typically other service providers operating in the email ecosystem, who may provide related products and services that were non-competitive with our own. We paid those third parties between 15% and 30% of the revenue generated from their referrals.

Customers

As of December 31, 2016, we had over 1,400 customers for our SharpSpring product, the majority of which were marketing agencies. Including agency partners, agency clients and direct end user clients, we had over 5,000 businesses using the SharpSpring platform as of December 31, 2016.

As of December 31, 2016, we had over 1,700 customers using our SharpSpring Mail+ product.

The vast majority of our customers are on month-to-month agreements, with a mixture of customers being charged in advance and in arrears. We have a small amount of customers that prepay for longer periods, such as quarterly or annually.

We are not heavily dependent on any one customer or even a few major customers. Our user base is diverse and the largest single customer represents less than 3% of our aggregate revenues. The loss of any one customer would not represent a material loss of sales. A large majority of our SharpSpring customers are marketing agencies who resell the SharpSpring product to their clients. From a client or end user perspective, we do not have any significant industry concentration in our customer base.

Technology & Technology Suppliers

Our SharpSpring product technology was developed internally over the past five years. SharpSpring's key features include web tracking, customer relationship management, call tracking, lead scoring and nurturing, rule-based triggers and notifications and deep analytics to measure ROI. We offer value to our customers by providing integration with industry standard technologies like Salesforce.com and others, and third-party data providers like Zoom Info.

SharpSpring Mail+ is a subset of the SharpSpring technology. During late 2015 and the first half of 2016, we modified SharpSpring to support the SharpSpring Mail+ features and functionality using the existing platform. This involved creating a subset of the technology with more limited features for SharpSpring Mail+.

We decommissioned the GraphicMail product in the middle of 2016. GraphicMail had been developed over the past nine years and consisted of an email editor that customers used to create sharp, professional email campaigns. It had an easy to use interface, integrated with social media channels, offered mobile messaging and included tools to effectively track campaign results. GraphicMail historically utilized Postfix software to assist in spooling emails, which is an open source technology, but began using the SMTP relay service during 2015 as its primary email sending platform.

The Company sold the SMTP relay service in June 2016. The SMTP relay service product used Message Transfer Agent (MTA) technology provided by Message Systems. This software can handle large volumes of email and provides unique features such as adaptive delivery for managing email delivery issues, such as throttling by the ISP's. Facebook, LinkedIn, and other very large email senders employ this same sophisticated software. Typically, our SMTP relay service customers would be too small and spend too little on email to be able to afford this type of sophisticated system on their own. The SMTP solution pooled a large number of customers into our proprietary and scalable system that handled billions of emails. The software was customized to optimize the speed at which email is delivered, and to manage the process of maximizing inbox delivery. The proprietary systems managed how emails are sent, and which IP addresses or pools of IP addresses were used for sending. We were able to control the speed and volume with which emails are released to various ISPs. Another key part of our technological assets were our 12,286 portable IPv4 addresses (which were sold along with the product). We allowed our customers to use our IP addresses to improve the inbox delivery of their email campaigns.

During the period of time before the sale of the SMTP product, we employed Message Systems as the backbone of our sending. During the first half of 2016, we also employed Postfix software for certain functions. PostFix software is open source and has been released under the IBM Public License 1.0, giving us and others rights to freely utilize and modify the software at our discretion and without cost. We operated the software in a clean unmodified state. We developed proprietary extensions that plugged into the PostFix software in an effort to optimize the speed at which email is delivered, and to manage the process of maximizing inbox delivery. Customizations to open source software code generally require developers to make their work available at no cost. Since we developed the software by creating extensions which live outside of the open source software layer, we were not required to offer our products or make our source code available.

Our platforms are hosted in third party data centers on equipment that is mostly leased or rented from the provider. During 2016, these providers included Google Compute, Amazon Web Services, Rackspace, Softlayer, Linode, Hetzner and Sadecehosting, Data Realms, Sprocket Networks, MongoHQ, Microsoft Azure, and others. These data centers use a mixture of biometric access controls, redundant power, environmental controls and secure internet connection points to ensure uptime and data security. The Company continuously monitors our services for availability, performance and security. When necessary we send engineers to these third-party providers' locations to maintain quality control and oversight. We rely on our data center providers to maintain peak operating conditions in their businesses and to quickly address issues related to their service as they arise.

Intellectual Property

The Company does not have any patents, and does not have any patents in progress.

Our trade secrets include our competencies in marketing automation, web tracking, integrations, workflow and email editing.

We registered "SharpSpring" and the related logo and certain other marks as trademarks in the United States and several other jurisdictions.

We are the registered holder of a variety of domestic and international domain names that include "sharpspring", "sharpspringmailplus", "graphicmail" and similar variations.

Regulation of our Business

We must comply with U.S. federal legislation entitled Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, or CAN-SPAM Act, which imposes certain obligations on the senders of commercial emails and specifies penalties for the transmission of commercial email messages that are intended to deceive the recipient as to source or content.

The CAN-SPAM Act's main provisions include:

- prohibiting false or misleading email header information
- prohibiting the use of deceptive subject lines
- ensuring that recipients may, for at least 30 days after an email is sent, opt out of receiving future commercial email messages from the sender, with the opt-out effective within 10 days of the request
- requiring that commercial email be identified as a solicitation or advertisement unless the recipient affirmatively assented to receiving the message
- requiring that the sender include a valid postal address in the email message

In addition, some states have passed laws regulating commercial email practices that are significantly more punitive and difficult to comply with than the CAN-SPAM Act, particularly Utah and Michigan, which have enacted do-not-email registries listing minors who do not wish to receive unsolicited commercial email that markets certain covered content, such as adult or other harmful products. Some portions of these state laws may not be preempted by the CAN-SPAM Act. Additionally, some foreign jurisdictions, such as Australia, Canada and the European Union, have also enacted laws that regulate sending email, some of which are more restrictive than the CAN-SPAM Act. For example, some foreign laws prohibit sending unsolicited email unless the recipient has provided the sender advance consent to receipt of such email, or in other words has "opted-in" to receiving it.

The ability of our customers' constituents to opt out of receiving commercial emails may minimize the effectiveness of our email marketing product. Moreover, non-compliance with the CAN-SPAM Act carries significant financial penalties. If we were found to be in violation of the CAN-SPAM Act, applicable state laws not preempted by the CAN-SPAM Act, or foreign laws regulating the distribution of commercial email, whether as a result of violations by our customers or if we were deemed to be directly subject to and in violation of these requirements, we could be required to pay penalties, which would adversely affect our financial performance and significantly harm our business. We also may be required to change one or more aspects of the way we operate our business, which could impair our ability to attract and retain customers or increase our operating costs.

As internet commerce continues to evolve, increasing regulation by federal, state or foreign governments becomes more likely. Our business could be negatively impacted by the application of existing laws and regulations or the enactment of new laws applicable to email communications. The cost to comply with such laws or regulations could be significant and would increase our operating expenses, and we may be unable to pass along those costs to our customers in the form of increased subscription fees. In addition, federal, state and foreign governmental or regulatory agencies may decide to impose taxes on services provided over the Internet or via email. Such taxes could discourage the use of the Internet and email as a means of commercial marketing and communications, which would adversely affect the viability of our services.

Additionally, certain aspects of how our customers utilize our platform are subject to regulations in the United States, European Union and elsewhere. In recent years, U.S. and European lawmakers and regulators have expressed concern over the use of third-party cookies or web beacons for online behavioral advertising, and legislation adopted recently in the European Union requires informed consent for the placement of a cookie on a user's device. Regulation of cookies and web beacons may lead to restrictions on our activities, such as efforts to understand users' Internet usage. New and expanding "Do Not Track" regulations have recently been enacted or proposed that protect users' right to choose whether or not to be tracked online. These regulations seek, among other things, to allow end users to have greater control over the use of private information collected online, to forbid the collection or use of online information, to demand a business to comply with their choice to opt out of such collection or use, and to place limits upon the disclosure of information to third party websites. These policies could have a significant impact on the operation of our marketing automation platform and could impair our attractiveness to customers, which would harm our business.

Customers and potential customers in the healthcare, financial services and other industries are subject to substantial regulation regarding their collection, use and protection of data and may be the subject of further regulation in the future. Accordingly, these laws or significant new laws or regulations or changes in, or repeals of, existing laws, regulations or governmental policy may change the way these customers do business and may require us to implement additional features or offer additional contractual terms to satisfy customer and regulatory requirements, or could cause the demand for and sales of our marketing automation platform to decrease and adversely impact our financial results.

Employees

As of March 17, 2017, we have approximately 144 people supporting our operations, including approximately 140 employees and 4 contractors. Nearly all of our employees and contractors devote their full effort to the company. Our resources include 38 sales and marketing resources, 29 development resources, 19 general & administrative resources and 58 customer services, network and support resources.

None of our employees are covered by collective bargaining agreements.

We believe that our future success will depend in part on our continued ability to attract, hire or acquire and retain qualified employees and contractors. There can be no assurance that we will be able to attract and retain such resources. If we are unsuccessful in managing the timely delivery of these services our business could be adversely affected. We believe we have good relations with our resources.

Properties

Our corporate headquarters is a leased facility located in Gainesville, FL. Additionally, we lease a satellite office in Kiev, Ukraine.

Financial Information About Segments

The Company operates as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is regularly evaluated by the chief operating decision maker ("CODM"), which is the Company's chief executive officer, in deciding how to allocate resources and assess performance. The Company's CODM evaluates the Company's financial information and resources and assess the performance of these resources on a consolidated basis. Since the Company operates in one operating segment, all required financial segment information can be found in the consolidated financial statements.

Corporate Information

SharpSpring, Inc. is a Delaware corporation. Its wholly owned subsidiaries consist of (i) SharpSpring Technologies, Inc., a Delaware corporation; (ii) InterInbox SA, a Swiss corporation; (iii) ERNEPH 2012A (Pty) Ltd. dba ISMS, a South African limited company; (iv) ERNEPH 2012B (Pty) Ltd. dba GraphicMail South Africa, a South African limited company; (v) Quattro Hosting LLC, a Delaware limited liability company; (vi) SMTP Holdings S.a.r.l., a Luxembourg S.a.r.l.; and (vii) InterCloud Ltd, a Gibraltar Limited Company.

Our corporate headquarters is located at 550 SW 2nd Avenue, Gainesville, FL 32601. Our telephone number is 888-428-9605. Our corporate website is www.sharpspring.com. The information on our website is not incorporated herein by reference and is not part of this Form 10-K Annual Report. Also, this report includes the trade names of other companies. Unless specifically stated otherwise, the use or display by us of such other parties' names and trade names in this report is not intended to and does not imply a relationship with, or endorsement or sponsorship of us by, any of these other parties.

ITEM 1A. RISK FACTORS

Risks Related To Our Business

The majority of our products and services are sold pursuant to short-term subscription agreements, and if our customers elect not to renew these agreements, our revenues may decrease.

Typically, our products and services are sold pursuant to short-term subscription agreements, which are generally one month to one year in length, with no obligation to renew these agreements. Our renewal rates may decline due to a variety of factors, including the products and services and prices offered by our competitors, new technologies offered by others, consolidation in our customer base or if some of our customers cease their operations. If our renewal rates are low or decline for any reason, or if customers renew on less favorable terms, our revenues may decrease, which could adversely affect our stock price.

We may not be able to scale our business quickly enough to meet our customers' growing needs, and if we are not able to grow efficiently, our operating results could be harmed.

As usage of our marketing software grows and as customers use our solutions for more advanced relationship marketing programs, we will need to devote additional resources to improving our application architecture, integrating with third-party systems, and maintaining infrastructure performance. In addition, we will need to appropriately scale our internal business systems and our services organization, including customer support and professional services, to serve our growing customer base, particularly as our customer demographics expand over time. Any failure of or delay in these efforts could cause impaired system performance and reduced customer satisfaction. These issues could reduce the attractiveness of our marketing software to customers, resulting in decreased sales to new customers, lower renewal rates by existing customers, the issuance of service credits, or requested refunds, which could adversely affect our revenue growth and harm our reputation. Even if we are able to upgrade our systems and expand our staff, any such expansion will be expensive and complex, requiring management time and attention. We could also face inefficiencies or operational failures as a result of our efforts to scale our infrastructure. Moreover, there are inherent risks associated with upgrading, improving and expanding our information technology systems. We cannot be sure that the expansion and improvements to our infrastructure and systems will be fully or effectively implemented on a timely basis, if at all. These efforts may reduce revenue and our margins and adversely affect our financial results.

If we fail to enhance our existing products and services or develop new products and services, our products and services may become obsolete or less competitive and we could lose customers.

If we are unable to enhance our existing products and services or develop new products and services that keep pace with rapid technological developments and meet our customers' needs, our business will be harmed. Creating and designing such enhancements and new products entail significant technical and business risks and require substantial expenditures and lead-time, and there is no guarantee that such enhancements and new products will be completed in a timely fashion. Nor is there any guarantee that any new service offerings will gain acceptance among our customers or by the broader market. For example, our existing customers may not view any new service as complementary to our service offerings and therefore decide not to purchase such service. If we cannot enhance our existing products and services or develop new products or if we are not successful in selling such enhancements and new products to our customers, we could lose customers or have difficulty attracting new customers, which would adversely impact our financial performance.

If we are unable to attract new customers and retain existing customers on a cost-effective basis, our business and results of operations will be adversely affected.

To succeed, we must continue to attract and retain a large number of customers on a cost-effective basis, many of whom have not previously used the types of products and services that we offer. Our sales process involves targeting customers, completing product demos and advancing customers through our marketing and sales pipeline to conversion using our SharpSpring marketing automation product, in addition to relying on outbound marketing and search engine traffic to attract potential leads. We rely on a variety of methods to attract new customers, such as outbound emails, hosting events, paying providers of online services, search engines, directories and other websites to provide content, advertising banners and other links that direct customers to our website. If we are unable to use any of our current marketing initiatives or the cost of such initiatives were to significantly increase or such initiatives or our efforts to satisfy our existing customers are not successful, we may not be able to attract new customers or retain existing customers on a cost-effective basis and, as a result, our revenue and results of operations would be adversely affected.

If we fail to develop our brands cost-effectively, our business may be adversely affected.

Successful promotion of our brands will depend largely on the effectiveness of our marketing efforts and on our ability to provide reliable and useful services at competitive prices. Brand promotion activities may not yield increased revenue, and even if they do, any increased revenue may not offset the expenses we incur in building our brands. If we fail to successfully promote and maintain our brands, or incur substantial expenses in an unsuccessful attempt to promote and maintain our brands, we may fail to attract enough new customers or retain our existing customers to the extent necessary to realize a sufficient return on our brand-building efforts, and our business and results of operations could suffer.

Email communications is a key component of our product. If the delivery of our customers' emails is limited or blocked, our product's capabilities would be severely limited and customers may cancel their accounts.

Internet Service Providers (ISP) can block emails from reaching their users. Although we work with one of the premier email delivery providers, recent releases of ISP software and the implementation of stringent new policies by ISPs make it more difficult to deliver our customers' emails. We continually monitor and improve our own technology and work closely with ISPs to maintain our deliverability rates. If ISPs materially limit or halt the delivery of our customers' emails, or if we fail to deliver our customers' emails in a manner compatible with ISPs' email handling or authentication technologies, then the fees we charge for our email marketing product may not be accepted by the market, and customers may cancel their accounts.

Following the migration of the GraphicMail customer base to our SharpSpring Mail+ product, we have experienced significant attrition and a material reduction in revenue. We may experience continued significant customer attrition, which could further impact our revenues, cash balance and future results.

During the first half of 2016, we migrated all of our GraphicMail customers over to our SharpSpring Mail+ product. Prior to, during and subsequent to the migration, we experienced significant attrition in our GraphicMail customer base, and revenues have been significantly reduced. We may continue to experience heavier attrition in this customer base. Any decrease in our revenues could negatively impact our stock price.

If we pursue future acquisitions, our inability to successfully acquire and integrate other businesses, assets, products or technologies could harm our operating results.

We may in the future evaluate and pursue acquisitions and strategic investments in businesses, products or technologies that we believe could complement or expand our existing solutions, expand our client base and operations worldwide, enhance our technical capabilities or otherwise offer growth or cost-saving opportunities. From time to time, we may enter into letters of intent with companies with which we are negotiating potential acquisitions or investments or as to which we are conducting due diligence. Although we are currently not a party to any binding definitive agreement with respect to potential investments in, or acquisitions of, complementary businesses, products or technologies, we may enter into these types of arrangements in the future, which could materially decrease the amount of our available cash or require us to seek additional equity or debt financing. We have limited experience in successfully acquiring and integrating businesses, products and technologies. We may not be successful in negotiating the terms of any potential acquisition, conducting thorough due diligence, financing the acquisition or effectively integrating the acquired business, product or technology into our existing business and operations. Our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues related to intellectual property, product quality or product architecture, regulatory compliance practices, revenue recognition or other accounting practices, or employee or customer issues.

Additionally, in connection with any acquisitions we complete, we may not achieve the synergies or other benefits we expected to achieve, and we may incur write-downs, impairment charges or unforeseen liabilities that could negatively affect our operating results or financial position or could otherwise harm our business. If we finance acquisitions using existing cash, the reduction of our available cash could cause us to face liquidity issues or cause other unanticipated problems in the future. If we finance acquisitions by issuing convertible debt or equity securities, the ownership interest of our existing stockholders may be diluted, which could adversely affect the market price of our stock. Further, contemplating or completing an acquisition and integrating an acquired business, product or technology could divert management and employee time and resources from other matters.

Our international operations subject us to additional risks and uncertainties.

Our international operations present unique challenges and risks to our Company. Compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business in international jurisdictions and could interfere with our ability to offer our products and services to one or more countries or expose us or our employees to fines and penalties. These laws and regulations include, but are not limited to, tax laws, data privacy and filtering requirements, U.S. laws such as the Foreign Corrupt Practices Act, and local laws prohibiting corrupt payments to governmental officials. Violations of these laws and regulations could result in monetary damages, criminal sanctions against us, our officers, or our employees, and prohibitions on the conduct of our business. Our international operations also subject us to additional foreign currency exchange rate risks and will require additional management attention and resources. Our international operations subject us to other inherent risks, including, but not limited to:

- the impact of recessions in economies outside of the United States
- changes in and differences between regulatory requirements between countries
- U.S. and foreign export restrictions, including export controls relating to encryption technologies
- anti-SPAM laws and other laws that may differ materially from US laws
- reduced protection for and enforcement of intellectual property rights in some countries
- potentially adverse tax consequences
- difficulties and costs of staffing and managing foreign operations
- political and economic instability
- international conflicts, wars or terrorism
- tariffs and other trade barriers
- seasonal reductions in business activity

Our failure to address these risks adequately could materially and adversely affect our business, revenue, results of operations, cash flows and financial condition.

We could be materially affected by the fluctuations of the U.S. Dollar against the Euro, Swiss Franc, South African Rand or British Pound.

In our fourth quarter of 2016, approximately 82% of our revenues are currently generated in U.S. Dollars, while approximately 18% of our revenues are denominated in other currencies including the Euro, Swiss Franc, South African Rand and British Pound. Our costs are generally incurred in similar currencies. Currency exchange rates can fluctuate dramatically, which will impact the amount of revenue we will record when translated to U.S. Dollars and will impact the amount of costs that we incur when translated to U.S. Dollars. Although our cost currencies are generally aligned to our revenue currencies, variances exist between the rate we incur costs in each currency compared to the revenue. Therefore, changes to currency rates may dramatically impact profitability.

If we do not or cannot maintain the compatibility of our marketing software with third-party applications that our customers use in their businesses, our revenue will decline.

The functionality and popularity of our marketing software depends, in part, on our ability to integrate our solutions with third-party applications and platforms, including CRM, event management, e-commerce, call center, and social media sites that our customers use and from which they obtain data. Third-party providers of applications and APIs may change the features of their applications and platforms, restrict our access to their applications and platforms or alter the terms governing use of their applications and APIs and access to those applications and platforms in an adverse manner. Such changes could functionally limit or terminate our ability to use these third-party applications and platforms in conjunction with our solution, which could negatively impact our offerings and harm our business. If we fail to integrate our software with new third-party applications and platforms that our customers use for marketing purposes, we may not be able to offer the functionality that our customers need, which would negatively impact our ability to generate revenue and adversely impact our business.

The market in which we participate is competitive and, if we do not compete effectively, our operating results could be harmed.

Our principal competitors include marketing automation companies like HubSpot, Marketo, Pardot and Act-On, as well as larger companies such as Amazon.com, and the in-house information technology capabilities of prospective customers. Competition could result in reduced sales, reduced margins or the failure of our products to achieve or maintain more widespread market acceptance, any of which could harm our business.

Our current and potential competitors may have significantly more financial, technical, marketing and other resources than we do and may be able to devote greater resources to the development, promotion, sale and support of their products. Our current and potential competitors may have more extensive customer bases and broader customer relationships than we have. In addition, these companies may have longer operating histories and greater name recognition than we have and may be able to bundle products with other products that have gained widespread market acceptance. These competitors may be better able to respond quickly to new technologies and to undertake more extensive marketing campaigns. If we are unable to compete with such companies, the demand for our products could substantially decline.

Our business is substantially dependent on continued demand for marketing and email technology and any decrease in demand could cause us to suffer a decline in revenues and profitability.

We derive, and expect to continue to derive, substantially all of our revenue from organizations, including marketing agencies and small and medium size businesses, associations and non-profits. As a result, widespread acceptance of marketing technology among small and medium size organizations is critical to our future growth and success. The overall market for marketing automation technology is relatively new and still evolving, and small organizations have generally been slower than larger organizations to adopt email marketing as part of their marketing mix. There is no certainty regarding how or whether this market will develop, or whether it will experience any significant contractions. Our ability to attract and retain customers will depend in part on our ability to make marketing communications convenient, effective and affordable. If small and medium size organizations determine that marketing technology and communication does not sufficiently benefit them, existing customers may cancel their accounts and potential customers may decide not to utilize our services.

We are a small public company and the requirements of being a public company are a strain on our systems and resources, are a diversion to management's attention and are costly.

As a public company, we are subject to the reporting requirements of the Securities Exchange Act of 1934 (Exchange Act) the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley Act), the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), and the rules and regulations of The NASDAQ Stock Market. The requirements of these rules and regulations increase our legal, accounting and financial compliance costs, make some activities more difficult, time-consuming and costly and may also place undue strain on our personnel, systems and resources.

The Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and operating results. The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. We are continuing the costly process of implementing and testing our systems to report our results as a public company, to continue to manage our growth and to implement internal controls. We are and will continue to be required to implement and maintain various other control and business systems related to our equity, finance, treasury, information technology, other recordkeeping systems and other operations. As a result of this implementation and maintenance, management's attention may be diverted from other business concerns, which could adversely affect our business.

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

In addition, we expect these laws, rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to incur substantial costs to maintain appropriate levels of coverage. These factors could also make it more difficult for us to attract and retain qualified members of our board of directors, particularly to serve on our audit committee, and qualified executive officers.

As a result of being a public company, our business and financial condition has become more visible, which we believe may result in threatened or actual litigation, including by competitors and other third parties. If such claims are successful, our business and operating results could be adversely affected, and even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the time and resources of our management and adversely affect our business and operating results.

Risks Related To Our Management

If we fail to retain our key personnel, we may not be able to achieve our anticipated level of growth and our business could suffer.

Our future depends, in part, on our ability to attract and retain key personnel. Our future also depends on the continued efforts and abilities of our executive officers, including our Chief Executive Officer and other key personnel, each of whom would be difficult to replace. In particular, Richard Carlson, our Chief Executive Officer and President and Travis Whitton, our Chief Technology Officer, are critical to the Company's strategic direction and product development process. The loss of the services of Messrs. Carlson, Whitton or other key personnel, and the process to replace any of our key personnel, would involve significant time and expense and may significantly delay or prevent the achievement of our business objectives. We currently do not maintain key person life insurance on any of our executives. Accordingly, the loss of the services of any of these persons would adversely affect our business.

Our anticipated growth in our operations could place a significant strain on our management team and our administrative, operational and financial reporting infrastructure.

Our success will depend in part on the ability of our management team to effectively manage our growth in our operations. To do so, we believe we will need to continue to hire, train and manage new employees as needed. If our new hires perform poorly, or if we are unsuccessful in hiring, training, managing and integrating these new employees, or if we are not successful in retaining our existing employees, our business may be harmed. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational and financial controls and update our reporting procedures and systems. The expected addition of new employees and the capital investments that we anticipate will be necessary to manage our anticipated growth will increase our cost base, which will make it more difficult for us to offset any future revenue shortfalls by reducing expenses in the short term. If we fail to successfully manage our anticipated growth, our business operations could be adversely affected.

Our officers and directors own a significant interest in our voting stock and it may be difficult for investors to overcome this influence in future shareholder votes, which could result in decisions adverse to our general stockholders.

As of December 31, 2016, our officers and directors, in the aggregate, beneficially own approximately or have the right to vote approximately 36% of our outstanding common shares on a fully diluted basis. As a result, these stockholders have significant influence over all matters submitted to our stockholders for approval including:

- election of our board of directors
- removal of any of our directors
- amendment of our Articles of Incorporation or By-laws
- adoption of measures that could delay or prevent a change in control or impede a merger, takeover or other business combination involving us

As a result of their ownership and positions, our officers and directors collectively are able to influence matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. The interests of our officers may differ from the interests of the other stockholders, and they may influence decisions with which the other stockholders may not agree. Such decisions may be detrimental to our business plan and/or operations and they may cause our business to fail in which case you may lose your entire investment.

Substantial future sales of shares of our common stock by large existing stockholders could depress the market price of our common stock.

The market price for our common stock could decline as a result of the sale of substantial amounts of our common stock, particularly sales by our chairman, directors, executive officers and significant stockholders, a large number of shares of our common stock becoming available for sale or the perception in the market that holders of a large number of shares intend to sell their shares.

A material weakness in internal controls may remain undetected for a longer period because of our Company's exemption from the auditor attestation requirements under Section 404(b) of Sarbanes-Oxley.

Our annual report does not include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's attestation in its annual report. As a result, a material weakness in our internal controls may remain undetected for a longer period.

Risks Related To Our Systems

Our customers' use of our products to transmit negative messages or website links to harmful applications could damage our reputation, and we may face liability for unauthorized, inaccurate or fraudulent information distributed via our services.

Although it is against our terms and conditions, our customers could use our email servers to transmit negative messages or website links to harmful applications, reproduce and distribute copyrighted material without permission, or report inaccurate or fraudulent data or information. Any such use of our products could damage our reputation and we could face claims for damages, copyright or trademark infringement, defamation, negligence or fraud. Moreover, our customers' promotion of their products and services through our email marketing product may not comply with federal, state and foreign laws. We cannot predict whether our role in facilitating these activities would expose us to liability under these laws.

Even if claims asserted against us do not result in liability, we may incur substantial costs in investigating and defending such claims. If we are found liable for our customers' activities, we could be required to pay fines or penalties, redesign business methods or otherwise expend resources to remedy any damages caused by such actions and to avoid future liability.

Various private spam blacklists have in the past interfered with, and may in the future interfere with, the effectiveness of our products and our ability to conduct business.

Our customers rely on email to communicate with their constituents and we depend on email to market to and communicate with our customers. Various private entities attempt to regulate the use of email for commercial solicitation. These entities often advocate standards of conduct or practice that significantly exceed current legal requirements and classify certain email solicitations that comply with current legal requirements as spam. Some of these entities maintain "blacklists" of companies and individuals, and the websites, ISPs and internet protocol addresses associated with those entities or individuals that do not adhere to those standards of conduct or practices for commercial email solicitations that the blacklisting entity believes are appropriate. If a company's internet protocol addresses are listed by a blacklisting entity, emails sent from those addresses may be blocked if they are sent to any Internet domain or Internet address that subscribes to the blacklisting entity's service or purchases its blacklist. Although we have not owned the internet protocol addresses we utilize since the sale of the SMTP product, blacklisting of the internet protocol addresses that the company uses could materially impact our sending ability.

Our facilities and systems are vulnerable to natural disasters and other unexpected events and any of these events could result in an interruption of our ability to execute clients' email campaigns.

While we have established contingency plans for certain potential disasters, it is possible that an unexpected disaster may occur, which could interrupt our ability to provide services. We also depend on the efficient and uninterrupted operations of our third-party data centers and hardware systems. The data centers and hardware systems are vulnerable to damage from earthquakes, tornados, hurricanes, fire, floods, power loss, telecommunications failures and similar events. If any of these events results in damage to our facilities or third-party data centers or systems, we may be unable to operate our services until the damage is repaired, and may accordingly lose clients and revenues. In addition, subject to applicable insurance coverage, we may incur substantial costs in repairing any damage.

System failures could reduce the attractiveness of our service offerings, which could cause us to suffer a decline in revenues and profitability.

The satisfactory performance, reliability and availability of the technology and the underlying network infrastructure are critical to our operations, level of client service, reputation and ability to attract and retain clients. We have experienced periodic interruptions, affecting all or a portion of our systems, which we believe will continue to occur from time to time. We are not aware of any loss of customers due to material service interruptions. However, any systems damage or interruption that impairs our ability to accept and fill client orders could result in an immediate loss of revenue to us, and could cause some clients to purchase services offered by our competitors. In addition, frequent systems failures could harm our reputation. Some factors that could lead to interruptions in customer service include: operator negligence; improper operation by, or supervision of, employees; physical and electronic break-ins; misappropriation; computer viruses and similar events; power loss; computer systems failures; and Internet and telecommunications failures. We do not carry sufficient business interruption insurance to fully compensate us for losses that may occur.

Any significant disruption in service on our websites or in our computer systems, or in our customer support services, could reduce the attractiveness of our products and result in a loss of customers.

The satisfactory performance, reliability and availability of our technology and our underlying network infrastructure are critical to our operations, level of customer service, reputation and ability to attract new customers and retain existing customers. Our production system hardware and the disaster recovery operations for our production system hardware are co-located in third-party hosting facilities. None of the companies who host our systems guarantee that our customers' access to our products will be uninterrupted, error-free or secure. Our operations depend on their ability to protect their and our systems in their facilities against damage or interruption from natural disasters, power or telecommunications failures, air quality, temperature, humidity and other environmental concerns, computer viruses or other attempts to harm our systems, criminal acts and similar events. In the event that our arrangements with third-party data centers are terminated, or there is a lapse of service or damage to their facilities, we could experience interruptions in our service as well as delays and additional expense in arranging new facilities. Any interruptions or delays in access to our services, whether as a result of a third-party error, our own error, natural disasters or security breaches, whether accidental or willful, could harm our relationships with customers and our reputation. Also, in the event of damage or interruption, our insurance policies may not adequately compensate us for any losses that we may incur. These factors could damage our brand and reputation, divert our employees' attention, reduce our revenue, subject us to liability and cause customers to cancel their accounts, any of which could adversely affect our business, financial condition and results of operations.

We rely on third-party computer hardware and software that may be difficult to replace or that could cause errors or failures of our service, which could cause us to suffer a decline in revenues and profitability.

We rely on computer hardware purchased and software licensed from third parties in order to offer our products, including software from Google, Microsoft, Nginx, Inc., MongoDB, Inc, The MariaDB Foundation and other open source vendors, hardware from such large vendors as Apple, International Business Machines Corporation, Dell Computer Corporation, Sun Microsystems, Inc. and EMC Corporation and hosting services from Amazon Web Services, Rackspace, Softlayer, Linode, Google Compute, Hetzner, Sadecehosting, Data Realms, Sprocket Networks, MongoHQ, Microsoft Azure, and others as well. This hardware and software may not continue to be available on commercially reasonable terms, or at all. If we lose the right to use any of this hardware or software or such hardware or software malfunctions, our customers could experience delays or be unable to access our services until we can obtain and integrate equivalent technology or repair the cause of the malfunctioning hardware or software. Any delays or failures associated with our services could upset our customers and harm our business.

If we are unable to protect the confidentiality of our unpatented proprietary information, processes and know-how and our trade secrets, the value of our technology and services could be adversely affected.

We rely upon unpatented proprietary technology, processes and know-how and trade secrets. Although we try to protect this information in part by executing confidentiality agreements with our employees, consultants and third parties, such agreements may offer only limited protection and may be breached. Any unauthorized disclosure or dissemination of our proprietary technology, processes and know-how or our trade secrets, whether by breach of a confidentiality agreement or otherwise, may cause irreparable harm to our business, and we may not have adequate remedies for any such breach. In addition, our trade secrets may otherwise be independently developed by our competitors or other third parties. If we are unable to protect the confidentiality of our proprietary information, processes and know-how or our trade secrets are disclosed, the value of our technology and services could be adversely affected, which could negatively impact our business, financial condition and results of operations.

Our use of open source software could impose limitations on our ability to commercialize our products, which could cause us to suffer a decline in revenues and profitability.

Customizations to open source software code generally require developers to make their work available at no cost. Since we have created our software by developing extensions which plug into open source software without modifying the open source code, we do not believe there is a risk we could be required to offer our products or make our source code available. Although we monitor our use of open source software closely, the terms of many open source licenses to which we are subject have not been interpreted by United States or foreign courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to commercialize our products. In such event, we could be required to seek licenses from third parties in order to continue offering our products, to re-engineer our products or to discontinue sales of our products, or to release our software code under the terms of an open source license, any of which could materially adversely affect our business.

Given the nature of open source software, there is also a risk that third parties may assert copyright and other intellectual property infringement claims against us based on our use of certain open source software programs. The risks associated with intellectual property infringement claims are discussed immediately below.

Because we have not filed for patent protection of our technologies, we face the risk of our technologies not being adequately protected.

We do not currently have any patents for our proprietary technology and do not have plans to file for patent protection currently. If we fail to obtain patents on our technologies and processes, we may be unable to adequately protect our intellectual property, especially if the designs and materials used in our products are replicated by our competitors. Further, even if we file for patent protection, there is no assurance that it will be approved by the US Patent and Trademark Office.

If a third party asserts that we are infringing its intellectual property, whether successful or not, it could subject us to costly and time-consuming litigation or require us to obtain expensive licenses, and our business may be adversely affected.

The software and Internet industries are characterized by the existence of a large number of patents, trademarks and copyrights and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. Third parties may assert patent and other intellectual property infringement claims against us in the form of lawsuits, letters or other forms of communication. These claims, whether or not successful, could:

- divert management's attention;
- result in costly and time-consuming litigation;
- require us to enter into royalty or licensing agreements, which may not be available on acceptable terms, or at all;
- in the case of open source software-related claims, require us to release our software code under the terms of an open source license; or
- require us to redesign our software and services to avoid infringement.

As a result, any third-party intellectual property claims against us could increase our expenses and adversely affect our business. In addition, many of our agreements with our channel partners require us to indemnify them for third-party intellectual property infringement claims, which would increase the cost to us resulting from an adverse ruling on any such claim. Even if we have not infringed any third parties' intellectual property rights, we cannot be sure our legal defenses will be successful, and even if we are successful in defending against such claims, our legal defense could require significant financial resources and management time. Finally, if a third party successfully asserts a claim that our products infringe its proprietary rights, royalty or licensing agreements might not be available on terms we find acceptable or at all and we may be required to pay significant monetary damages to such third party.

If the security of our customers' confidential information stored in our systems is breached or otherwise subjected to unauthorized access, our reputation may be severely harmed, we may be exposed to liability and we may lose the ability to offer our customers a credit card payment option.

Our system stores our customers' proprietary email distribution lists, credit card information and other critical data. Any accidental or willful security breaches or other unauthorized access could expose us to liability for the loss of such information, adverse regulatory action by federal and state governments, time-consuming and expensive litigation and other possible liabilities as well as negative publicity, which could severely damage our reputation. If security measures are breached because of third-party action, employee error, malfeasance or otherwise, or if design flaws in our software are exposed and exploited, and, as a result, a third party obtains unauthorized access to any of our customers' data, our relationships with our customers will be severely damaged, and we could incur significant liability. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until they are launched against a target, we and our third-party hosting facilities may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, many states have enacted laws requiring companies to notify individuals of data security breaches involving their personal data. These mandatory disclosures regarding a security breach often lead to widespread negative publicity, which may cause our customers to lose confidence in the effectiveness of our data security measures. Any security breach, whether actual or perceived, would harm our reputation, and we could lose customers and fail to acquire new customers.

If we fail to maintain our compliance with the data protection policy documentation standards adopted by the major credit card issuers, we could lose our ability to offer our customers a credit card payment option. Any loss of our ability to offer our customers a credit card payment option would make our products less attractive to many small organizations by negatively impacting our customer experience and significantly increasing our administrative costs related to customer payment processing.

We may be the subjected of intentional cyber disruptions and attacks.

We expect to be an ongoing target of attacks specifically designed to impede the performance of our products. Experienced computer programmers, or hackers, may attempt to penetrate our network security or the security of our data centers and IT environments. These hackers, or others, which may include our employees or vendors, may cause interruptions of our services. Although we continually seek to improve our countermeasures to prevent and detect such incidents, if these efforts are not successful, our business operations, and those of our customers, could be adversely affected, losses or theft of data could occur, our reputation and future sales could be harmed, governmental regulatory action or litigation could be commenced against us and our business, financial condition, operating results and cash flow could be materially adversely affected.

Risks Related To Our Industry

Existing federal, state and foreign laws regulate Internet tracking software, the senders of commercial emails and text messages, website owners and other activities, and could impact the use of our marketing tools and potentially subject us to regulatory enforcement or private litigation.

Certain aspects of how our customers utilize our marketing tools are subject to regulations in the United States, European Union and elsewhere. New and expanding “Do Not Track” regulations have recently been enacted or proposed that protect users’ right to choose whether or not to be tracked online. These regulations seek, among other things, to allow consumers to have greater control over the use of private information collected online, to forbid the collection or use of online information, to demand a business to comply with their choice to opt out of such collection or use, and to place limits upon the disclosure of information to third party websites. These policies could have a significant impact on the operation of our marketing software and could impair our attractiveness to customers, which would harm our business.

Customers and potential customers in the healthcare, financial services and other industries are subject to substantial regulation regarding their collection, use and protection of data and may be the subject of further regulation in the future. Accordingly, these laws or significant new laws or regulations or changes in, or repeals of, existing laws, regulations or governmental policy may change the way these customers do business and may require us to implement additional features or offer additional contractual terms to satisfy customer and regulatory requirements, or could cause the demand for and sales of our marketing software to decrease and adversely impact our financial results.

In addition, U.S., state and foreign jurisdictions are considering and may in the future enact legislation or laws restricting the ability to conduct marketing activities in mobile, social and web channels. Any of the foregoing existing or future restrictions could require us to change one or more aspects of the way we operate our business, which could impair our ability to attract and retain customers, or increase our operating costs or otherwise harm our business. We may be unable to pass along those costs to our customers in the form of increased subscription fees.

While these laws and regulations generally govern our customers’ use of our marketing tools, we may be subject to certain laws as a data processor on behalf of, or as a business associate of, our customers. For example, these laws and regulations governing the collection, use and disclosure of personal information include, in the United States, rules and regulations promulgated under the authority of the Federal Trade Commission, the Health Insurance Portability and Accountability Act of 1996, the Gramm-Leach-Bliley Act of 1999 and state breach notification laws, and internationally, the Data Protection Directive in the European Union and the Federal Data Protection Act in Germany. If we were found to be in violation of any of these laws or regulations as a result of government enforcement or private litigation, we could be subjected to civil and criminal sanctions, including both monetary fines and injunctive action that could force us to change our business practices, all of which could adversely affect our financial performance and significantly harm our reputation and our business.

Privacy concerns and consumers' acceptance of Internet behavior tracking may limit the applicability, use and adoption of our marketing software.

Privacy concerns may cause consumers to resist providing the personal data necessary to allow our customers to use our services effectively. We have implemented various features intended to enable our customers to better protect consumer privacy, but these measures may not alleviate all potential privacy concerns and threats. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our services in certain industries. In addition to government activity, privacy advocacy groups and the technology and other industries are considering various new, additional or different self-regulatory standards that may place additional burdens on us. There are numerous lawsuits in process against various technology companies that collect and use personal information. If those lawsuits are successful, it could impact the way we conduct our business and adversely affect our financial results. The costs of compliance with, and other burdens imposed by, the foregoing laws, regulations, policies and actions may limit the use and adoption of our cloud-based marketing software and reduce overall demand for it, or lead to significant fines, penalties or liabilities for any noncompliance or loss of any such action.

Evolving regulations concerning data privacy may restrict our customers' ability to solicit, collect, process and use data necessary to conduct email campaigns or to analyze the results or may increase their costs, which could harm our business.

Federal, state and foreign governments have enacted, and may in the future enact, laws and regulations concerning the solicitation, collection, processing or use of consumers' personal information. Such laws and regulations may require companies to implement privacy and security policies, permit users to access, correct and delete personal information stored or maintained by such companies, inform individuals of security breaches that affect their personal information, and, in some cases, obtain individuals' consent to use personal information for certain purposes. Other proposed legislation could, if enacted, prohibit the use of certain technologies that track individuals' activities on web pages or that record when individuals click through to an Internet address contained in an email message. Such laws and regulations could restrict our customers' ability to collect and use email addresses, page viewing data, and personal information, which may reduce demand for our products. They may also negatively impact our ability to effectively market our products.

The growth of the marketing automation market depends partially on the continued growth and effectiveness of anti-spam products, which may be insufficient to enable us to offer our services at a profit.

Adoption and retention of email as a communications medium depends on the ability to prevent junk mail, or "spam," from overwhelming a subscriber's electronic mailbox. In recent years, many companies have evolved to address this issue and filter unwanted messages before they reach customers' mailboxes. In response, spammers have become more sophisticated and have also begun using junk messages as a means for fraud. Email protection companies in turn have evolved to address this new threat. However, if their products fail to be effective against spam, adoption of email as a communications tool will decline, which would adversely affect the market for our services.

Another economic downturn could negatively affect the business sector, which may cause our customers to terminate existing accounts with us or cause potential customers to fail to purchase our products, resulting in a decrease in our revenue and impairing our ability to operate profitably.

Our email services are designed specifically for small and medium size organizations, including small and medium size businesses, associations and non-profits that frequently have limited budgets and may be more likely to be significantly affected by economic downturns than their larger, more established counterparts. Small organizations may choose to spend the limited funds that they have on items other than our products and may experience higher failure rates. Moreover, if small organizations experience economic hardship, they may be unwilling or unable to expend resources on marketing, including email marketing, which would negatively affect the overall demand for our products, increase customer attrition and could cause our revenue to decline. In addition, we have limited experience operating our business during an economic downturn. Accordingly, we do not know if our current business model will continue to operate effectively during an economic downturn. Furthermore, we are unable to predict the likely duration and severity of potential adverse economic conditions in the U.S. and other countries, but the longer the duration the greater risks we face in operating our business. There can be no assurance, therefore, that worsening economic conditions, or a prolonged or recurring recession, will not have a significant adverse impact on our operating and financial results.

U.S. federal legislation entitled Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 imposes certain obligations on the senders of commercial emails, which could minimize the effectiveness of our email marketing product, and establishes financial penalties for non-compliance, which could increase the costs of our business.

The Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, or CAN-SPAM Act, establishes certain requirements for commercial email messages and specifies penalties for the transmission of commercial email messages that are intended to deceive the recipient as to source or content. The CAN-SPAM Act, among other things, obligates the sender of commercial emails to provide recipients with the ability to opt out of receiving future emails from the sender. In addition, some states have passed laws regulating commercial email practices that are significantly more punitive and difficult to comply with than the CAN-SPAM Act, particularly Utah and Michigan, which have enacted do-not-email registries listing minors who do not wish to receive unsolicited commercial email that markets certain covered content, such as adult or other harmful products. Some portions of these state laws may not be preempted by the CAN-SPAM Act. The ability of our customers' constituents to opt out of receiving commercial emails may minimize the effectiveness of our email marketing product. Moreover, non-compliance with the CAN-SPAM Act carries significant financial penalties. If we were found to be in violation of the CAN-SPAM Act, applicable state laws not preempted by the CAN-SPAM Act, or foreign laws regulating the distribution of commercial email, whether as a result of violations by our customers or if we were deemed to be directly subject to and in violation of these requirements, we could be required to pay penalties, which would adversely affect our financial performance and significantly harm our business. We also may be required to change one or more aspects of the way we operate our business, which could impair our ability to attract and retain customers or increase our operating costs.

As Internet commerce develops, federal, state and foreign governments may adopt new laws to regulate Internet commerce, which may negatively affect our business.

As Internet commerce continues to evolve, increasing regulation by federal, state or foreign governments becomes more likely. Our business could be negatively impacted by the application of existing laws and regulations or the enactment of new laws applicable to email communications. The cost to comply with such laws or regulations could be significant and would increase our operating expenses, and we may be unable to pass along those costs to our customers in the form of increased subscription fees. In addition, federal, state and foreign governmental or regulatory agencies may decide to impose taxes on services provided over the Internet or via email. Such taxes could discourage the use of the Internet and email as a means of commercial marketing and communications, which would adversely affect the viability of our services.

Risks Related To Owning Our Securities

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

We generated a net loss from continuing operations of \$5.7 million in 2016. We will need to generate and sustain increased revenue levels in future periods to become profitable, and, even if we do, we may not be able to maintain or increase our level of profitability. We intend to continue to expend significant funds to expand and grow our marketing automation platform and obtain customers. Our efforts to grow our business may be more costly than we expect, and we may not be able to increase our revenue enough to offset higher operating expenses. We may incur significant losses in the future for a number of reasons, including the other risks described in this Annual Report on Form 10-K, and unforeseen expenses, difficulties, complications and delays and other unknown events. If we are unable to achieve and sustain profitability, the market price of our common stock may significantly decrease.

We may need additional capital in the future, which may not be available to us on favorable terms, or at all, and may dilute your ownership of our common stock.

We have historically relied on outside financing and cash from operations to fund our operations, capital expenditures and expansion. Although the sale of the SMTP email relay business provided the Company with a one-time source of funds, cash from operations following the divestiture is significantly lower than historic levels. We may require additional capital from equity or debt financing in the future to:

- fund our operations;
- respond to competitive pressures;
- take advantage of strategic opportunities, including more rapid expansion of our business or the acquisition of complementary products, technologies or businesses; and
- develop new products or enhancements to existing products.

We may not be able to secure timely additional financing on favorable terms, or at all. The terms of any additional financing may place limits on our financial and operating flexibility. If we raise additional funds through issuances of equity, convertible debt securities or other securities convertible into equity, our existing stockholders could suffer significant dilution in their percentage ownership of our company, and any new securities we issue could have rights, preferences and privileges senior to those of our common stock. If we are unable to obtain adequate financing or financing on terms satisfactory to us, if and when we require it, our ability to grow or support our business and to respond to business challenges could be significantly limited.

We may expand through acquisitions of, or investments in, other companies or through business relationships, all of which may result in additional dilution to our stockholders and consumption of resources that are necessary to sustain our business.

One of the strategies available to us to grow our business would be to acquire competing or complementary services, technologies or businesses. We also may enter into relationships with other businesses in order to expand our service offerings, which could involve preferred or exclusive licenses, additional channels of distribution or discount pricing or investments in other companies.

In connection with one or more of those transactions, we may:

- issue additional equity securities that would dilute our stockholders;
- use cash that we may need in the future to operate our business;
- incur debt on terms unfavorable to us or that we are unable to repay;
- incur large charges or substantial liabilities;
- encounter difficulties retaining key employees of the acquired company or integrating diverse business cultures;
- become subject to adverse tax consequences, substantial depreciation or deferred compensation charges; and
- encounter unfavorable reactions from investment banking market analysts who disapprove of our completed acquisitions.

Our board of directors has the authority, without stockholder approval, to issue preferred stock with terms that may not be beneficial to existing common stockholders and with the ability to affect adversely stockholder voting power and perpetuate their control over us.

Our certificate of incorporation allows us to issue shares of preferred stock without any vote or further action by our stockholders. Our board of directors has the authority to fix and determine the relative rights and preferences of preferred stock. Our board of directors also has the authority to issue preferred stock without further stockholder approval, including large blocks of preferred stock. As a result, our board of directors could authorize the issuance of a series of preferred stock that would grant to holders thereof the preferred right to our assets upon liquidation, the right to receive dividend payments before dividends are distributed to the holders of common stock or other preferred stockholders and the right to the redemption of the shares, together with a premium, prior to the redemption of our common stock or existing preferred stock, if any.

Preferred stock could be used to dilute a potential hostile acquirer. Accordingly, any future issuance of preferred stock or any rights to purchase preferred stock may have the effect of making it more difficult for a third party to acquire control of us. This may delay, defer or prevent a change of control or an unsolicited acquisition proposal. The issuance of preferred stock also could decrease the amount of earnings attributable to, and assets available for distribution to, the holders of our common stock and could adversely affect the rights and powers, including voting rights, of the holders of our common stock and preferred stock.

A sale of a substantial number of shares of our common stock may cause the price of our common stock to decline and may impair our ability to raise capital in the future.

Our common stock is traded on The NASDAQ Capital Market and, despite certain increases of trading volume from time to time, our common stock is considered “thinly-traded,” meaning that the number of persons interested in trading our common stock at any given time may be relatively small or non-existent. Finance transactions resulting in a large amount of newly issued shares that become readily tradable, or other events that cause current stockholders to sell shares, could place downward pressure on the trading price of our stock. As of December 31, 2016, we have outstanding a total of 3,040,735 shares of common stock that are held by certain insider stockholders. In addition, the lack of a robust resale market may require a stockholder who desires to sell a large number of shares of common stock to sell the shares in increments over time to mitigate any adverse impact of the sales on the market price of our stock.

If our stockholders sell, or the market perceives that our stockholders intend to sell for various reasons, including the ending of restriction on resale, substantial amounts of our common stock in the public market, including shares issued upon the exercise of outstanding options or warrants, the market price of our common stock could fall. Sales of a substantial number of shares of our common stock may make it more difficult for us to sell equity or equity-related securities in the future at a time and price that we deem reasonable or appropriate. We may become involved in securities class action litigation that could divert management’s attention and harm our business.

Our amended certificate of incorporation and bylaws, and certain provisions of Delaware corporate law, as well as certain of our contracts, contain provisions that could delay or prevent a change in control even if the change in control would be beneficial to our stockholders.

Delaware law, as well as our amended certificate of incorporation and bylaws, contains anti-takeover provisions that could delay or prevent a change in control of our Company, even if the change in control would be beneficial to our stockholders. These provisions could lower the price that future investors might be willing to pay for shares of our common stock. These anti-takeover provisions:

- authorize our board of directors to create and issue, without stockholder approval, preferred stock, thereby increasing the number of outstanding shares, which can deter or prevent a takeover attempt;
- prohibit cumulative voting in the election of directors, which would otherwise allow less than a majority of stockholders to elect director candidates;
- empower our board of directors to fill any vacancy on our board of directors, whether such vacancy occurs as a result of an increase in the number of directors or otherwise;
- provide that our board of directors is expressly authorized to adopt, amend or repeal our bylaws; and
- provide that our directors will be elected by a plurality of the votes cast in the election of directors.

Section 203 of the Delaware General Corporation Law, the terms of our employee stock option agreements and other contractual provisions may also discourage, delay or prevent a change in control of our Company. Section 203 generally prohibits a Delaware corporation from engaging in a business combination with an interested stockholder for three years after the date the stockholder became an interested stockholder. Our employee stock option agreements include change-in-control provisions that allow us to grant options or stock purchase rights that may become vested immediately upon a change in control. The terms of change of control provisions contained in certain of our senior executive employee agreements may also discourage a change in control of our Company. Our board of directors also has the power to adopt a stockholder rights plan that could delay or prevent a change in control of our Company even if the change in control is generally beneficial to our stockholders. These plans, sometimes called “poison pills,” are oftentimes criticized by institutional investors or their advisors and could affect our rating by such investors or advisors. If our board of directors adopts such a plan, it might have the effect of reducing the price that new investors are willing to pay for shares of our common stock.

Together, these charter, statutory and contractual provisions could make the removal of our management and directors more difficult and may discourage transactions that otherwise could involve payment of a premium over prevailing market prices for our common stock. Furthermore, the existence of the foregoing provisions, as well as the significant common stock beneficially owned by our founder, executive officers, and members of our board of directors, could limit the price that investors might be willing to pay in the future for shares of our common stock. They could also deter potential acquirers of our Company, thereby reducing the likelihood that you could receive a premium for your common stock in an acquisition.

Our quarterly results may fluctuate and if we fail to meet the expectations of analysts or investors, our stock price could decline substantially.

Our quarterly operating results may fluctuate, and if we fail to meet or exceed the expectations of securities analysts or investors, the trading price of our common stock could decline. Some of the important factors that could cause our revenue and operating results to fluctuate from quarter to quarter include:

- our ability to retain existing customers, attract new customers and satisfy our customers' requirements;
- general economic conditions;
- changes in our pricing policies;
- our ability to expand our business;
- Our ability to successfully integrate our acquired businesses;
- new product and service introductions;
- technical difficulties or interruptions in our services;
- the timing of additional investments in our hardware and software systems;
- regulatory compliance costs;
- costs associated with future acquisitions of technologies and businesses; and
- extraordinary expenses such as litigation or other dispute-related settlement payments.

Some of these factors are not within our control, and the occurrence of one or more of them may cause our operating results to vary widely. As such, we believe that quarter-to-quarter comparisons of our revenue and operating results may not be meaningful and should not be relied upon as an indication of future performance.

Our common stock is subject to volatility.

We cannot assure you that the market price for our common stock will remain at its current level and a decrease in the market price could result in substantial losses for investors. The market price of our common stock may be significantly affected by one or more of the following factors:

- announcements or press releases relating to our industry or to our own business or prospects;
- regulatory, legislative, or other developments affecting us or our industry generally;
- sales by holders of restricted securities pursuant to effective registration statements or exemptions from registration; and
- market conditions specific to our company, our industry and the stock market generally.

If securities or industry analysts do not publish research or reports about our business, or if they change their recommendations regarding our stock adversely, our stock price and trading volume 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. We currently have three independent research analyst covering our stock and may not obtain additional research coverage by securities and industry analysts. If no additional securities or industry analysts commence coverage of us, the trading price for our common stock could be negatively affected. In the event any analyst who covers us downgrades our securities, the price of our securities would likely decline. If one or more of these analysts ceases to cover us or fails to publish regular reports on us, interest in the purchase of our securities could decrease, which could cause the price of our common stock and its trading volume to decline.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None

ITEM 2. PROPERTIES

Our corporate headquarters is located in Gainesville, FL. We have a small satellite office in Kiev, Ukraine. Presently, we lease both of these office spaces.

ITEM 3. LEGAL PROCEEDINGS

We are not a party to any litigation of a material nature.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Market Information

Our common stock trades on The NASDAQ Capital Market under the symbol "SHSP". Prior to our name change on December 1, 2015 our common stock traded on the NASDAQ Capital Market under the symbol "SMTP". The following table set forth below lists the range of high and low sales prices for our common stock for our two most recent fiscal years.

		<u>High</u>	<u>Low</u>
2015	1st Quarter	\$ 6.09	\$ 4.50
	2nd Quarter	\$ 6.35	\$ 4.66
	3rd Quarter	\$ 6.56	\$ 4.60
	4th Quarter	\$ 5.19	\$ 3.16
2016	1st Quarter	\$ 4.31	\$ 2.90
	2nd Quarter	\$ 5.68	\$ 3.06
	3rd Quarter	\$ 6.30	\$ 4.48
	4th Quarter	\$ 5.75	\$ 5.01

*The prices in the table reflect inter-dealer prices, without retail markup, markdown or commission and may not represent actual transactions or a liquid trading market.

Stockholders

As of March 27, 2017 we have a total of 8,371,547 shares of common stock outstanding, held of record by approximately 75 stockholders. We do not have any shares of preferred stock outstanding.

Dividends

Our Company did not distribute any cash dividends in 2015 or 2016. Presently, we do not have any intentions to pay a dividend and our Loan and Security Agreement with Western Alliance Bank restricts our ability to pay cash dividends on our common stock and it will continue to do so for the foreseeable future.

Securities Authorized for Issuance under Equity Compensation Plans

Equity Compensation Plans as of December 31, 2016.

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders (1)	1,128,368	\$ 5.12	239,596
Equity compensation plans not approved by security holders (2)	170,973	\$ 6.26	-0-
Total	1,299,341	\$ 5.27	239,596

- (1) Reflects our 2010 Employee Stock Plan, as amended for the benefit of our directors, officers, employees and consultants. We have reserved 1,650,000 shares of common stock for such persons pursuant to that plan.
 (2) Comprised of common stock purchase warrants we issued for services.

Recent Sales of Unregistered Securities

During the period covered by this report, our Company issued the following securities without registering the securities under the Securities Act:

Securities issued as consideration for acquisition

<u>Date</u>	<u>Security</u>
March 2016	Common stock – 53,924 shares of common stock issued to satisfy earn out liability valued at \$207,929 or \$3.85 per share.
June 2016	Common stock – 1,039,636 shares of common stock issued to satisfy earn out liability valued at \$4,000,000 or \$3.85 per share.

No underwriters were utilized and no commissions or fees were paid with respect to any of the above transactions. These persons were the only offerees in connection with these transactions. We relied on Section 4(a)(2) of the Securities Act since the transactions did not involve any public offering.

ITEM 6. SELECTED FINANCIAL DATA

Not Applicable.

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

The information in this report contains forward-looking statements. All statements other than statements of historical fact made in this report are forward looking. In particular, the statements herein regarding industry prospects and future results of operations or financial position are forward-looking statements. These forward-looking statements can be identified by the use of words such as "believes," "estimates," "could," "possibly," "probably," "anticipates," "projects," "expects," "may," "will," or "should" or other variations or similar words. No assurances can be given that the future results anticipated by the forward-looking statements will be achieved. Forward-looking statements reflect management's current expectations and are inherently uncertain. Our actual results may differ significantly from management's expectations.

The following discussion and analysis should be read in conjunction with our financial statements, included herewith. This discussion should not be construed to imply that the results discussed herein will necessarily continue into the future, or that any conclusion reached herein will necessarily be indicative of actual operating results in the future. Such discussion represents only the best present assessment of our management.

Background Overview

We provide SaaS based marketing technologies to customers around the world. Our focus is on marketing automation tools that enable customers to interact with a lead from an early stage and nurture that potential customer using advanced features until it becomes a qualified sales lead or customer. We offer our premium SharpSpring marketing automation solution as well as SharpSpring Mail+, which is a subset of the full suite solution that is focused on more traditional email marketing while also including some of the advanced functionality available in our premium offering. During 2016, we discontinued the GraphicMail email marketing product and migrated those customers to our SharpSpring Mail+ product. On June 27, 2016, we sold our SMTP email relay service which provided customers with the ability to increase the deliverability of email with less time, cost and complexity than handling it themselves.

In addition to our growth through strategic acquisitions in 2014, we believe our recent growth has been driven by the strong demand for marketing automation technology solutions, particularly in the small and mid-size business market. Our products are offered at competitive prices with unlimited multi-lingual customer support. We employ a subscription-based revenue model. We also earn revenues from additional usage charges that may come into effect when a customer exceeds a transactional quota, as well as fees earned for additional products and services.

On August 15, 2014, we acquired substantially all the assets and assumed certain liabilities of SharpSpring LLC, a Delaware limited liability company, which were assigned to our wholly owned subsidiary SharpSpring Technologies, Inc. (formerly called SharpSpring, Inc.). The SharpSpring product engages in the business of creating, marketing, and selling software that provides marketing automation, call tracking, and website traffic analysis and customer relationship management. It is a cloud-based marketing automation platform that enables users to connect with customers and build relationships to drive revenue.

On October 17, 2014, we acquired the GraphicMail group companies ("GraphicMail") consisting of InterInbox SA, a Swiss corporation, InterCloud Ltd, a Gibraltar limited company, ERNEPH 2012A (Pty) Ltd. dba ISMS, a South African limited company, ERNEPH 2012B (Pty) Ltd. dba GraphicMail South Africa, a South African limited company, and Quattro Hosting LLC, a Delaware limited liability company. Prior to its discontinuation in the middle of 2016, GraphicMail operated as an email service provider, enabling customers to create content and manage emails being sent to customers and distribution lists.

On December 1, 2015, we changed our name from SMTP, Inc. to SharpSpring, Inc., and we changed the name of our SharpSpring operating subsidiary from SharpSpring, Inc. to SharpSpring Technologies, Inc.

On June 27, 2016, we sold the assets related to our SMTP email relay service.

Unless the context otherwise requires, in this section titled Management's Discussion and Analysis Of Financial Condition and Results of Operations all references to "SharpSpring" relate to the SharpSpring product, while all references to "our Company," "we," "our" or "us" and other similar terms means SharpSpring, Inc., a Delaware corporation, and all subsidiaries as of the dates of their respective acquisitions.

Results of Operations

Year Ended December 31, 2016 Compared to the Year Ended December 31, 2015

	Year Ended December 31,		Change from Prior Year	Percent Change from Prior Year
	2016	2015		
Revenues and Cost of Sales:				
Revenues	\$ 11,541,702	\$ 9,184,307	\$ 2,357,395	26%
Cost of Sales	4,462,440	2,781,691	1,680,749	60%
Gross Profit	\$ 7,079,262	\$ 6,402,616	\$ 676,646	11%

Revenues from continuing operations increased for the year ended December 31, 2016 as compared to the year ended December 31, 2015, primarily due to growth in our SharpSpring marketing automation customer base. Revenues for our flagship marketing automation platform increased to \$9.1 million in the year ended December 31, 2016 from \$4.3 million in the year ended December 31, 2015. This growth in revenues was offset by reduced revenue from our traditional email marketing products (SharpSpring Mail+ and GraphicMail). Additionally, we experienced higher attrition related to the migration of customers from the GraphicMail platform to the SharpSpring Mail+ platform during the last three quarters of 2016. Currency rate changes had an approximate \$228,000 negative impact on our year to date revenues for the period ending December 31, 2016 compared to the same period in 2015.

Cost of services increased for the year ended December 31, 2016 as compared to the year ended December 31, 2015 primarily due to costs to support increased revenues and incremental business from new customer additions to SharpSpring. As a percentage of revenues, cost of services were 39% and 30% of revenues for the year ended December 31, 2016 and 2015, respectively. This reflects a lower gross margin for our SharpSpring product, which has become a much larger percent of the overall business, as we invest in resources to support the future growth of that product. Additionally, we added infrastructure costs during the year ended December 31, 2016 related to our migration of GraphicMail customers to the SharpSpring platform.

	Year Ended December 31,		Change from Prior Year	Percent Change from Prior Year
	2016	2015		
Operating expenses:				
Sales and marketing	\$ 5,340,351	\$ 5,039,395	\$ 300,956	6%
Research and development	2,308,650	1,733,951	574,699	33%
General and administrative	4,418,500	4,005,244	413,256	10%
Change in earn out liability	219,473	2,555,649	(2,336,176)	-91%
Intangible asset amortization	1,360,105	1,508,616	(148,511)	-10%
Impairment of intangibles	1,459,541	1,310,386	149,155	11%
	\$ 15,106,620	\$ 16,153,241	\$ (1,046,621)	-6%

Sales and marketing expenses increased for the year ended December 31, 2016 as compared to the year ended December 31, 2015. The increase was primarily due to an increase in marketing program spending for events and other lead generation activities. Additionally, we experienced an increase in sales and marketing headcount-related costs due to recent hires and higher commissions expense. These increases were somewhat offset by lower partner reseller fees related to the fact that the Company acquired the customer bases for several resellers during the last nine months, and ceased paying reseller fees to those partners following the acquisitions.

Research and development expenses increased for the year ended December 31, 2016 as compared to the year ended December 31, 2015 primarily due to additional hiring of development and quality assurance staff since last year. Headcount-related costs for this group increased by approximately \$463,000 in the year ended December 31, 2016 compared to the same period in 2015.

General and administrative expenses increased for the year ended December 31, 2016 as compared to the year ended December 31, 2015, with higher facilities costs and bad debt expense offsetting reductions in restructuring fees. During the third quarter of 2015, we incurred approximately \$459,000 of restructuring charges, primarily associated with the departure of our former CEO.

The acquisitions of SharpSpring and GraphicMail included liability-based contingent consideration which is re-measured during each reporting period until the ultimate settlement in the first and second quarters of 2016. These re-measurements resulted in additional charges that are recorded on the Consolidated Statements of Comprehensive Income (Loss). During the years ended December 31, 2016 and 2015, we incurred charges of \$219,473 and \$2,555,649, respectively, related to the adjustment to the earn out liabilities for SharpSpring and GraphicMail. The charge in the year ended December 31, 2015 includes an accelerated charge for the early settlement of \$5.0 million of SharpSpring earn out liability in May 2015. The GraphicMail earn out was fully settled during the quarter ended March 31, 2016 and the SharpSpring earn out was fully settled during the quarter ended June 30, 2016. As of December 31, 2016, there are no remaining earn out related charges or liabilities.

Amortization of intangible assets decreased for the year ended December 31, 2016 as compared to the year ended December 31, 2015 due primarily to the reduction of amortization related to the GraphicMail trade name and technology intangibles. Due to the elimination of the GraphicMail product and the Company's decision to cease using the GraphicMail name brand, the Company accelerated the amortization expense of the associated intangible values to become fully amortized as of March 31, 2016. Offsetting this decrease was higher SharpSpring intangible amortization for an increased expected benefit derived in the 2016 period compared to 2015. Additionally, we incurred additional amortization expense from the acquisition of intangible assets related to the buy-out of several country partners during late 2015 and 2016 which are now being amortized.

During 2016 and 2015, we recorded impairment of intangible assets charges related to the assets acquired in the GraphicMail acquisition. In 2016, a decline in revenues related to the former customer base (migrated to SharpSpring Mail+) created an impairment in our customer relationship intangibles. In 2015, our planned migration off of the GraphicMail platform created an impairment of the trade name and technology-related intangible assets, due to the planned limited future use and benefit of the platform.

	<u>Year Ended December 31,</u>		<u>Change from</u>	<u>Percent Change from</u>
	<u>2016</u>	<u>2015</u>		
Other				
Other income (expense), net	\$ 442,195	\$ (231,718)	\$ 673,913	n/a
Provision (benefit) for income tax	(1,869,188)	(360,409)	(1,508,779)	419%

Other income (expense) is generally related to foreign exchange gains and losses derived from owing amounts or having amounts owed in currencies other than the entity's functional currency. However, during the year ended December 31, 2016, the Company recorded a gain related to a favorable claim from the GraphicMail escrow hold-back account of \$259,760. Additionally, during the year ended December 31, 2016, the Company recorded other income in the amount of \$9,871 related to the performance of services pursuant to the transition services agreement associated with the SMTP email relay product sale.

During the year ended December 31, 2016, our income tax benefit from continuing operations related to losses incurred by our consolidated U.S. entities offset by a small amount of tax expense related to income derived in foreign jurisdictions at the applicable statutory tax rates. The tax expense related to the gain on the sale of the SMTP email relay business is shown in discontinued operations, net of tax, for the year ended December 31, 2016. During the year ended December 31, 2015, our income tax expense primarily related to income derived in foreign jurisdictions, as we created a valuation allowance against certain U.S. deferred tax assets given the uncertainty of recoverability of these amounts.

	<u>Year Ended December 31,</u>		<u>Change from</u>	<u>Percent Change from</u>
	<u>2016</u>	<u>2015</u>		
Discontinued operations				
Income from discontinued operations, net of tax	\$ 10,666,985	\$ 1,377,632	\$ 9,289,353	674%

Discontinued operations, net of tax, represents revenue, offset by expenses and taxes, related to our SMTP email relay business that was sold on June 27, 2016 to an unrelated third party.

Liquidity and Capital Resources

Our primary source of operating cash inflows from continuing operations are net remittances from customers for our services. Such payments are sometimes received in advance of providing the services, yielding a deferred revenue liability on our consolidated balance sheet. On June 27, 2016, we sold our SMTP email relay business for approximately \$15.0 million, approximately \$14.0 million of which was received during the second quarter of 2016 with \$1.0 million scheduled to be received at the one year anniversary of the disposition, pursuant to the terms of the asset purchase agreement. From time to time, we also raise funds from offering our common stock for sale to new and existing investors. Additionally, in March 2016, the Company obtained a \$2.5 million revolving credit facility to provide additional financing flexibility in the future. No amounts have been borrowed under the facility to date.

Our other primary sources of cash outflows from operations include payroll and payments to vendors and third party service providers. As a result of the sale of the SMTP email relay business, we also have significant cash outflows in the 2016 year related to payments of U.S. income taxes from the gain on the asset sale. In the third quarter of 2016, we made preliminary tax payments of approximately \$2.6 million related to this gain (offset by other operating losses) and made additional payments of approximately \$1.1 million during the fourth quarter of 2016 related to our estimated U.S. tax liability. During 2016, we also acquired customer relationship assets for cash from several former GraphicMail third party resellers. Additionally, we also disbursed \$1,000,000 of cash in April 2016 for an earn out payment to the former SharpSpring shareholders and \$207,929 of cash in March 2016 for an earn out payment to the former GraphicMail shareholders.

Analysis of Cash Flows

Net cash used in operating activities from our continuing operations increased by \$5.3 million to \$8.3 million for the year ended December 31, 2016, compared to \$3.0 million for the year ended December 31, 2015. The increase in cash used in operating activities was attributable primarily to an increase in tax payments of \$3.6 million and other expenditures related to growing our SaaS marketing automation platform, which generated greater losses in 2016 compared to 2015.

Net cash used in investing activities from our continuing operations was \$1.2 million and \$0.5 million during the year ended December 31, 2016, and 2015, respectively. For the year ending December 31, 2016, cash used in investing activities includes \$724,678 of cash paid to several former GraphicMail third-party resells to acquire customer relationship assets. Additionally, the Company used \$455,506 to purchase property and equipment during the year ended December 31, 2016, compared to \$456,512 in the year ended December 31, 2015. The majority of the asset purchases in 2016 relate to furniture and fixtures in the Company's new headquarters office in Gainesville, FL, while the assets acquired in 2015 related to general business growth and expansion.

Net cash used in financing activities was \$1.2 million during the year ended December 31, 2016 compared to \$3.5 million provided by financing activities during the year ended December 31, 2015. During the year ending December 31, 2016, the Company paid \$1.0 million to the former SharpSpring shareholders and \$207,929 to the former GraphicMail shareholders related to earn out payments from those 2014 acquisitions. During the year ended December 31, 2015, we raised cash in two equity financings. In the first, we raised \$2 million (net of expenses) in an offering of common stock and paid \$2 million to former SharpSpring shareholders related to an early settlement of part of the cash-based earn out for that acquisition. In the second equity financing, we raised approximately \$3.4 million (net of expenses) from a stock offering in August 2015. We also received \$141,441 related to proceeds from stock option exercises during the year ended December 31, 2015.

We had net working capital of approximately \$10.5 million and negative (\$1.8 million) as of December 31, 2016 and December 31, 2015, respectively. The change to positive working capital in 2016 relates to the sale proceeds from the SMTP asset sale and the settlement of the SharpSpring earn out liability (in cash and shares), both of which occurred during the year ended December 31, 2016. The negative net working capital at December 31, 2015 was primarily attributable to our short term earn out liability of \$5.2 million. The majority of this earn out liability related to SharpSpring, for which 80% of the liability was ultimately settled in stock. Our cash balance increased to \$8.7 million at December 31, 2016 compared to \$4.2 million at December 31, 2015.

Contractual Obligations

We rent our facilities with leases ranging from month-to-month to several years in duration. Most of our service contracts are also on a month-to-month basis. However, from time to time, we enter into non-cancelable service contracts including longer-term contracts and payments for the acquisition of customer relationships from resellers. Future minimum lease payments and payments due under non-cancelable service contracts are as follows as of December 31, 2016:

2017	\$	745,563
2018		448,918
2019		373,015
2020		382,884
2021		292,843
Thereafter		-
	\$	<u>2,243,223</u>

Significant Accounting Policies

Our significant accounting policies, including the assumptions and judgments underlying them, are disclosed in the Notes to the Financial Statements. We have consistently applied these policies in all material respects. We do not believe that our operations to date have involved uncertainty of accounting treatment, subjective judgment, or estimates, to any significant degree.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

New Accounting Pronouncements

For information on recent accounting pronouncements, see *Recently Issued Accounting Pronouncements* in the notes to the consolidated financial statements appearing elsewhere in this Annual Report on Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements included in this annual report under this item are set forth beginning on Page F-1 of this Annual Report, immediately following the signature pages.

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

Not Applicable.

ITEM 9A. CONTROLS AND PROCEDURES*Evaluation of Disclosure Controls and Procedures*

As of the end of the period covered by this report, our Company evaluated the effectiveness and design and operation of its disclosure controls and procedures. Our Company's disclosure controls and procedures are the controls and other procedures that we designed to ensure that our Company records, processes, summarizes, and reports in a timely manner the information that it must disclose in reports that our Company files with or submits to the Securities and Exchange Commission. Our principal executive officer and principal financial officer reviewed and participated in this evaluation. Based on this evaluation, our Company made the determination that its disclosure controls and procedures were effective.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal controls over financial reporting based on the framework in Internal Control -Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on this evaluation, management has concluded that our internal control over financial reporting was not effective as of December 31, 2016 due to gaps in controls documentation and segregation of duties.

The Company's internal control over financial reporting includes policies and procedures that (1) pertain to maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Our management, including our principal executive officer and principal financial officer, does not expect that our disclosure controls or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. In addition, the design of any system of controls is based in part on certain assumptions about the likelihood of future events, and controls may become inadequate if conditions change. There can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

This annual report does not include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's attestation in this annual report.

Changes in Company Internal Controls

No change in our Company's internal control over financial reporting occurred during our fourth fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

Not Applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item is incorporated by reference from the information contained within our Company's definitive proxy statement for the 2017 Annual Meeting of Stockholders.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item is incorporated by reference from our Proxy Statement to be filed prior to the 2017 the Annual Meeting of Stockholders.

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

The information required by this Item is incorporated by reference from our Proxy Statement to be filed prior to the 2017 the Annual Meeting of Stockholders.

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

The information required by this Item is incorporated by reference from our Proxy Statement to be filed prior to the 2017 the Annual Meeting of Stockholders.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item is incorporated by reference from our Proxy Statement to be filed prior to the 2017 the Annual Meeting of Stockholders.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report:

1. *Financial Statements and Reports*

The financial statements included in Part II, Item 8 of this Annual Report on Form 10-K are filed as part of this Report.

2. *Financial Statements Schedule*

Other financial statement schedules have been omitted because either the required information (i) is not present, (ii) is not present in amounts sufficient to require submission of the schedule or (iii) is included in the Financial Statements and Notes thereto under Part II, Item 8 of this Annual Report on Form 10-K.

3. *Exhibits*

The exhibit list in the Index to Exhibits is incorporated herein by reference as the list of exhibits required as part of this Report.

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 on March 30, 2017.

SharpSpring, Inc.

By: /s/ Richard A. Carlson

Richard A. Carlson
Chief Executive Officer and President
(Principal Executive Officer)

Pursuant to the requirements of the Securities Act of 1933, this registration statement has been signed by the following persons in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Richard A. Carlson</u> Richard A. Carlson	Chief Executive Officer and President (Principal Executive Officer), Director	March 30, 2017
<u>/s/ Edward S. Lawton</u> Edward S. Lawton	Chief Financial Officer (Principal Financial Officer)	March 30, 2017
<u>/s/ Semyon Dukach</u> Semyon Dukach	Chair of the Board of Directors	March 30, 2017
<u>/s/ Vadim Yasinovsky</u> Vadim Yasinovsky	Director	March 30, 2017
<u>/s/ John L. Troost</u> John L. Troost	Director	March 30, 2017
<u>/s/ David A. Buckel</u> David A. Buckel	Director	March 30, 2017
<u>/s/ Steven A. Huey</u> Steven A. Huey	Director	March 30, 2017

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McCONNELL & JONES LLP
CERTIFIED PUBLIC ACCOUNTANTS

Report of Independent Registered Public Accounting Firm

To the Board of Directors
SharpSpring, Inc.

We have audited the accompanying consolidated balance sheet of SharpSpring, Inc. (the Company) (f/k/a SMTP, Inc.) as of December 31, 2015, and the related consolidated statements of comprehensive loss, changes in shareholders' equity, and cash flows for the year then ended. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with 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 consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal controls over financial reporting. Our audit included consideration of internal controls 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 controls over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of SharpSpring, Inc as of December 31, 2015 and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ McConnell & Jones, LLP

Houston, Texas
March 30, 2016, except for Note 5, as to which the date is March 30, 2017

4828 Loop Central Drive, Suite 1000
Houston, TX 77081
Phone: 713.968.1600

WWW.MCCONNELLJONES.COM

Report of Independent Registered Public Accounting Firm

To the Board of Directors and
Stockholders of SharpSpring, Inc.

We have audited the accompanying consolidated balance sheet of SharpSpring, Inc. (the Company) (f/k/a SMTP, Inc.) as of December 31, 2016, and the related consolidated statements of comprehensive loss, changes in stockholders' equity, and cash flows for the year then ended. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit 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, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2016, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Cherry Bekaert LLP
Atlanta, Georgia
March 30, 2017

SHARPSRING, INC.
CONSOLIDATED BALANCE SHEETS

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Assets		
Cash and cash equivalents	\$ 8,651,374	\$ 4,158,646
Accounts receivable, net of allowance for doubtful accounts of \$508,288 and \$23,582 at December 31, 2016 and 2015, respectively	1,261,923	794,123
Deferred income taxes	-	16,645
Income taxes receivable	1,355,180	793,189
Other current assets	1,396,642	205,143
Assets held for sale	-	45,697
Total current assets	<u>12,665,119</u>	<u>6,013,443</u>
Property and equipment, net	905,345	565,481
Goodwill	8,845,394	8,881,933
Other intangible assets, net	2,850,635	5,518,305
Deposits and other	30,464	11,280
Deferred income taxes	32,996	-
Assets held for sale	-	251,565
Total assets	<u>\$ 25,329,953</u>	<u>\$ 21,242,007</u>
Liabilities and Shareholders' Equity		
Accounts payable	\$ 498,534	\$ 609,454
Accrued expenses and other current liabilities	953,171	1,098,790
Deferred revenue	280,159	525,217
Current portion of earn out liabilities	-	5,191,116
Income taxes payable	484,349	36,469
Deferred income taxes	-	7,598
Liabilities held for sale	-	369,941
Total current liabilities	<u>2,216,213</u>	<u>7,838,585</u>
Deferred income taxes	195,495	-
Total liabilities	<u>2,411,708</u>	<u>7,838,585</u>
Commitments and Contingencies (Note 17)		
Shareholders' equity:		
Preferred stock, \$0.001 par value, 5,000,000 shares authorized, no shares issued or outstanding at December 31, 2016 and December 31, 2015	-	-
Common stock, \$0.001 par value, Authorized shares-50,000,000; issued shares-8,380,663 at December 31, 2016 and 7,233,035 at December 31, 2015; outstanding shares-8,360,663 at December 31, 2016 and 7,233,035 at December 31, 2015	8,381	7,233
Additional paid in capital	27,556,398	22,607,290
Accumulated other comprehensive income (loss)	(445,055)	(142,613)
Accumulated deficit	(4,117,479)	(9,068,488)
Treasury stock	(84,000)	-
Total shareholders' equity	<u>22,918,245</u>	<u>13,403,422</u>
Total liabilities and shareholders' equity	<u>\$ 25,329,953</u>	<u>\$ 21,242,007</u>

See accompanying notes to the consolidated financial statements.

SHARPSRING, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

	Year Ended December 31,	
	2016	2015
Revenue	\$ 11,541,702	\$ 9,184,307
Cost of services	4,462,440	2,781,691
Gross profit	7,079,262	6,402,616
Operating expenses:		
Sales and marketing	5,340,351	5,039,395
Research and development	2,308,650	1,733,951
General and administrative	4,418,500	4,005,244
Change in earn out liability	219,473	2,555,649
Intangible asset amortization	1,360,105	1,508,616
Impairment of intangible assets	1,459,541	1,310,386
Total operating expenses	15,106,620	16,153,241
Operating loss	(8,027,358)	(9,750,625)
Other income (expense), net	442,195	(231,718)
Loss before income taxes	(7,585,163)	(9,982,343)
Provision (benefit) for income tax	(1,869,188)	(360,409)
Net loss from continuing operations	(5,715,975)	(9,621,934)
Net income from discontinued operations, net of tax	10,666,985	1,377,632
Net income (loss)	\$ 4,951,010	\$ (8,244,302)
<u>Net loss per share from continuing operations</u>		
Basic net loss per share	\$ (0.72)	\$ (1.51)
Diluted net loss per share	\$ (0.72)	\$ (1.51)
<u>Net income per share from discontinued operations</u>		
Basic net income per share	\$ 1.35	\$ 0.22
Diluted net income per share	\$ 1.35	\$ 0.22
<u>Net income (loss) per share</u>		
Basic net income (loss) per share	\$ 0.63	\$ (1.30)
Diluted net income (loss) per share	\$ 0.63	\$ (1.30)
Shares used in computing basic net income (loss) per share	7,895,197	6,354,134
Shares used in computing diluted net income (loss) per share	7,895,197	6,354,134
<u>Other comprehensive income (loss):</u>		
Foreign currency translation adjustment	(302,442)	35,154
Comprehensive income (loss)	\$ 4,648,568	\$ (8,209,148)

See accompanying notes to the consolidated financial statements.

SHARPSRING, INC.
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

	Common Stock		Additional Paid in Capital	Accumulated Other Comprehensive Loss	Treasury Stock		Retained Earnings (Accumulated Deficit)	Total
	Shares	Amount			Shares	Amount		
Balance, December 31, 2014	5,447,528	5,448	13,248,992	(177,767)	-	-	(824,185)	12,252,487
Stock based compensation - stock options	-	-	689,871	-	-	-	-	689,871
Issuance of common stock for cash	1,198,984	1,199	5,485,707	-	-	-	-	5,486,906
Issuance of common stock for services	41,068	41	182,019	-	-	-	-	182,060
Issuance of common stock for earn out payment	545,455	545	2,999,455	-	-	-	-	3,000,000
Tax benefit from stock-based award activity, net	-	-	1,246	-	-	-	-	1,246
Foreign currency translation adjustment	-	-	-	35,154	-	-	-	35,154
Net loss	-	-	-	-	-	-	(8,244,302)	(8,244,302)
Balance, December 31, 2015	7,233,035	7,233	22,607,290	(142,613)	-	-	(9,068,488)	13,403,422
Stock based compensation - stock options	-	-	510,002	-	-	-	-	510,002
Issuance of common stock for cash	3,088	3	12,214	-	-	-	-	12,217
Issuance of common stock for services	50,976	51	220,479	-	-	-	-	220,530
Issuance of common stock for earn out payment	1,093,564	1,094	4,206,835	-	-	-	-	4,207,929
Receipt of treasury shares of shares	-	-	-	-	20,000	(84,000)	-	(84,000)
Tax benefit from stock-based award activity, net	-	-	(422)	-	-	-	-	(422)
Foreign currency translation adjustment	-	-	-	(302,442)	-	-	-	(302,442)
Net income	-	-	-	-	-	-	4,951,010	4,951,010
Balance, December 31, 2016	8,380,663	\$ 8,381	\$27,556,398	\$ (445,055)	20,000	\$(84,000)	\$ (4,117,479)	\$22,918,245

See accompanying notes to the consolidated financial statements.

SHARPSRING, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,	
	2016	2015
Cash flows from operating activities:		
Net income (loss)	\$ 4,951,010	\$ (8,244,302)
Deduct: Income from discontinued operations, net of income taxes	10,666,985	1,377,632
Net loss from continuing operations	(5,715,975)	(9,621,934)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,519,257	1,598,032
Impairment of intangibles	1,459,541	1,310,386
Excess tax benefits from share-based payments	-	(1,247)
Non-cash stock compensation	705,649	842,863
Deferred income taxes	167,757	842,688
Loss on disposal of property and equipment	128,978	2,491
Non-cash change in value of earn out liability	219,473	2,556,209
Non-cash gain from escrow claim	(84,000)	-
Unearned foreign currency (gain) loss	(185,414)	152,211
Changes in operating assets and liabilities:		
Accounts receivable	(499,516)	(428,764)
Other assets	(210,715)	(18,734)
Income taxes, net	(5,706,659)	(445,145)
Accounts payable	(156,081)	238,957
Accrued expenses and other current liabilities	271,058	71,487
Deferred revenue	(246,721)	(91,703)
Net cash provided by (used in) operating activities - Continuing operations	(8,333,368)	(2,992,203)
Net cash provided by (used in) operating activities - Discontinued operations	1,265,364	1,493,756
Net cash used in operating activities	(7,068,004)	(1,498,447)
Cash flows from investing activities:		
Purchases of property and equipment	(455,506)	(456,512)
Acquisitions of customer assets from resellers	(724,678)	-
Net cash provided by (used in) investing activities - Continuing operations	(1,180,184)	(456,512)
Net cash provided by (used in) investing activities - Discontinued operations	13,945,548	(169,219)
Net cash provided by (used in) investing activities	12,765,364	(625,731)
Cash flows from financing activities:		
Payment to reduce earn out liabilities	(1,207,929)	(2,000,000)
Proceeds from exercise of stock options	12,217	141,441
Proceeds from issuance of common stock	-	5,332,023
Excess tax benefits from share-based payments	(422)	1,247
Net cash provided by (used in) financing activities - Continuing operations	(1,196,134)	3,474,711
Net cash provided by (used in) financing activities - Discontinued operations	-	-
Net cash provided by (used in) financing activities	(1,196,134)	3,474,711
Effect of exchange rate on cash	(8,498)	(17,407)
Change in cash and cash equivalents	4,492,728	1,333,126
Cash and cash equivalents, beginning of period	4,158,646	2,825,520
Cash and cash equivalents, end of period	<u>\$ 8,651,374</u>	<u>\$ 4,158,646</u>
Supplemental information on consolidated statements of cash flows:		
Cash paid for income taxes	\$ 3,643,858	\$ 130,292
Supplemental information on non-cash investing and financing activities:		
Receipt of common stock for escrow claim	\$ 84,000	\$ -
Settlement of earn out liabilities with common stock	\$ (4,207,929)	\$ (3,000,000)
Other receivable created for sale of SMTP email relay business	\$ (1,000,000)	\$ -

See accompanying notes to the consolidated financial statements.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Organization

We were incorporated in Massachusetts in October 1998 as EMUmail, Inc. and we changed our name in April 2010 to SMTP.com, Inc. In November 2010, we reincorporated in the State of Delaware and changed our name to SMTP, Inc. In December 2013, we effected a 1-for-5 reverse stock split of our common stock whereby every five shares of our pre-reverse stock split common stock was combined and reclassified into one share of post-reverse stock split common stock.

On August 15, 2014, we acquired substantially all the assets and assumed the liabilities of SharpSpring LLC, and on October 17, 2014, we acquired all of the outstanding equity of the GraphicMail group companies. See Note 3 for details of these acquisitions.

On December 1, 2015, our Company changed its parent company name from SMTP, Inc. to SharpSpring, Inc. and changed the name of its SharpSpring product U.S. operating subsidiary from SharpSpring, Inc. to SharpSpring Technologies, Inc.

On June 27, 2016, we sold the assets related to our SMTP email relay product to the Electric Mail Company, a Nova Scotia company. See Note 5 for details of this disposition.

Our Company focuses on providing cloud-based marketing automation solutions. Our SharpSpring marketing automation solution is designed to increase the rates at which businesses generate leads and convert leads to sales opportunities by improving the way businesses communicate with customers and prospects. Our products are marketed directly by us and through a small group of reseller partners. Prior to June 27, 2016, our Company also provided cloud-based email relay delivery services to its customers.

Note 2: Summary of Significant Accounting Policies

Basis of Presentation and Consolidation

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). Our Consolidated Financial Statements include the accounts of SharpSpring, Inc. and our subsidiaries (“the Company”). Our Consolidated Financial Statements reflect the elimination of all significant inter-company accounts and transactions.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Operating Segments

The Company operates as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is regularly evaluated by the chief operating decision maker (“CODM”), which is the Company’s chief executive officer, in deciding how to allocate resources and assess performance. The Company’s CODM evaluates the Company’s financial information and resources and assess the performance of these resources on a consolidated basis. The Company does not present geographical information about revenues because it is impractical to do so.

Foreign Currencies

The Company’s subsidiaries utilize the U.S. Dollar, Swiss Franc, South African Rand and British Pound as their functional currencies. The assets and liabilities of these subsidiaries are translated at ending exchange rates for the respective periods, while revenues and expenses are translated at the average rates in effect for the period. The related translation gains and losses are included in other comprehensive income or loss within the Consolidated Statements of Comprehensive Loss.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Cash and Cash Equivalents

Cash equivalents are short-term, liquid investments with remaining maturities of three months or less when acquired. Cash and cash equivalents are deposited or managed by major financial institutions and at most times are in excess of Federal Deposit Insurance Corporation (FDIC) insurance limits.

Fair Value of Financial Instruments

U.S. GAAP establishes a fair value hierarchy which has three levels based on the reliability of the inputs to determine the fair value. These levels include: Level 1, defined as inputs such as unadjusted quoted prices in active markets for identical assets or liabilities; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs for use when little or no market data exists, therefore requiring an entity to develop its own assumptions.

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, deposits and accounts payable. The carrying amount of cash and cash equivalents, accounts receivable and accounts payable approximates fair value because of the short-term nature of these items.

Accounts Receivable

Accounts receivable are carried at the original invoiced amount less an allowance for doubtful accounts based on the probability of future collection. Management reviews accounts receivable on a periodic basis to determine if any receivables will potentially be uncollectible. The Company reserves for receivables that are determined to be uncollectible, if any, in its allowance for doubtful accounts. The Company had an allowance for doubtful accounts of \$508,288 and \$23,582 as of December 31, 2016 and 2015, respectively. After the Company has exhausted all collection efforts, the outstanding receivable is written off against the allowance.

Intangibles

Finite-lived intangible assets include trade names, developed technologies and customer relationships and are amortized based on the estimated economic benefit over their estimated useful lives, with periods ranging from 5 to 11 years. We continually evaluate the reasonableness of the useful lives of these assets. Finite-lived intangibles are tested for recoverability whenever events or changes in circumstances indicate the carrying amounts may not be recoverable. Impairment losses are measured as the amount by which the carrying value of an asset group exceeds its fair value and are recognized in operating results. Judgment is used when applying these impairment rules to determine the timing of the impairment test, the undiscounted cash flows used to assess impairments and the fair value of an asset group. The dynamic economic environment in which the Company operates and the resulting assumptions used to estimate future cash flows impact the outcome of these impairment tests. During the year ended December 31, 2016, the Company recorded an impairment loss of \$1,459,541 related to the impaired recovery of its GraphicMail customer relationship assets due to significant erosion of that customer base following the migration onto the SharpSpring Mail+ product. During the year ended December 31, 2015, the Company recorded an impairment loss of \$1,310,386 related to the impaired recovery of its GraphicMail technology and trade name assets after the decision was made to discontinue using the GraphicMail technology and brand.

Goodwill and Impairment

As of December 31, 2016 and 2015, we had recorded goodwill of \$8,845,394 and \$8,881,933, respectively. Goodwill consists of the excess of the purchase price over the fair value of tangible and identifiable intangible net assets acquired in the SharpSpring and GraphicMail acquisitions (See Note 3). Under FASB ASC 350, "*Intangibles - Goodwill and Other*" deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests, and tests between annual tests in certain circumstances, based on estimated fair value in accordance with FASB ASC 350-10, and written down when impaired.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Income Taxes

Provision for income taxes are based on taxes payable or refundable for the current year and deferred taxes on temporary differences between the amount of taxable income and pretax financial income and between the tax bases of assets and liabilities and their reported amounts in the financial statements. Deferred tax assets and liabilities are included in the financial statements at currently enacted income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled as prescribed in FASB ASC 740, *Accounting for Income Taxes*. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that a deferred tax asset will not be realized.

The Company applies the authoritative guidance in accounting for uncertainty in income taxes recognized in the consolidated financial statements. This guidance prescribes a two-step process to determine the amount of tax benefit to be recognized. First, the tax position must be evaluated to determine the likelihood that it will be sustained upon external examination. If the tax position is deemed “more-likely-than-not” to be sustained, the tax position is then assessed to determine the amount of benefit to recognize in the financial statements. The amount of the benefit that may be recognized is the largest amount that has a greater than 50% likelihood of being realized upon ultimate settlement. There are no material uncertain tax positions taken by the Company on its tax returns. Tax years subsequent to 2012 remain open to examination by U.S. federal and state tax jurisdictions.

In determining the provision for income taxes, the Company uses statutory tax rates and tax planning opportunities available to the Company in the jurisdictions in which it operates. This includes recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns to the extent pervasive evidence exists that they will be realized in future periods. The deferred tax balances are adjusted to reflect tax rates by tax jurisdiction, based on currently enacted tax laws, which are expected to be in effect in the years in which the temporary differences are expected to reverse. In accordance with the Company’s income tax policy, significant or unusual items are separately recognized in the period in which they occur. The Company is subject to routine examination by domestic and foreign tax authorities and frequently faces challenges regarding the amount of taxes due. These challenges include positions taken by the Company related to the timing, nature and amount of deductions and the allocation of income among various tax jurisdictions. As of December 31, 2016, the Company is not being examined by domestic or foreign tax authorities.

Property and Equipment

Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful life of the assets. Upon retirement or sale, the cost of assets disposed of and the related accumulated depreciation are eliminated from the accounts and any resulting gain or loss is credited or charged to operations. Repairs and maintenance costs are expensed as incurred. Depreciation expense from continuing operations related to property and equipment was \$159,152 and \$89,416 for the years ended December 31, 2016 and 2015, respectively.

Property and equipment as of December 31 is as follows:

	December 31, 2016	December 31, 2015
Property and equipment, net:		
Leasehold improvements	\$ 128,122	\$ 1,909
Furniture and fixtures	316,819	126,929
Computer equipment and software	641,722	295,613
Construction in progress	-	280,000
Total	<u>1,086,663</u>	<u>704,451</u>
Less: Accumulated depreciation and amortization	<u>(181,318)</u>	<u>(138,970)</u>
	<u>\$ 905,345</u>	<u>\$ 565,481</u>

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Useful lives are as follows:

Leasehold improvements	3-5 years
Furniture and fixtures	3-5 years
Computing equipment	3 years
Software	3-5 years

Revenue Recognition

The Company recognizes revenue from its services when it is probable that the economic benefits associated with the transactions will flow to the Company and the amount of revenue can be measured reliably. This is normally demonstrated when: (i) persuasive evidence of an arrangement exists; (ii) the fee is fixed or determinable; (iii) performance of service has been delivered; and (iv) collection is reasonably assured.

For the Company's internet-based SharpSpring marketing automation solution, the services are typically offered on a month-to-month basis with a fixed fee charged each month depending on the size of the engagement with the customer. Monthly fees are recorded as revenue during the month they are earned. Some customers are charged annually, for which revenues are deferred and recorded ratably over the subscription period. The Company also charges transactional-based fees if monthly volume limitations are reached or other chargeable activity occurs. Additionally, customers are typically charged an upfront implementation and training fee. The upfront implementation and training fees represent short-term "use it or lose it" services offered for a flat fee. Such flat fees are recognized over the service period, which is 60 days.

For the Company's SMTP email delivery product (prior to its sale in June 2016), the Company's GraphicMail email product (which was discontinued in 2016) and the SharpSpring Mail+ product, services are provided over various contractual periods for a fixed fee that varies based on a maximum volume of transactions. Revenue is recognized on a straight-line basis over the contractual period. If the customer's transactions exceed contractual volume limitations, overages are charged and recorded as revenue in the periods in which the transaction overages occur.

During 2015 and the first half of 2016, certain of the Company's GraphicMail customers were sold through third party resellers. In some cases, we allowed the third party resellers to collect the funds directly from the customer, withhold their own reseller fee, and remit the net amount owed back to the Company. In those situations, because the Company is the primary obligor in the arrangement, the Company recorded the gross revenue and expenses such that 100% of the end customer revenue is reported by the Company and a corresponding expense is recorded for the reseller fee. The Company discontinued selling through third party resellers for the GraphicMail and SharpSpring Mail+ products during 2016.

From time to time, the Company offers refunds to customers and experiences credit card chargebacks relating to cardholder disputes that are commonly experienced by businesses that accept credit cards. The Company makes estimates for refunds and credit card chargebacks based on historical experience.

Deferred Revenue

Some of the Company's customers pay for services in advance on a periodic basis (such as monthly, quarterly, annually or bi-annually). Also, the Company charges an upfront implementation and training fee for its SharpSpring marketing automation solution that is paid in advance, for which services are performed over a 60-day period. Deferred revenue consists of payments received in advance of the Company's providing the services. Deferred revenues are amortized on a straight-line basis in connection with the contractual period or recorded as revenue when the services are used.

Accrued Revenue

In cases where our customers pay for services in arrears, we accrue for revenue in advance of billings as long as the criteria for revenue recognition is met. A portion of our accounts receivable balance is therefore unbilled at the balance sheet date.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Concentration of Credit Risk and Significant Customers

Financial instruments that potentially expose the Company to concentrations of credit risk consist primarily of cash, cash equivalents. At December 31, 2016 and 2015, the Company had cash balances at financial institutions that exceed federally insured limits. The Company maintains its cash balances with accredited financial institutions. The Company does not believe that it is subject to unusual credit risk beyond the normal credit risk associated with commercial banking relationships.

For the years ended December 31, 2016, and 2015, there were no customers that accounted for more than 10% of total revenue or 10% of total accounts receivable.

Cost of Services

Cost of services consists primarily of the direct labor costs, technology hosting costs, software license costs, and fees paid to resellers of the Company's product.

Credit Card Processing Fees

Credit card processing fees are included as a component of general and administrative expenses and are expensed as incurred.

Advertising Costs

The Company expenses advertising costs as incurred. Advertising and marketing expenses from continuing operations was \$1,619,294 and \$869,603 for the years ended December 31, 2016 and 2015, respectively.

Research and Development Costs and Capitalized Software Costs

We capitalize certain costs associated with internal use software during the application development stage, mostly related to software that we use in providing our hosted solutions. We expense costs associated with preliminary project phase activities, training, maintenance and any post-implementation period costs as incurred. For the years ended December 31, 2016 and December 31, 2015, we capitalized \$5,239 and \$115,649, respectively, in software development costs. We amortize capitalized software costs over the estimated useful life of the software, which is typically estimated to be 3 years, once the related project has been completed and deployed for customer use. At December 31, 2016 and December 31, 2015, the net carrying value of capitalized software was \$78,005 and \$99,764, respectively.

All other software development costs are charged to expenses when incurred, and generally consist of salaries, software development tools and personnel-related costs for those engaged in research and development activities.

Stock Compensation

We account for stock based compensation in accordance with FASB ASC 718, which requires companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the grant-date fair value of the award. Stock-based compensation expense is recognized on a straight-line basis over the requisite service period.

Net Income (Loss) Per Share

Basic net income (loss) per share is computed using the weighted average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted average number of common shares and, if dilutive, potential common shares outstanding during the period.

Comprehensive Income or Loss

Comprehensive income or loss includes all changes in equity during a period from non-owner sources, such as net income or loss and foreign currency translation adjustments.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Recently Issued Accounting Standards

Recent accounting standards not included below are not expected to have a material impact on our consolidated financial position and results of operations.

In March 2016, the Financial Accounting Standards Board (“FASB”) issued guidance that changes the accounting for certain aspects of share-based payments to employees. The guidance requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid-in capital pools. The guidance also allows for the employer to repurchase or sell more shares than required under local statutory regulation without triggering liability accounting. In addition, the guidance allows for a policy election to account for forfeitures as they occur rather than on an estimated basis. The guidance is effective in 2017 with early adoption permitted. The Company is currently evaluating the impact of this guidance on the consolidated financial statements.

In February 2016, the FASB issued guidance that requires lessees to recognize most leases on their balance sheets but record expenses on their income statements in a manner similar to current accounting. For lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. The guidance is effective in 2019 with early adoption permitted. The Company is currently evaluating the impact of this guidance on the consolidated financial statements.

In May 2014, the FASB issued updated guidance and disclosure requirements for recognizing revenue. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In July 2015, the FASB approved the deferral of the new standard’s effective date by one year. The new standard now is effective for annual reporting periods beginning January 1, 2018. The FASB will permit companies to adopt the new standard early, but not before the original effective date of January 1, 2017. The Company is currently evaluating the impact of this guidance on the consolidated financial statements.

Note 3: Acquisitions

During 2014, the Company pursued strategic acquisitions to further extend its product offerings. Such acquisitions have been accounted for as business combinations pursuant to ASC 805 “*Business Combinations*.” Under this ASC, acquisition and integration costs are not included as components of consideration transferred, but are accounted for as expenses in the period in which the costs are incurred.

SharpSpring

On August 15, 2014, the Company acquired substantially all the assets and assumed the liabilities of SharpSpring LLC, a Delaware limited liability company for a cash payment of \$5,000,000 plus potential earn out consideration of \$10,000,000 that was contingent on the SharpSpring product achieving certain levels of revenue in 2015. SharpSpring is a cloud-based marketing automation platform that enables users to connect with customers and build relationships to drive revenue through marketing automation, call tracking and customer relationship management.

The SharpSpring earn out was initially \$10,000,000, payable 60% in cash and 40% in stock, depending on SharpSpring achieving certain revenue levels in 2015. At the time of the acquisition, the Company utilized the income approach to estimate the fair value of the earn out. The Company analyzed scenarios and determined a probability weighting for each scenario. The Company calculated the earn out payments based on the respective revenues for each scenario and then weighted the resulting payment by the probabilities of achieving each scenario. In order to calculate an appropriate risk-adjusted discount rate for the earn out, the Company calculated the weighted average cash-flows of the business based on the three scenarios and their respective weightings. The Company then calculated an implied internal rate of return (“IRR”) of 18.9%, which is the discount rate necessary in order to reconcile the weighed cash-flows of the three scenarios to the total purchase price including the earn out payment. The earn out payment was then discounted by the 18.9% IRR. Based on these methods and the Company’s original assessment of meeting those revenue levels in 2015, an earn out liability of \$6,963,000 was originally recorded as a liability during purchase accounting. This was re-measured in each subsequent quarter since the transaction, resulting in additional charges of \$222,000 and \$2,133,000 during the years ended December 31, 2016 and December 31, 2015, respectively. These earn out adjustments have been recorded on the Consolidated Statement of Comprehensive Income (Loss) for the respective periods.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Company entered into a transaction with RCTW, LLC, a Delaware limited liability company, f/k/a SharpSpring, LLC (“RCTW”) during May 2015 to pay a portion of the cash-based earn out early, as well as to agree that the future earn out for the SharpSpring assets would be paid in its entirety. Although the Company was obligated to pay the full earn out for the SharpSpring assets, the earn out liability value was increased over time as a result of the discount factor applied to the liability. The final payments against the earn out of \$1.0 million in cash and \$4.0 million in common stock occurred in the quarter ended June 30, 2016 and there was no remaining liability as of December 31, 2016.

As of December 31, 2016, management had completed its evaluation of the fair value of certain intangible and other net assets acquired and there will be no future changes.

The following table presents the components of the purchase price consideration:

Cash consideration	\$	5,000,000
Earn out liability		6,963,000
Liabilities assumed		149,841
Total purchase price	\$	<u>12,112,841</u>

The following represents the allocation of the purchase price to the acquired net tangible and intangible assets acquired and liabilities assumed of SharpSpring:

Total purchase price	\$	12,112,841
Less:		
Net tangible assets acquired		(135,614)
Intangible assets acquired:		
Trade Name		(120,000)
Developed Technologies		(2,130,000)
Customer Relationships		(1,320,000)
Total intangible assets		<u>(3,570,000)</u>
Goodwill	\$	<u>8,407,227</u>

Acquired intangible assets include trade names which are to be amortized over the useful life of five years, and technology and customer relationships which are to be amortized over the useful life of 11 years.

Goodwill of \$8,407,227 was recorded. Goodwill will not be amortized but instead tested for impairment at least annually (more frequently if certain indicators are present). The \$8,407,227 of goodwill is not expected to be deductible for tax purposes. Goodwill arose primarily as a result of the expected future growth of the SharpSpring product and the assembled workforce.

GraphicMail

On October 17, 2014, we acquired 100% of the equity interest owned, directly or indirectly, in GraphicMail group companies (“GraphicMail”) consisting of InterInbox SA, a Swiss corporation, InterCloud Limited, a Gibraltar limited company, ERNEPH 2012A (Pty) Ltd. dba ISMS, a South African limited company, ERNEPH 2012B (Pty) Ltd. dba GraphicMail South Africa, a South African limited company, and Quattro Hosting LLC, a Delaware limited liability company. The acquisition consideration consisted of \$5.3 million, \$2.6 million of which was paid in cash and \$2.7 million of which was paid in stock, plus potential earn out consideration of up to \$0.8 million based on achieving certain revenue levels in 2015 (paid 50% in cash and 50% in stock). GraphicMail operates as a campaign management solution, enabling customers to create content and manage emails being sent to customers and distribution lists.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Pursuant to the equity interest purchase agreement, the Company was liable for an earn out of up to \$0.8 million, related to GraphicMail achieving certain revenue levels in 2015. The Company utilized the income approach to estimate the fair value of the earn out. The Company analyzed scenarios and determined a probability weighting for each scenario. The Company calculated the earn out payments based on the respective revenues for each scenario and then weighted the resulting payment by the probabilities of achieving each scenario. In order to calculate an appropriate risk-adjusted discount rate for the earn out, the Company calculated the weighted average cash-flows of the business based on the three scenarios and their respective weightings. The Company then calculated an implied internal rate of return (“IRR”) of 29.8%, which is the discount rate necessary in order to reconcile the weighed cash-flows of the three scenarios to the total purchase price including the earn out payment. The earn out payment was then discounted by the 29.8% IRR. Based on these methods and the Company’s initial assessment of meeting those revenue levels in 2015, an earn out liability of \$36,000 was recorded as a liability during purchase accounting. This was re-measured in the subsequent quarters, resulting in a benefit of \$2,527 during the year ended December 31, 2016 and additional charges of \$422,649 during the year ended December 31, 2015. During the quarter ended March 31, 2016, the Company paid \$415,858 in the form of \$207,929 in cash and 53,924 shares of common stock in full settlement of the earn out liability to the former GraphicMail shareholders.

Additionally, in March 2016, the Company received \$175,970 in cash and 20,000 shares of Company stock (valued at \$84,000) from the GraphicMail escrow fund related to an indemnified claim for unrecorded liabilities at the time of the acquisition. The total value of the claim of \$259,970 was recorded as a gain in other income (expense), net during the year ended December 31, 2016. The Company accounted for the receipt of 20,000 shares as treasury stock with a carrying value of \$84,000.

Note 4: Asset Purchase Agreements

During 2015 and 2016, the Company entered into separation agreements with several third-party GraphicMail resellers to terminate the reseller arrangements and for the Company to purchase the customer relationships that each had accumulated as a GraphicMail reseller. Pursuant to the terms of the separation agreements, the Company will make cash payments to the resellers in exchange for the rights to the customer relationships. The Company accounted for these purchases as intangible asset acquisitions. The aggregate estimated purchase price for the intangible assets acquired during the years ended December 31, 2016 and December 31, 2015 was approximately \$143,000 and \$574,000, respectively, combining for an aggregate total of \$717,000. As of December 31, 2016, approximately \$608,000 of the consideration had been paid and approximately \$109,000 was included in accrued liabilities on the Consolidated Balance Sheets.

Note 5: Dispositions

On June 27, 2016, the Company completed the sale of the assets and deferred revenue liabilities of its SMTP email relay business (“SMTP”) to the Electric Mail Company for approximately \$15.0 million. Of the total proceeds from the sale of SMTP, approximately \$1.0 million in cash is held in escrow to be received in July 2017, and recorded in Other current assets at December 31, 2016. In conjunction with the sale, the Company also entered into a transition services agreement (the “TSA”) with the buyer to assist in the transition of operations over a six-month period, with an option to extend for an additional six months. Pursuant to the terms of the transition services agreement, in exchange for assisting in the transfer of operations, the Company may continue utilizing the SMTP email relay platform for its email sending needs at no cost. Although no cash was exchanged for the services performed by the parties to the TSA, the Company recorded the estimated cost to utilize the SMTP sending platform as a cost of sale and recorded a benefit to Other income (expense), net for the value of services provided to the Electric Mail Company. Also, in conjunction with the sale, the Company abandoned a software asset that was not acquired, but will not be utilized by the Company in the future. The Company recorded a gain on the sale of SMTP of approximately \$9.8 million, net of tax of \$5.2 million in the second quarter of 2016.

Pursuant to the reporting requirements of ASC 205-20, *Presentation of Financial Statements – Discontinued Operations*, the Company has determined that the SMTP business qualifies for presentation as a discontinued operation because it represents a component of our entity and the sale of SMTP represents a strategic shift in our business plans. Therefore, the Company has reclassified the assets and liabilities of the SMTP business as held for sale in the accompanying Consolidated Balance Sheets and presented the operating results of SMTP (for periods prior to the sale) as discontinued operations, net of tax, in the accompanying Consolidated Statements of Comprehensive Income (Loss) and Consolidated Statements of Cash Flows.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Financial information for the SMTP email relay business for the year ended December 31, 2016 and 2015, are presented in the following table:

	Three Months Ended December 31,		Year Ended December 31,	
	2016	2015	2016	2015
Revenue	\$ -	\$ 1,367,252	\$ 2,746,378	\$ 5,404,870
Cost of services	-	276,465	642,013	1,169,175
Gross profit	-	1,090,787	2,104,365	4,235,695
Operating expenses:				
Sales and marketing	-	43,013	177,265	789,308
Research and development	-	127,198	152,898	429,318
General and administrative	-	204,368	474,048	817,081
Total operating expenses	-	374,579	804,211	2,035,707
Operating income	-	716,208	1,300,154	2,199,988
Other income (expense), net, before gain on sale	-	-	-	-
Income before income taxes, before gain on sale	-	716,208	1,300,154	2,199,988
Income tax expense	-	267,719	447,675	822,356
Net income, before gain on sale	\$ -	\$ 448,489	\$ 852,479	\$ 1,377,632
Gain on sale of discontinued operations, net of tax expense of \$5,154,026	-	-	9,814,506	-
Income from discontinued operations, net of income taxes	\$ -	\$ 448,489	\$ 10,666,985	\$ 1,377,632

The financial information above includes the financial results for the SMTP email relay business through June 27, 2016, plus any residual costs incurred after June 27, 2016 related to the transition of the business to the buyer. The results are comprised of revenue and costs directly attributable to the SMTP email relay business as well as allocated costs for resources that have historically had shared roles in our consolidated operations. For resources performing shared roles, cost allocations have been created based on estimated work performed and job activities. Although our SharpSpring and GraphicMail products had utilized the SMTP email relay sending platform prior to the disposition, no intercompany revenues have been reflected in the SMTP email relay business operating results related to the use of the email sending platform by our other product lines.

The assets and liabilities of discontinued operations are stated separately as of December 31, 2015, in the Consolidated Balance Sheets and are comprised of the following items:

	December 31, 2015
Assets	
Other current assets	\$ 45,697
Total current assets held for sale	45,697
Property and equipment, net	251,565
Total assets held for sale	\$ 297,262
Liabilities and Shareholders' Equity	
Deferred revenue	369,941
Total liabilities held for sale	\$ 369,941

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Note 6: Goodwill and Other Intangible Assets

Goodwill and acquired intangible assets are initially recorded at fair value and measured periodically for impairment. In performing the Company's annual impairment analysis during the fourth quarters of 2016 and 2015, the Company determined that the carrying amount of the Company's goodwill was recoverable and no additional tests were required. Since some of the goodwill is denominated in foreign currencies, relatively minor changes to the goodwill balance occur over time due to changes in foreign exchange rates. During 2016, changes in foreign exchange rates caused a reduction to goodwill of \$36,539.

In addition to our annual goodwill impairment review, the Company also performs periodic reviews of the carrying value and amortization periods of other acquired intangible assets. If indicators of impairment are present, an estimate of the undiscounted cash flows that the specific asset is expected to generate must be made to ensure that the carrying value of the asset can be recovered. These estimates involve significant subjectivity.

During the year ended December 31, 2016, the Company recorded an impairment loss of \$1,459,541 related to the impaired recovery of its GraphicMail customer relationship assets due to significant erosion of that customer base following the migration onto the SharpSpring Mail+ product. During the year ended December 31, 2015, the Company recorded an impairment of its GraphicMail technology and trade name assets in the amount of \$1,310,386 related to the decision to migrate customers off of the GraphicMail platform and abandon the trade name in 2016. The impairments have been included in the Accumulated Amortization referenced below.

The following tables set forth the information for intangible assets subject to amortization and for intangible assets not subject to amortization.

	As of December 31, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Amortized intangible assets:			
Trade names	\$ 326,992	\$ (256,988)	\$ 70,004
Technology	3,686,270	(2,001,270)	1,685,000
Customer relationships	4,024,005	(2,928,374)	1,095,631
Unamortized intangible assets:	8,037,267	(5,186,632)	2,850,635
Goodwill			8,845,394
Total intangible assets			\$ 11,696,029

	As of December 31, 2015		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Amortized intangible assets:			
Trade names	\$ 367,800	\$ (245,551)	\$ 122,249
Technology	3,993,089	(1,888,516)	2,104,573
Customer relationships	4,175,479	(883,996)	3,291,483
Unamortized intangible assets:	8,536,368	(3,018,063)	5,518,305
Goodwill			8,881,933
Total intangible assets			\$ 14,400,238

Estimated amortization expense for 2017 and subsequent years is as follows:

2017	\$ 514,627
2018	435,996
2019	435,996
2020	435,996
2021	435,996
Thereafter	592,024
Total	\$ 2,850,635

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Amortization expense, excluding impairments, for the years ended December 31, 2016 and 2015 was \$1,360,105 and \$1,508,616, respectively.

Note 7: Restructuring Costs

During the year ended December 31, 2016, in an effort to consolidate operations into one primary office, the Company executed a plan to close its South African offices in Cape Town and Johannesburg and terminate approximately 50 resources based in those offices. All employees were notified of the restructuring during the month of September 2016. The Company recorded pre-tax restructuring expenses associated with severance, asset write offs and contract termination expenses of \$294,249 in 2016 as follows:

Cost of services	\$	83,544
Sales and marketing		102,904
Research and development		30,693
General and administrative		77,108
	<u>\$</u>	<u>294,249</u>

At December 31, 2016, our remaining liability for restructuring expenses was as follows:

Facility closure costs	\$	10,705
Accrued contract termination fees		-
Accrual balance - December 31, 2016	<u>\$</u>	<u>10,705</u>

A rollforward of the activity in the restructuring accrual during the period was as follows:

Accrual balance - December 31, 2015	\$	-
Amounts charged to expense		294,249
Payments charged against accrual		(283,544)
Accrual balance - December 31, 2016	<u>\$</u>	<u>10,705</u>

During the year ended December 31, 2015, the Company incurred restructuring charges of approximately \$528,000, primarily associated with the departure of its former Chief Executive Officer. There was no remaining liability as of December 31, 2015.

Note 8: Credit Facility

In March 2016, the Company entered into a \$2.5 million revolving loan agreement (the "Loan Agreement") with Western Alliance Bank. The facility matures on March 21, 2018 and has no mandatory amortization provisions and is payable in full at maturity. Loan proceeds accrue interest at the higher of Western Alliance Bank's Prime interest rate (3.75% as of December 31, 2016) or 3.5%, plus 1.75%. The Loan Agreement is collateralized by a lien on substantially all of the existing and future assets of the Company and secured by a pledge of 100% of the capital stock of SharpSpring Technologies, Inc. and Quattro Hosting, LLC and a 65% pledge of the Company's foreign subsidiaries' stock. The Loan Agreement subjects the Company to a number of restrictive covenants, including financial and non-financial covenants customarily found in loan agreements for similar transactions. The Loan Agreement also restricts our ability to pay cash dividends on our common stock. During June 2016, the Company amended the Loan Agreement to modify its financial covenants and allow for the sale of the SMTP business assets. There are no amounts outstanding under the Loan Agreement as of December 31, 2016 and no events of default have occurred to date. As of December 31, 2016, based on the borrowing base calculations \$1,633,721 was available for withdrawal under the Loan Agreement.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Note 9: Shareholders' Equity

On, January 28, 2015, the Company transferred 30,000 warrants issued on August 1, 2013 in connection with a consulting agreement in exchange for the Company issuing 5,000 shares of Company common stock.

On May 18, 2015, the Company entered into a subscription agreement with investors for the sale of an aggregate of 363,909 shares of the Company's common stock, at a price of \$5.50 per share and an aggregate value of \$2.0 million, which shares have been registered with the Securities and Exchange Commission on the Company's registration statement on Form S-3. The closing occurred on May 21, 2015.

On May 18, 2015, the Company entered into a subscription agreement with RCTW for the issuance of 545,455 shares of common stock to RCTW for an aggregate value of \$3.0 million, which is in satisfaction of an equal amount of the earn-out due and payable by the Company to RCTW under the Asset Purchase Agreement dated August 12, 2014 between the Company and RCTW. The closing occurred on May 21, 2015.

In August 2015 the Company completed a registered public offering, which raised \$3.4 million (net of expenses) by offering 800,000 shares of common stock for sale.

In March 2016, the Company issued 53,924 shares of common stock to the former owners of GraphicMail in satisfaction of the GraphicMail stock-based earn out (see Note 3). Additionally, in March 2016, the Company received 20,000 shares of stock from the GraphicMail escrow fund related to an indemnified claim.

In June 2016, the Company issued 1,039,636 shares of common stock to the RCTW, LLC shareholders to satisfy the remaining stock-based portion of the SharpSpring earn out (see Note 3).

Note 10: Changes in Accumulated Other Comprehensive Income (Loss)

	Foreign Currency Translation Adjustment
Balance as of December 31, 2015	\$ (142,613)
Other comprehensive income (loss) prior to reclassifications	-
Amounts reclassified from accumulated other comprehensive income	-
Tax effect	-
Net current period other comprehensive loss	(302,442)
Balance as of December 31, 2016	<u>\$ (445,055)</u>

Note 11: Net Loss Per Share

Computation of net income per share is as follows:

	Three Months Ended December 31,		Year Ended December 31,	
	2016	2015	2016	2015
Net income (loss)	\$ (2,188,332)	\$ (3,918,587)	\$ 4,951,010	\$ (8,244,302)
Basic weighted average common shares outstanding	8,356,735	7,229,950	7,895,197	6,354,134
Add incremental shares for:				
Warrants	-	-	-	-
Stock options	-	-	-	-
Diluted weighted average common shares outstanding	<u>8,356,735</u>	<u>7,229,950</u>	<u>7,895,197</u>	<u>6,354,134</u>
Net loss per share:				
Basic	<u>\$ (0.26)</u>	<u>\$ (0.54)</u>	<u>\$ 0.63</u>	<u>\$ (1.30)</u>
Diluted	<u>\$ (0.26)</u>	<u>\$ (0.54)</u>	<u>\$ 0.63</u>	<u>\$ (1.30)</u>

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the year ended December 31, 2016, 1,128,368 stock options and 170,973 warrants were excluded from diluted net loss per share, because the effect of including these potential shares was anti-dilutive. For the year ended December 31, 2015, 1,066,710 stock options and 170,973 warrants were excluded from diluted net loss per share, because the effect of including these potential shares was anti-dilutive.

Pursuant to ASC 260, *Earnings Per Share*, since a loss is reported from continuing operations, diluted net loss per share has been computed with the same average common shares outstanding as basic net loss per share, even during periods when the discontinued operations provide for an overall consolidated net income.

Note 12: Income Taxes

Income taxes for years ended December 31, is summarized as follows:

	Year Ended December 31,	
	2016	2015
Current provision	\$ 3,451,571	\$ (519,437)
Payable true-up	101,783	119,838
Deferred provision (benefit)	179,159	861,546
Net income tax provision	3,732,513	461,947
Less: net income tax provision from discontinued operations	(5,601,701)	(822,356)
Net income tax provision from continuing operations	<u>\$ (1,869,188)</u>	<u>\$ (360,409)</u>

	Year Ended December 31,	
	2016	2015
From continuing operations:		
Federal	\$ (2,366,022)	\$ (133,046)
State	32,928	(227,988)
Foreign	463,906	625
Net income tax provision	<u>\$ (1,869,188)</u>	<u>\$ (360,409)</u>
From discontinued operations:		
Federal	\$ 5,531,353	\$ 753,996
State	70,348	68,360
Foreign	-	-
Net income tax provision	<u>\$ 5,601,701</u>	<u>\$ 822,356</u>

A reconciliation of income tax for continuing operations computed at the U.S. statutory rate to the effective income tax rate is as follows:

	2016		2015	
	Amount	Percent	Amount	Percent
Federal statutory rates on continuing operations	\$ (2,578,955)	34%	\$ (3,393,997)	34%
State income taxes, net of federal benefit	32,928	0%	(227,988)	2%
Permanent differences	621,683	-8%	27,691	0%
Other	375,738	1%	133,295	-1%
Credits	(164,297)	-5%	-	0%
Foreign	29,040	0%	193,108	-2%
Valuation Allowance	(185,325)	2%	2,907,482	-29%
Effective rate from continuing operations	<u>\$ (1,869,188)</u>	<u>25%</u>	<u>\$ (360,409)</u>	<u>4%</u>

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The following is a summary of the components of the Company's deferred tax assets:

	December 31,	
	2016	2015
Deferred tax assets:		
Accrual to cash	\$ 184,958	\$ 264,031
Stock-based compensation	595,576	550,299
Depreciation	-	43,002
Intangibles	1,140,222	1,780,593
NOL	939,725	302,273
Unrealized gains	-	432
Valuation allowance	(2,560,975)	(2,923,985)
Deferred tax assets, net of valuation allowance	299,506	16,645
Deferred tax liabilities:		
Asset dispositions	(309,479)	-
Depreciation	(152,542)	-
Other	16	(7,598)
Deferred tax liabilities	(462,005)	(7,598)
Net deferred tax assets (liabilities)	<u>\$ (162,499)</u>	<u>\$ 9,047</u>

The company has foreign net operating loss carryforwards of approximately \$939,725 and \$692,993 as of December 31, 2016 and 2015, respectively. Depending on the jurisdiction, some of these net operating loss carryovers will begin to expire within 3 years, while other net operating losses can be carried forward indefinitely as long as the company is trading.

Valuation Allowance

We record a deferred tax asset if we believe that it is more likely than not that we will realize a future tax benefit. Ultimate realization of any deferred tax asset is dependent on our ability to generate sufficient future taxable income in the appropriate tax jurisdiction before the expiration of carryforward periods, if any. Our assessment of deferred tax asset recoverability considers many different factors including historical and projected operating results, the reversal of existing deferred tax liabilities that provide a source of future taxable income, the impact of current tax planning strategies and the availability of future tax planning strategies. We establish a valuation allowance against any deferred tax asset for which we are unable to conclude that recoverability is more likely than not. This is inherently judgmental, since we are required to assess many different factors and evaluate as much objective evidence as we can in reaching an overall conclusion. The particularly sensitive component of our evaluation is our projection of future operating results since this relies heavily on our estimates of future revenue and expense levels by tax jurisdiction.

At December 31, 2016 we have established a \$2.6 million valuation allowance against certain deferred tax assets given the uncertainty of recoverability of these amounts.

In making our assessment of deferred tax asset recoverability, we considered our historical financial results, our projected future financial results, the planned reversal of existing deferred tax liabilities and the impact of any tax planning actions. Based on our analysis we noted both positive and negative factors relative to our ability to support realization of certain deferred tax assets. However, based on the weighting of all the evidence, including the near term effect on our income projections of investments we are making in our team, product and systems infrastructure, we concluded that it was more likely than not that the majority of our deferred tax assets related to temporary differences and net operating losses may not be recovered. The establishment of a valuation allowance has no effect on our ability to use the underlying deferred tax assets prior to expiration to reduce cash tax payments in the future to the extent that we generate taxable income.

Note 13: Defined Contribution Retirement Plan

Starting in 2016, we offered our U.S. employees the ability to participate in a 401(k) plan. Eligible U.S. employees may contribute up to 60% of their eligible compensation, subject to limitations established by the Internal Revenue Code. The Company contributes a matching contribution equal to 100% of each such participant's contribution up to the first 3% of their annual eligible compensation. During 2015, we provided similar matching contributions into eligible U.S. employees' SIMPLE IRA accounts. We charged \$108,228 and \$69,924 to expense in the years ended December 31, 2016 and 2015, respectively, associated with our matching contribution for those years.

Note 14: Related Party Transactions

Intercompany transactions have been eliminated in our consolidated financial statements. There were no material related party transactions for the years ended December 31, 2016 or 2015.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Note 15: Stock-Based Compensation

From time to time, the Company grants stock option awards to officers and employees and grants stock awards to directors as compensation for their service to the Company.

In November 2010, the Company adopted the 2010 Stock Incentive Plan (“the Plan”) which was amended in April 2011, August 2013, April 2014 and February 2016. As amended, up to 1,650,000 shares of common stock are available for issuance under the Plan. The Plan provides for the issuance of stock options and other stock-based awards.

Stock Options

Stock option awards under the Plan have a 10-year maximum contractual term and must be issued at an exercise price of not less than 100% of the fair market value of the common stock at the date of grant. The Plan is administered by the Board of Directors, which has the authority to determine to whom options may be granted, the period of exercise and what other restrictions, if any, should apply. Vesting for awards granted to date under the Plan is principally over four years from the date of the grant, with 25% of the award vesting after one year with monthly vesting thereafter.

Option awards are valued based on the grant date fair value of the instruments, net of estimated forfeitures, using a Black-Scholes option pricing model with the following assumptions:

	Year Ended December 31,	
	2016	2015
Volatility	38% - 50%	29% - 39%
Risk-free interest rate	1.12% - 1.93%	1.31% - 1.94%
Expected term	6.25 years	6.25 years

The weighted average grant date fair value of stock options granted during the year ended December 31, 2016 was \$2.06.

For grants prior to January 1, 2015, the volatility assumption was based on historical volatility of similar sized companies due to lack of historical data of the Company’s stock price. For all grants subsequent to January 1, 2015, the volatility assumption reflects the Company’s historic stock volatility for the period of February 1, 2014 forward, which is the date the Company’s stock started actively trading. The risk free interest rate was determined based on treasury securities with maturities equal to the expected term of the underlying award. The expected term was determined based on the simplified method outlined in Staff Accounting Bulletin No. 110.

Stock option awards are expensed on a straight-line basis over the requisite service period. During the year ended December 31, 2016 and 2015, the Company recognized expense of \$510,002 and \$689,871, respectively, associated with stock option awards. At December 31, 2016, future stock compensation expense associated with stock options (net of estimated forfeitures) not yet recognized was \$1,115,816 and will be recognized over a weighted average remaining vesting period of 2.8 years. The following summarizes stock option activity for the year ended December 31, 2016:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding at December 31, 2015	1,066,360	\$ 5.37	7.4	\$ 64,500
Granted	264,750	4.32		
Exercised	(3,088)	3.96		
Forfeited	(199,654)	5.40		
Outstanding at December 31, 2016	<u>1,128,368</u>	<u>\$ 5.12</u>	<u>7.0</u>	<u>\$ 514,439</u>
Exercisable at December 31, 2016	<u>527,539</u>	<u>\$ 5.32</u>	<u>5.0</u>	<u>\$ 205,828</u>

The total intrinsic value of stock options exercised during the year ended December 31, 2016 was \$2,368.

SHARPSRING, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Stock Awards

During the year ended December 31, 2016 and 2015, the Company issued 50,976 and 41,068 shares, respectively, to non-employee directors as compensation for their service on the board. Such stock awards are immediately vested.

Stock awards are valued based on the closing price of our common stock on the date of grant, and compensation cost is recorded immediately if there is no vesting period or on a straight line basis over the vesting period. The total fair value of stock awards granted, vested and expensed during the year ended December 31, 2016 and 2015 was \$220,530 and \$182,060, respectively. As of December 31, 2016, there was no unrecognized compensation cost related to stock awards.

Note 16: Warrants

On January 30, 2014, in connection with an \$11.5 million financing transaction, the Company issued 80,000 warrants to purchase common stock at an exercise price of \$7.81 per share with a term of 5 years. The fair value of the warrants was determined using the Black-Scholes option valuation model. The warrants expire on January 30, 2020 and have a remaining contractual life of 3.1 years as of December 31, 2016. These warrants became exercisable on January 30, 2015.

On, January 28, 2015, the Company cancelled 30,000 warrants originally issued on August 1, 2013 in connection with a consulting agreement in exchange for the Company issuing 5,000 shares of restricted Company common stock.

The following table summarizes information about the Company's warrants at December 31, 2016:

	<u>Number of Units</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Term</u>	<u>Intrinsic Value</u>
Outstanding at December 31, 2015	170,973	\$ 6.26	5.6	\$ -
Granted	-	-		
Cancelled	-	-		
Outstanding at December 31, 2016	<u>170,973</u>	<u>\$ 6.26</u>	<u>4.6</u>	<u>\$ 33,660</u>
Exercisable at December 31, 2016	<u>170,973</u>	<u>\$ 6.26</u>	<u>4.6</u>	<u>\$ 33,660</u>

No warrants were issued in 2016 or 2015.

Note 17: Commitments and Contingencies

Litigation

The Company may from time to time be involved in legal proceedings arising from the normal course of business. The Company is not a party to any litigation of a material nature.

Operating Leases and Service Contracts

The Company rents its facilities with leases ranging from month-to-month to several years in duration, and records lease expense as incurred. The Company rent expense associated with its leased facilities of \$500,183 and \$352,265 during the years ended December 31, 2016 and December 31, 2015, respectively.

Most of its service contracts are on a month-to-month basis, however, some contracts and agreements extend out to longer periods. Future minimum lease payments and payments due under non-cancelable service contracts are as follows as of December 31, 2016:

2017	\$ 745,563
2018	448,918
2019	373,015
2020	382,884
2021	292,843
Thereafter	-
	<u>\$ 2,243,223</u>

Employment Agreements

The Company has employment agreements with several members of its leadership team and executive officers.

INDEX TO EXHIBITS

Exhibit Number	Title of Document	Location
3.1	Certificate of Incorporation	Incorporated by reference to our Form S-1 filed on December 2, 2010
3.2	Amendment to Certificate of Incorporation	Incorporated by reference to our Form 8-K filed on December 17, 2013
3.3	Amendment to Certificate of Incorporation	Incorporated by reference to our Form 8-K filed December 1, 2015
3.4	Bylaws	Incorporated by reference to our Registration Statement on Form S-1 filed on December 2, 2010
10.1	Extension Agreement dated March 15, 2016, by and between the Company and RCTW, LLC.	Incorporated by reference to our Form 8-K filed on March 17, 2016
10.2	Asset Purchase Agreement dated August 12, 2014, by and between the Company and RCTW, LLC	Incorporated by reference to our Form 8-K filed on August 15, 2014
10.3	Loan Agreement dated March 21, 2016, by and among SharpSpring, Inc., Quattro Hosting LLC, SharpSpring Technologies, Inc. and Western Alliance Bank	Incorporated by reference to our Form 8-K filed on March 22, 2016
10.4	Intellectual Property Security Agreement dated March 21, 2016, by and among SharpSpring, Inc., Quattro Hosting LLC, SharpSpring Technologies, Inc. and Western Alliance Bank	Incorporated by reference to our Form 8-K filed on March 22, 2016
10.5	Amendment to 2010 Employee Stock Plan	Incorporated by reference to Appendix A to the Company's Definitive Schedule 14A filed on April 15, 2016
10.6	2010 Employee Stock Plan	Incorporated by reference to Form S-1 filed on December 2, 2010
10.7	Asset Purchase Agreement dated June 27, 2016, by and between SharpSpring, Inc. and The Electric Mail Company	Incorporated by reference to our Form 8-K filed June 28, 2016
10.8	Loan and Security Modification Agreement dated June 24, 2016, by and among SharpSpring, Inc., Quattro Hosting LLC, SharpSpring Technologies, Inc. and Western Alliance Bank	Incorporated by reference to our Form 8-K filed on June 28, 2016
10.9	Travis Whitton Employee Agreement Amendment dated June 19, 2015	Incorporated by reference to our Form 8-K filed on July 8, 2016
10.10	Travis Whitton Employee Agreement dated August 15, 2014	Incorporated by reference to our Form 8-K filed on July 8, 2016
14.1	Code of Ethics and Business Standards	Incorporated by reference to our Form 8-K filed on January 14, 2014
21.1	Subsidiaries of the registrant	Incorporated by reference to Note 3 of the Financial Statements included in Part II – Item 7 of this Form 10-K
31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
101.1	XBRL	Filed herewith

EXHIBIT 31.1

CERTIFICATION

I, Richard A. Carlson, certify that:

1. I have reviewed this Annual Report on Form 10-K of SharpSpring, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2017

Signature: */s/ Richard A. Carlson*

Richard A. Carlson
Principal Executive Officer

EXHIBIT 31.2

CERTIFICATION

I, Edward Lawton, certify that:

1. I have reviewed this Annual Report on Form 10-K of SharpSpring, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 30, 2017

Signature: */s/ Edward Lawton*

Edward Lawton
Chief Financial Officer
(Principal Financial Officer)

EXHIBIT 32.1

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

In connection with the Annual Report of SharpSpring, Inc. (the "Company") on Form 10-K for the year ended December 31, 2016, as filed with the Securities and Exchange Commission (the "Report"), I, Richard A. Carlson, Principal Executive Officer of the Company, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that, to my knowledge:

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

Date: March 30, 2017

/s/ Richard A. Carlson

Richard A. Carlson
Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 32.2

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

In connection with the Annual Report of SharpSpring, Inc. (the "Company") on Form 10-K for the year ended December 31, 2016, as filed with the Securities and Exchange Commission (the "Report"), I, Edward Lawton, Principal Financial Officer of the Company, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that, to my knowledge:

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

Date: March 30, 2017

/s/ Edward Lawton

Edward Lawton
Chief Financial Officer
(Principal Financial Officer)
