ELLIE MAE INC
Form 10-Q
August 08, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2012

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: 001-35140

ELLIE MAE, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-3288780**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
4155 Hopyard Road, Suite 200	
Pleasanton, California	**94588**
(Address of principal executive offices)	**(Zip Code)**

(925) 227-7000

(Registrant s telephone number, including area code)

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

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

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 small reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if smaller reporting company)	Smaller reporting company	¨

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

Indicate the number of shares outstanding of each of the registrant s classes of common stock as of the latest practicable date:

As of July 31, 2012:

Class	**Number of Shares**
Common Stock, $0.0001 par value	25,190,676

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PART I FINANCIAL INFORMATION

ITEM 1 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Ellie Mae, Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands, except share and per share amounts)

	June 30, 2012	December 31, 2011
Assets		
Current assets		
Cash and cash equivalents	$ 30,924	$ 23,732
Short-term investments	2,920	1,933
Accounts receivable, net of allowances for doubtful accounts of $18 and $47, as of June 30, 2012 and December 31, 2011, respectively	7,911	6,819
Prepaid expenses and other	3,269	1,381
Note receivable	1,000	1,000
Total current assets	46,024	34,865
Property and equipment, net	8,353	5,539
Deposits and other assets	135	135
Note receivable	13	15
Other intangible assets, net	7,348	8,166
Goodwill	51,051	51,051
Total assets	$ 112,924	$ 99,771
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$ 2,470	$ 2,255
Accrued and other current liabilities	6,420	4,931
Acquisition holdback, net of discount	2,990	2,948
Deferred revenue	4,198	4,548
Deferred rent	231	212
Leases payable	7	6
Total current liabilities	16,316	14,900
Deferred revenue, net of current portion		62
Deferred rent, net of current portion	502	624
Acquisition holdback, net of current portion and discount	4,792	4,725
Other long-term liabilities	618	598
Leases payable, net of current portion		4
Total liabilities	22,228	20,913
Commitments and contingencies (Note 6)		
Stockholders' equity:		
	2	2

Common stock, $0.0001 par value per share; 140,000,000 authorized shares, 21,627,127 and 21,019,590 shares issued and outstanding as of June 30, 2012 and December 31, 2011, respectively		
Additional paid-in capital	119,209	116,012
Accumulated deficit	(28,515)	(37,156)
Total stockholders' equity	90,696	78,858
Total liabilities and stockholders' equity	$ 112,924	$ 99,771

See accompanying notes to these condensed consolidated financial statements.

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Ellie Mae, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(UNAUDITED)

(in thousands, except share and per share amounts)

	Three months ended June 30, 2012	Three months ended June 30, 2011	Six months ended June 30, 2012	Six months ended June 30, 2011
Revenues	$ 23,569	$ 11,464	$ 44,475	$ 22,067
Cost of revenues	5,283	3,512	10,540	6,875
Gross profit	18,286	7,952	33,935	15,192
Operating expenses:				
Sales and marketing	4,232	2,497	8,232	4,948
Research and development	4,299	2,606	8,432	5,410
General and administrative	4,496	2,922	8,172	5,727
Total operating expenses	13,027	8,025	24,836	16,085
Income (loss) from operations	5,259	(73)	9,099	(893)
Other income (expense), net	(18)	47	(38)	79
Income (loss) before income taxes	5,241	(26)	9,061	(814)
Income tax provision	242	14	420	25
Net income (loss)	$ 4,999	$ (40)	$ 8,641	$ (839)
Net income (loss) per share of common stock:				
Basic	$ 0.23	$ (0.00)	$ 0.40	$ (0.08)
Diluted	$ 0.21	$ (0.00)	$ 0.38	$ (0.08)
Weighted average common shares used in computing net income (loss) per share of common stock:				
Basic	21,610,578	17,137,819	21,507,683	10,412,469
Diluted	23,296,653	17,137,819	22,939,744	10,412,469
Comprehensive income (loss)	$ 4,999	$ (40)	$ 8,641	$ (839)

See accompanying notes to these condensed consolidated financial statements.

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Ellie Mae, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(in thousands)

	Six months ended June 30, 2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 8,641	$ (839)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	1,362	838
Provision for uncollectible accounts receivable	8	295
Amortization of other intangible assets	818	223
Amortization of discount related to holdback	109	
Stock-based compensation	1,395	757
Loss on sale of property and equipment	20	
Excess tax benefit from exercise of stock options	(181)	
Changes in operating assets and liabilities:		
Accounts receivable	(1,100)	(869)
Prepaid expenses and other	(1,232)	(361)
Deposits and other assets		530
Accounts payable	(802)	745
Accrued and other liabilities	1,690	(313)
Deferred revenue	(412)	(216)
Deferred rent	(103)	(95)
Net cash provided by operating activities	10,213	695
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of property and equipment	(3,845)	(2,882)
Proceeds from sale of property and equipment	10	
Purchase of short-term investments	(3,473)	(3,667)
Acquisitions, net of cash acquired		(1,000)
Maturities of short-term investments	2,486	3,777
Other investing activities, net	2	(18)
Net cash used in investing activities	(4,820)	(3,790)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from initial public offering net of issuance costs		23,667
Payment of capital lease obligations	(3)	(102)
Proceeds from issuance of common stock under employee stock plans	1,621	318
Excess tax benefit from exercise of stock options	181	
Net cash provided by financing activities	1,799	23,883
NET INCREASE IN CASH AND CASH EQUIVALENTS	7,192	20,788
CASH AND CASH EQUIVALENTS, Beginning of period	23,732	14,349
CASH AND CASH EQUIVALENTS, End of period	$ 30,924	$ 35,137

Supplemental disclosure of non-cash investing and financing activities:				
Property and equipment purchases not yet paid	$	673	$	310
Deferred offering costs not yet paid	$	344	$	657
Conversion of preferred stock to common stock	$		$	82,670

See accompanying notes to these condensed consolidated financial statements.

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Ellie Mae, Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 Description of Business

Ellie Mae, Inc. (the Company or Ellie Mae) was originally incorporated in California in August 1997 and reincorporated in Delaware in November 2009. The Company provides business automation software for a large segment of the mortgage industry in the United States. Its on-demand, technology-enabled software solutions help streamline and automate the process of originating and funding new mortgage loans, thereby increasing efficiency, facilitating regulatory compliance and reducing documentation errors.

NOTE 2 Basis of Presentation and Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company s Annual Report on Form 10-K, which was filed with the SEC on March 28, 2012 (2011 Form 10-K).

The condensed consolidated balance sheet as of December 31, 2011, included herein, was derived from the audited financial statements as of that date but does not include all disclosures, including notes required by GAAP.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial positions, results of operations and cash flows for the interim periods, but are not necessarily indicative of the results of operations to be anticipated for the full year 2012 or any future period.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Ellie Mae, Inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with 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 financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Significant Accounting Policies

The Company s significant accounting policies are described in Note 2 of the Notes to Consolidated Financial Statements in its 2011 Form 10-K. There have been no significant changes to these policies.

Software and Website Development Costs

The Company capitalizes costs related to internal-use software and website application development. Costs related to preliminary project activities and post implementation activities are expensed as incurred. Internal-use software is amortized on a straight-line basis over its estimated useful life, generally three years. Management evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets. The capitalized costs are included in Property and equipment in the accompanying condensed consolidated balance sheets. In each case the software or website application is for internal needs and the Company does not plan to market the software externally. For the six months ended June 30, 2012, the Company capitalized approximately $0.2 million of software and website application development costs. There were no costs capitalized during the six months ended June 30, 2011. There was no amortization recorded in the six months ended June 30, 2012 and 2011, respectively.

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Goodwill

Goodwill is evaluated for impairment annually in the fourth quarter of the Company s fiscal year and whenever events or changes in circumstances indicate the carrying value of goodwill may not be recoverable. Triggering events that may indicate possible impairment include, but are not limited to, a significant adverse change in customer demand or business climate that could affect the value of goodwill or result in a significant decrease in expected cash flows.

Pursuant to recent authoritative accounting guidance, the Company may elect to assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If the Company determines that it is more likely than not that a reporting unit s fair value is less than its carrying value, then the two-step assessment is performed. The first step, identifying a potential impairment, compares the fair value of the reporting unit with its carrying value. If the carrying value exceeds its fair value, the second step would need to be conducted; otherwise, no further steps are necessary as no potential impairment exists. The second step, measuring the impairment loss, compares the implied fair value of the goodwill with the carrying value of that goodwill. Any excess of the goodwill carrying value over the respective implied fair value is recognized as an impairment loss, and the carrying value of goodwill is written down to fair value. Through June 30, 2012, no impairment of goodwill has been identified.

Revenue Recognition

The Company generates revenue primarily from on-demand and on-premise fees for software and related services. The Company re-categorized its revenues beginning with the first quarter of 2012 to on-demand revenues and on-premise revenues (see Note 10) to better align with the Company s strategic plan. On-demand revenues are revenues generated from company-hosted software subscriptions that customers access through the Internet and revenues from a small number of customers that have opted to self-host a portion of the software but pay fees based on a per closed loan, or success, basis subject to monthly base fees, which the company refers to as success-based pricing. On-demand revenues are also comprised of software services sold transactionally and Ellie Mae Network transaction fees. On-premise revenues generally are revenues generated from customer-hosted software licenses and related implementation (except for customer-hosted success-based pricing revenues included in on-demand revenues described above), training and maintenance services. Sales taxes assessed by a governmental authorities are excluded from revenue.

On-Demand Revenues

Subscription Services and Usage-Based Fee Arrangements. Subscription services and usage-based fee arrangements generally include a combination of the Company s products delivered as software-as-a-service, or SaaS, product updates and support services. These revenues generally include the following:

SaaS Encompass Revenues. The Company offers web-based access to its Encompass software for a monthly recurring fee. The Company provides the right to access its loan origination software and handles the responsibility of managing the servers, providing robust security, backing up the data and applying updates; however, except where customers self-host a portion of the software in a success-based pricing structure, customers under these arrangements may not take possession of the software at any time during the term of the agreement. Associated set-up fees are recognized ratably over the life of the relationship with its customers, which is generally the life of the contract. Contracts generally range from one to three years. Alternatively, customers can elect to pay on a per closed loan, or success, basis subject to monthly base fees. Success-based pricing contracts generally have a term of two to three years. Monthly base fees are recognized as the service is performed and additional revenues arising from closed loans are recognized when the loans close or in the subsequent month when revenue recognition criteria are met. This offering also includes CenterWise for Encompass as an integrated component, which is a combined element of the arrangement that is delivered in conjunction with the SaaS Encompass offering and therefore is not accounted for separately.

CenterWise for Encompass Licensees. The Company provides a bundled offering of electronic document management and websites used for customer relationship management. Generally, the Company recognizes revenue for CenterWise as the service is performed, except when CenterWise is automatically included as an integrated component of the SaaS Encompass offering, in which case the associated revenue is recognized as described above.

Services Revenues. The Company has entered into agreements with customers that provide mortgage related and other business services, including automated documentation preparation and compliance reports. Revenue is recognized only when the price is fixed or determinable, persuasive evidence of an arrangement exists, the service is performed and collectability of the resulting receivable is reasonably assured.

Transaction Revenues. The Company has entered into agreements with various lenders, service providers and certain government agencies participating in the mortgage origination process that provides them access to, and interoperability with, mortgage originators on the Ellie Mae Network. Under these agreements, the Company has the opportunity to earn transaction fees when transactions are processed through the Company s Ellie Mae Network. Transaction revenues are recognized when there is evidence that the qualifying transactions have occurred on the Ellie Mae Network and collection of the resulting receivable is reasonably assured. Associated set-up fees are recognized ratably, beginning upon completion of the integration and continuing over the remaining estimated life of the relationship with its customer, which generally is the remaining life of the contract.

On-Premise Revenues

With the exception of revenue from customers that self-host a portion of the software in a success-based pricing structure (which is recognized as described above), revenue from the sale of software licenses is recognized in the month in which the required revenue recognition criteria are met, generally in the month in which the software is delivered. Revenue is recognized when persuasive evidence of an arrangement exists, which is evidenced by a signed agreement, the product has been downloaded or delivered freight on board shipping point, the fee is fixed or determinable and collection of the resulting receivable is reasonably assured.

Revenue Recognition Methodologies

For software arrangements with multiple elements (e.g., undelivered maintenance and support contracts bundled with licenses), the Company, when vendor specific objective evidence (VSOE) is determinable, allocates revenue to the delivered elements of the arrangement using the residual value method based on objective evidence of the fair value of the undelivered elements, which is specific to the Company. When VSOE is not determinable, the Company allocates all revenue to the undelivered elements and the entire arrangement is recognized ratably over the term of the contract. The Company recognizes revenue under this model upon receipt of cash payment from the customer, if collectability is not reasonably assured. The VSOE of fair value for maintenance and support obligations related to licenses is based upon the prices paid for the separate renewal of these services by the customer. Maintenance revenues are recognized ratably over the period of the contract. License revenues include the nominal shipping and handling charges associated with most license orders. Actual shipping costs incurred by the Company are included in cost of revenues.

When subscription services and usage-based fee arrangements involve multiple elements that qualify as separate units of accounting, the Company allocates arrangement consideration in multiple-deliverable revenue arrangements at the inception of an arrangement to all deliverables based on the relative selling price method in accordance with the selling price hierarchy, which includes: (i) VSOE if available; (ii) third-party evidence (TPE) if VSOE is not available; and (iii) the best estimate of selling price (BESP) if neither VSOE nor TPE is available.

VSOE. The Company determines VSOE based on its historical pricing and discounting practices for the specific product or service when sold separately. In determining VSOE, the Company requires that a substantial majority of the selling prices for these services fall within a reasonably narrow pricing range.

TPE. When VSOE cannot be established for deliverables in multiple element arrangements, the Company applies judgment with respect to whether it can establish a selling price based on TPE. TPE is determined based on competitor prices for similar deliverables when sold separately. Generally, the Company s go-to-market strategy differs from that of its peers and its offerings contain a significant level of differentiation such that the comparable pricing of services with similar functionality cannot be obtained. Furthermore, the Company is unable to reliably determine what similar competitor services selling prices are on a standalone basis. As a result, the Company has not been able to establish selling prices based on TPE.

BESP. When the Company is unable to establish a selling price using VSOE or TPE, the Company uses BESP in its allocation of arrangement consideration. The objective of BESP is to determine the price at which the Company would transact a sale if the service was sold on a standalone basis. The Company determines BESP for deliverables by considering multiple factors including, but not limited to, prices it charges for similar offerings, market conditions, competitive landscape and pricing practices.

The Company has not historically priced its subscription services and usage-based fee arrangements within a narrow range and has limited standalone sales or renewals for these arrangements. As a result, the Company has determined that neither VSOE nor TPE are available and uses BESP to allocate the selling price to subscription services and usage-based fee deliverables.

Comprehensive Income (Loss)

Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes certain changes in equity that are excluded from net income (loss), specifically unrealized gains (losses) on short-term investments, which were insignificant for the three and six months ended June 30, 2012 and 2011. As a result, comprehensive income (loss) is equivalent to net income (loss) for all periods presented.

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NOTE 3 Net Income (Loss) Per Share of Common Stock

Net income (loss) per share of common stock is calculated by dividing net income (loss) by the weighted average shares of common stock outstanding during the period. Diluted net income (loss) per share of common stock is calculated by dividing net income (loss) by the weighted average shares of common stock outstanding and potential shares of common stock during the period. Potential shares of common stock include dilutive shares attributable to the assumed exercise of stock options, warrants and employee stock purchase plan shares using the treasury stock method and contingent issuances of common stock related to redeemable convertible preferred stock, if dilutive.

The components of net income (loss) per share of common stock were as follows:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
	(in thousand, except share and per share amounts)			
Net income (loss)	$ 4,999	$ (40)	$ 8,641	$ (839)
Basic shares:				
Weighted average common shares outstanding	21,610,578	17,137,819	21,507,683	10,412,469
Diluted shares:				
Weighted average shares used to compute basic net income (loss) per share	21,610,578	17,137,819	21,507,683	10,412,469
Effect of potentially dilutive securities:				
Warrants to purchase common stock, employee stock options and convertible preferred stock	1,686,075		1,432,061	
Weighted average shares use to compute diluted net income (loss) per share	23,296,653	17,137,819	22,939,744	10,412,469
Net income (loss) per share:				
Basic	$ 0.23	$ (0.00)	$ 0.40	$ (0.08)
Diluted	$ 0.21	$ (0.00)	$ 0.38	$ (0.08)

The following potential common shares were excluded from the computation of diluted net income (loss) per share, as their effect would have been anti-dilutive:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Warrants to purchase common stock		41,667		175,134
Employee stock options and awards	144,700	3,254,821	641,002	3,225,240
Convertible preferred stock		2,457,571		7,088,295
	144,700	5,754,059	641,002	10,488,669

Performance-based awards are included in the diluted shares outstanding for each period if the established performance criteria have been met at the end of the respective periods. However, if none of the required performance criteria have been met for such awards, the Company excludes the shares of such awards from its diluted shares outstanding. Accordingly, weighted average shares of 516,666 and 583,333 have also been excluded from the dilutive shares outstanding for each of the three and six months ended June 30, 2012 and 2011, respectively.

All of the redeemable convertible preferred stock automatically converted to common stock on a 1-for-1 basis in connection with the consummation of the Company s initial public offering (the IPO). For the three and six months ended June 30, 2011, the amount presented in the table above was the weighted average shares of common stock underlying outstanding shares of redeemable convertible preferred stock.

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NOTE 4 Financial Instruments and Fair Value Measurements

Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are classified and disclosed in one of the following three categories:

Level 1 Valuations based on quoted prices in active markets for identical assets or liabilities.

Level 2 Valuations based on other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Valuations based on inputs that are generally unobservable and typically reflect management s estimates of assumptions that market participants would use in pricing the asset or liability.

The following tables set forth by level within the fair value hierarchy the Company s financial assets that were accounted for at fair value on a recurring basis at June 30, 2012 and December 31, 2011, according to the valuation techniques the Company used to determine their values:

	Fair value at June 30, 2012	Fair value measurements using inputs considered as		
		Level 1	Level 2	Level 3
		(in thousands)		
Money market funds	$ 26,522	$ 26,522	$	$
U.S. government agency obligations	3,219		3,219	
	$ 29,741	$ 26,522	$ 3,219	$

	Fair value at December 31, 2011	Fair value measurements using inputs considered as		
		Level 1	Level 2	Level 3
		(in thousands)		
Money market funds	$ 16,926	$ 16,926	$	$
U.S.government agency obligations	3,297		3,297	
	$ 20,223	$ 16,926	$ 3,297	$

As of June 30, 2012 and December 31, 2011, the Company did not have any assets or liabilities that were valued using Level 3 inputs.

Money Market Funds

Money market funds are open-ended mutual funds that typically invest in short-term debt securities. Money market funds are classified as cash and cash equivalents on the Company s consolidated balance sheets. The Company classified these funds that are specifically backed by debt securities as Level 1 instruments due to its usage of unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

U.S. Government and Governmental Agency Obligations

U.S. government and governmental agency obligations are issued by U.S. federal, state and local governments, government-sponsored enterprises and other governmental entities such as authorities or special districts that generally mature within two years. These are classified as cash and cash equivalents and short-term investments on the Company s condensed consolidated balance sheets. The market approach was used to value the Company s treasury U.S. government and governmental agency obligations. The Company classified these securities as Level 2 instruments due to either its usage of observable market prices in less active markets or, when observable market prices were not available, its use of non-binding market prices that are corroborated by observable market data or quoted market prices for similar instruments.

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NOTE 5 Goodwill and Other Intangible Assets

There were no changes in the carrying value of goodwill during the three and six months ended June 30, 2012.

Other intangible assets, net, consisted of the following:

	June 30, 2012		
	Gross carrying amount	Accumulated amortization (in thousands)	Net intangibles
Developed technology	$ 1,874	$ (914)	$ 960
Tradenames	260	(85)	175
Customer lists and contracts	7,300	(1,087)	6,213
	$ 9,434	$ (2,086)	$ 7,348

	December 31, 2011		
	Gross carrying amount	Accumulated amortization (in thousands)	Net intangibles
Developed technology	$ 4,252	$ (3,047)	$ 1,205
Tradenames	1,606	(1,391)	215
Customer lists and contracts	10,502	(3,756)	6,746
	$ 16,360	$ (8,194)	$ 8,166

Amortization expense associated with other intangible assets was $0.4 million and $0.8 million for the three and six months ended June 30, 2012, respectively, and $0.1 million and $0.2 million for the three and nine months ended June 30, 2011, respectively.

Minimum future amortization expense for other intangible assets at June 30, 2012 was as follows:

	Amortization (in thousands)
Remainder of fiscal 2012	$ 817
2013	1,441
2014	1,405
2015	1,033
2016	928
Thereafter	1,724
	$ 7,348

NOTE 6 Commitments and Contingencies

Leases

As of June 30, 2012, the Company leased four facilities under operating lease arrangements. The lease expiration dates range from May 2014 to April 2015. Certain leases contain escalation clauses calling for increased rents. The Company recognizes rent expense on a straight-line basis over the lease period and has recorded deferred rent for the difference between rent payments and rent expense recognized. An additional facility is leased on a month-to-month basis. Rent expense was $0.3 million and $0.6 million for the three and six months ended June 30, 2012, respectively, and $0.2 million and $0.4 million for the three and six months ended June 30, 2011, respectively.

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Legal Proceedings

On August 28, 2009, DocMagic, Inc., (DocMagic), filed a lawsuit against the Company in the U.S. District Court for the Northern District of California (*DocMagic, Inc. v. Ellie Mae, Inc*., Case No. 3:09-CV-4017), which is referred to in this report as the Federal Action, alleging that the Company had engaged in monopolization and/or attempted monopolization of an alleged product market composed of internet portal[s] providing electronic linkages for mortgage loan closing document preparation services, and that it is subject to liability for related state court claims for intentional interference with contractual relationship, interference with prospective economic advantage and unfair competition. DocMagic s claims relate to the August 2009 expiration of a September 2006 Electronic Bridge Agreement pursuant to which DocMagic had been a vendor on the Ellie Mae Network. In addition, DocMagic filed a separate lawsuit against Ellie Mae in the Superior Court of California for the City and County of San Francisco (*DocMagic, Inc. v. Ellie Mae, Inc.*, Case No. CGC-09-491986), which is referred to in this report as the State Action, wherein it alleged a related claim of breach of a September 2006 reseller agreement between the parties and also alleged unfair competition. The State Action was later dismissed without prejudice pursuant to an agreement between the parties so that the parties could re-file their state law claims in the Federal Action. DocMagic amended its complaint to include the state claims and also Lanham Act and Copyright Act claims.

In response to DocMagic s federal claim, the Company filed an answer and counterclaim, denying all material allegations. In the counterclaim, the Company raised various affirmative claims against DocMagic for copyright infringement, violation of the federal Computer Fraud and Abuse Act and violation of state law claims for breach of the Electronic Bridge Agreement inducing its customers to breach contracts and engaging in unfair competition. Subsequent to the State Action being dismissed, the Company filed an amended counterclaim in the Federal Action, adding an additional state claim for violation of California s Comprehensive Computer Data Access and Fraud Act.

The initial complaint was dismissed with leave to amend as to certain claims and DocMagic s claims for attempted monopolization and false advertising were dismissed with prejudice. DocMagic then filed a second amended complaint, re-alleging claims that were dismissed with leave to amend. The Company answered the second amended complaint, denying all material allegations, and filed its second amended counterclaim. DocMagic answered the second amended counterclaim, denying all material allegations. Pursuant to the second amended complaint and the second amended counterclaim, each of the parties is seeking unspecified damages and injunctive relief. Discovery is proceeding. On May 16, 2011, the Court ordered the parties to mediation, which the parties attended on August 24, 2011. The case is ongoing.

On March 25, 2011, Industry Access Incorporated filed a patent infringement lawsuit against the Company and another defendant in the U.S. District Court for the Central District of California. The complaint alleges, among other things, that certain aspects of the Company s Encompass360 loan management software system and related operations infringe a single patent, and seeks declaratory relief and unspecified damages from the defendants, including enhanced damages for willful infringement and reasonable attorneys fees. On June, 24, 2011, the Court issued an order requiring plaintiff to serve the complaint on all defendants within three days of the order. On June 28, 2011, plaintiff served the Company with the complaint and the Company filed its answer on August 5, 2011 denying all material allegations of the complaint. On November 18, 2011 the other defendant filed with the United States Patent and Trademark Office (the PTO) a request for ex parte reexamination of Industry Access US Patent No 7,769,681, which the PTO granted on February 14, 2012. On December 15, 2011, the Company filed a motion to stay the litigation pending the reexamination, which the court granted on February 28, 2012. The Company intends to defend this claim vigorously.

Although as of June 30, 2012, the Company had not been served with the initial complaints, the Company has been named as a co-defendant in three purported class action lawsuits filed in the Missouri Circuit Court in St. Louis County, Missouri. These lawsuits against the Company and various other defendants were filed by (i) David and Lisa Clepper on May 4, 2012 (the Clepper Matter), (ii) Russell and Kathleen Klingel and Lee McMurray on May 4, 2012 (the Klingel Matter), (iii) Richard and Susan Ryffel on May 25, 2012 (the Ryffel Matter) and (iv) Nicole and Kenneth Boegeman on June 27, 2012 (the Boegeman Matter), all the plaintiffs of which are being represented by the same law firm. The respective plaintiffs in these lawsuits allege that the Company, among other things, violated Missouri s Merchandising Practices Act and engaged in the unauthorized practice of law in connection with document preparation services that the Company began offering following the acquisition of certain assets from Online Documents, Inc. in September 2008. The respective plaintiffs seek unspecified damages, injunctive relief, attorney s fees, other costs and expenses and pre-judgment interest. The plaintiffs in the Clepper Matter and Boegeman Matter voluntarily dismissed the Company without prejudice from the lawsuit on July 12, 2012. The plaintiffs in the Ryffel Matter voluntarily dismissed all the defendants, including the Company, without prejudice from the lawsuit on June 14, 2012. In addition, the Company may be subject to similar claims and legal proceedings in the future.

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The Company believes that it has substantial and meritorious defenses in each of these cases and, if these matters are re-filed or similar claims are pursued, the Company intends to defend these claims vigorously. However, neither the outcome of this litigation nor the amount or range of potential damages can be assessed with certainty.

The Company is also subject to various other legal proceedings and claims arising in the ordinary course of business. With respect to these matters and the litigations described above, the Company cannot predict the ultimate outcome of these legal proceedings and the amounts and ranges of potential damages associated with such proceedings cannot be estimated. An unfavorable outcome of these any of litigations could materially adversely affect the Company s business, financial condition and results of operations.

NOTE 7 Stock Incentive Plans

2011 Equity Incentive Award Plan

Stock Options

The following table summarizes the Company s stock option activities for the six months ended June 30, 2012:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2011	4,246,285	$ 3.97		
Granted	637,500	$ 11.45		
Exercised	(550,562)	$ 2.31		
Forfeited or expired	(122,710)	$ 6.42		
Outstanding at June 30, 2012	4,210,513	$ 5.25	7.01	$ 53,679
Ending vested and expected to vest at June 30, 2012	4,043,606	$ 5.25	6.98	$ 51,563
Exercisable at June 30, 2012	1,857,693	$ 3.36	5.09	$ 27,189

Intrinsic value of an option is the difference between the fair value of the Company s common stock at the time of exercise and the exercise price to be paid. The aggregate intrinsic value for options outstanding at June 30, 2012 in the table above represents the total intrinsic value, based on the Company s closing stock price of $18.00 as of June 30, 2012, which would have been received by option holders had all option holders exercised their in-the-money options as of that date.

Following is additional information pertaining to the Company s stock option activities for the three and six months ended June 30, 2012 and 2011:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
	(in thousands, except per option amounts)			
Weighted average fair value per option granted	$ 7.97	$ 3.50	$ 5.82	$ 3.50
Intrinsic value of options exercised	$ 450	$ 308	$ 2,558	$ 492
Proceeds received from options exercised	$ 115	$ 84	$ 1,274	$ 193

As of June 30, 2012, total unrecognized compensation cost related to unvested stock options, adjusted for estimated forfeitures, was $7.0 million and is expected to be recognized over a weighted average period of 3.3 years.

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Restricted Stock Units

The fair value of the Company s Restricted Stock Unit (RSU) awards is measured based upon the closing price of its underlying common stock on the New York Stock Exchange as of the grant date. Upon vesting, RSUs convert into an equivalent number of shares of common stock. The following table summarizes the Company s RSU activity for the six months ended June 30, 2012:

	Number of RSUs	Weighted Average Grant Date Fair Value Per RSU
Outstanding at December 31, 2011		$
Granted	50,000	8.90
Released	(3,125)	8.90
Forfeited or expired		
Outstanding at June 30, 2012	46,875	$ 8.90
Expected to vest at June 30, 2012	43,538	

RSUs that are expected to vest are net of estimated future forfeitures.

As of June 30, 2012, total unrecognized compensation cost related to unvested RSUs, adjusted for estimated forfeitures, was $0.4 million and is expected to be recognized over a weighted average period of 3.7 years.

Employee Stock Purchase Plan

Employee participation in the Employee Stock Purchase Plan (ESPP) began in the second quarter of 2011. For the six months ended June 30, 2012, employees purchased 60,254 shares under the ESPP plan for a total of $282,000. As of June 30, 2012, unrecognized compensation cost related to the current ESPP period which ends on August 31, 2012 is approximately $51,000 and is expected to be recognized over two months.

Total stock-based compensation expense recognized by the Company for the three and six months ended June 30, 2012 and 2011 consisted of:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
	(in thousands)			
Stock-based compensation by type of award:				
Stock options	$ 773	$ 325	$ 1,258	$ 688
ESPP	77	69	99	69
RSUs(1)	28		38	
	$ 878	$ 394	$ 1,395	$ 757
Stock-based compensation by category of expense:				
Cost of revenues	$ 59	$ 20	$ 90	$ 37
Sales and marketing	100	42	170	109
Research and development	252	54	384	148
General and administrative	467	278	751	463
	$ 878	$ 394	$ 1,395	$ 757

(1) There were no outstanding RSUs during 2011.

The Company did not capitalize any stock-based compensation for the three and six months ended June 30, 2012 and 2011 as such amounts were not material.

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The fair value of stock options and stock purchase rights granted under the 2011 Plan and the ESPP were estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions during the three and six months ended June 30, 2012:

	Three months ended June 30,		Six months ended June 30,	
	2012	**2011**	**2012**	**2011**
Stock option plans:				
Risk-free interest rate	0.90%	2.00%	1.03%	2.00%
Expected life of options (in years)	5.72	5.67	5.95	5.67
Expected dividend yield	0%	0%	0%	0%
Volatility	57%	54%	56%	54%
Employee Stock Purchase Plan:				
Risk-free interest rate	n/a	*	0.15%	*
Expected life of options (in years)	n/a	*	0.50	*
Expected dividend yield	n/a	*	0%	*
Volatility	n/a	*	47%	*

* Employee participation in the ESPP did not begin until the second quarter of 2011.

Common Stock

The following number of shares of common stock were reserved and available for future issuance at June 30, 2012:

	Reserved Shares
Stock Plans	2,596,664
Employee Stock Purchase Plan	767,065
Total	3,363,729

NOTE 8 Income Taxes

The Company computes its provision for income taxes by applying the estimated annual effective tax rate to income from recurring operations and adjusts the provision for discrete tax items recorded in the period. The estimated annual effective tax rate for the six months ended June 30, 2012 and 2011 was 4.6% and 9.5%, respectively. The difference between the statutory rate of 35% and the Company s estimated annual effective tax rate was primarily due the utilization of federal and state net operating losses and research and development credits not previously benefited.

The Company has established and continues to maintain a full valuation allowance against its deferred tax assets as the Company does not believe that the realization of those assets is more likely than not.

The Company records liabilities related to its uncertain tax positions. Tax positions for the Company and its subsidiaries are subject to income tax audits by multiple tax jurisdictions. The Company believes that it has provided adequate reserves for its income tax uncertainties in all open tax years. The Company has a policy to classify accrued interest and penalties associated with uncertain tax positions together with the related liability, and the expenses incurred related to such accruals are included in the provision for income taxes.

NOTE 9 Related Party Transactions

A related party is generally defined as (i) any person that holds 10% or more of the Company s securities and their immediate families, (ii) the Company s management, (iii) someone that directly or indirectly controls, is controlled by or is under common control with the Company or (iv) anyone who can significantly influence the financial and operating decisions of the Company. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

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Prior to the IPO, certain investors in the Company were also trade customers. Revenues earned from these related parties were $366,000 and $858,000 for the three and six months ended June 30, 2011 and were primarily included in on-demand revenues, respectively. Accounts receivable with respect to these related parties under these arrangements were $341,000 as of December 31, 2011. Amounts due to these related parties were $355,000 as of December 31, 2011. As a result of the IPO and investor divestitures, by December 31, 2011, none of these investors met the definition of a related party.

Director Carl Buccellato served as the chief executive officer of SavingStreet, LLC (formerly New Casa 188, LLC) (Saving Street), from May 2008 until February 2012, and owns 32% of the membership interests of SavingStreet. During 2008, the Company entered into a strategic relationship agreement with SavingStreet (which was subsequently amended and restated on June 15, 2010) pursuant to which the Company provided to SavingStreet certain information from borrowers who consented to the distribution of such information, SavingStreet used this borrower information to market certain move-related and home ownership-related products and services and the Company was entitled to receive 20% of SavingStreet s net income until investors had recouped their initial investment, and then 50% of its net income thereafter. In connection with this transaction, the Company issued to SavingStreet a five-year warrant to purchase up to 133,333 shares of its common stock at an exercise price of $5.94 per share. This warrant may only be exercised at any time after the Company has received an aggregate of $5.0 million pursuant to the agreement and prior to the termination date of the warrant, which is December 31, 2012. In March 2012, the Company terminated its existing agreements and arrangements with SavingStreet. The five-year warrant remains outstanding and unvested as of June 30, 2012 and December 31, 2011 as the performance requirements under the arrangement were not met. There was $0 and $47,000 expenses incurred for services from SavingStreet for the three months ended June 30, 2012 and 2011, respectively and $3,000 and $100,000 for the six months ended June 30, 2012 and 2011, respectively. Amount due to SavingStreet was $11,000 as of December 31, 2011. The Company has no outstanding liabilities due to SavingStreet as of June 30, 2012.

NOTE 10 Segment Information

The Company has concluded that it operates in one industry mortgage-related software and services. The Company s chief operating decision maker is its chief executive officer, who reviews financial information presented on a consolidated basis. Accordingly, the Company has determined that it has a single reporting segment and operating unit structure, specifically technology-enabled solutions to help streamline and automate the mortgage origination process for its network participants.

The Company is organized primarily on the basis of service lines. The Company re-categorized its revenues beginning with the first quarter of 2012 to on-demand revenues and on-premise revenues to better align with the Company s strategic plan. Supplemental disclosure of revenues by type is as follows:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
	(in thousands)			
On-demand revenues	$ 20,400	$ 9,624	$ 38,155	$ 18,725
On-premise revenues	3,169	1,840	6,320	3,342
	$ 23,569	$ 11,464	$ 44,475	$ 22,067

NOTE 11 Subsequent Events

On July 3, 2012, the Company sold 3,465,245 shares of its common stock and certain directors and executive officers of the Company (the Selling Stockholders) sold an aggregate of 101,638 shares in an underwritten public offering pursuant to the Company s effective Registration Statement on Form S-3 (Registration No. 333-181980) at a public offering price of $17.00 per share. The Company received the net proceeds from the sale of the shares offered by the Company of approximately $55.7 million, after deducting underwriting discounts and commissions and estimated offering expenses. The Company did not receive any proceeds from the sale of shares offered by the Selling Stockholders.

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

This Quarterly Report on Form 10-Q, including this Management s Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements relate to future events or our future financial performance. Forward-looking statements may include words such as may, will, should, expect, plan, intend, anticipate, believe, estimate, predict, potential, continue or other wording indicating future results or expectations. Forward-looking statements are subject to risks and uncertainties, and actual events or results may differ materially. Factors that could cause our actual results to differ materially include, but are not limited to, those discussed under Risk Factors in this report. We also face risks and uncertainties relating to our business including: our ability to accurately forecast revenues and appropriately plan our expenses; the impact of changes in mortgage interest rates; the volume of mortgages originated by our Encompass users; fluctuations in mortgage lending volume; the number of Encompass users; transaction volume on the Ellie Mae Network; the risk that the anticipated benefits, growth prospects and synergies expected from the Del Mar Datatrac,Inc., or DMD, acquisition may not be fully realized or may take longer to realize than expected; the impact of uncertain domestic and worldwide economic conditions, including the resulting effect on residential mortgage volumes; the effectiveness of our marketing and sales efforts to attract new and retain existing SaaS Encompass users and Ellie Mae Network participants; our ability to enhance the features and functionality of our Encompass software and the Ellie Mae Network; the level of demand for our Encompass Closer document preparation and other services we offer; the timing of the introduction and acceptance of new Ellie Mae Network offerings and new on-demand services; changes in mortgage originator, lender, investor or service provider behavior and any related impact on the residential mortgage industry; interruptions in Ellie Mae Network service, our hosted Encompass software and any related impact on our reputation; our ability to successfully manage our growth and any future acquisitions of businesses, solutions or technologies; the timing of future acquisitions of businesses, solutions or technologies and new product launches; changes in government regulation affecting Ellie Mae Network participants or our business, and potential structural changes in the U.S. residential mortgage industry; our ability to protect the confidential information of our Encompass users, Ellie Mae Network participants and their respective customers; the attraction and retention of qualified employees and key personnel; our ability to protect our intellectual property, including our proprietary Encompass software; our ability to compete effectively in a highly competitive market and adapt to technological changes; our ability to protect our intellectual property, including our proprietary Encompass software; and costs associated with defending intellectual property infringement and other claims. We undertake no obligation to revise or update any forward-looking statements to reflect any event or circumstance that arises after the date of this report, or to conform such statements to actual results or changes in our expectations.

This discussion should be read in conjunction with the condensed consolidated financial statements and notes presented in this Quarterly Report on Form 10-Q and the consolidated financial statements and notes in our last filed Annual Report on Form 10-K for the year ended December 31, 2011, or 2011 Form 10-K.

The Company

We provide business automation software for a large segment of the mortgage industry in the United States. Our on-demand software solutions help streamline and automate the process of originating and funding new mortgage loans, increasing efficiency, facilitating regulatory compliance and reducing documentation errors. Mortgage originators use our Encompass software, a comprehensive operating system that handles key business and management functions, in running a mortgage origination business. Mortgage originators use Encompass as a single tool for loan processing, marketing and customer communication, as well as to interact electronically with mortgage lenders, investors and service providers over the Ellie Mae Network. We also offer Encompass users a variety of other on-demand services, including Encompass Closer, which automatically prepares the disclosure and closing documents necessary to fund a mortgage; CenterWise, a bundled offering of electronic document management and websites used for customer relationship management; Encompass Compliance Service, which automatically checks for regulatory compliance throughout the origination process; tax transcript services which provide income verification capability to our customers; and Encompass Product and Pricing Service, which allows Encompass users to compare loans offered by different lenders and investors to determine the best product and price available to a particular borrower.

Our revenues are comprised of on-demand and on-premise revenues. On-demand revenues are revenues generated from software subscriptions we host that customers access through the Internet and revenues from a small number of customers that have opted to self-host a portion of the software but pay fees based on a per closed loan, or success, basis subject to monthly base fees, which we refer to as success-based pricing. On-demand revenues also include software services that are sold transactionally and Ellie Mae Network transaction fees. On-premise revenues generally are revenues generated from customer-hosted software licenses and related implementation (except for customer-hosted success-based pricing revenues included in on-demand revenues described above), training and maintenance services.

A component of our on-demand and on-premise revenues is software revenues which are derived from mortgage originators who either subscribe to SaaS Encompass, our on-demand solution, or license Encompass software for an initial perpetual license fee with annual maintenance, our on-premise solution. Mortgage originators subscribing to SaaS Encompass either pay monthly per-user subscription fees or success-based pricing. In addition, we offer CenterWise software either as a standalone product on

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a subscription-fee basis or bundled as part of our SaaS Encompass offering. Software services revenues are derived from fees paid by mortgage originators for the Encompass services they order. These services include Encompass Closer, Encompass Compliance Service and Encompass Product and Pricing Services. Lenders, service providers and certain government-sponsored entities using Encompass over the Ellie Mae Network pay us fees when they effect a transaction by sending an electronic service request over the Ellie Mae Network to any lender, service provider or other participant through our network and that request has been accepted.

Our on-demand revenues generally track the seasonality of the mortgage industry, with increased activity in the second and third quarters and reduced activity in the first and fourth quarters as home buyers tend to purchase their homes during the spring and summer in order to move to a new home before the start of the school year. These revenues are also affected by factors that impact mortgage volumes, such as interest rate fluctuations and general economic conditions.

The mortgage industry has undergone significant changes since 2007, largely in response to the hundreds of billions of dollars of loan defaults and massive losses suffered by lenders and investors. Our business strategy has evolved to address recent industry trends, including:

- lower lending volume;
- greater focus on operational efficiencies;
- significant market shift from mortgage brokerages to mortgage lenders;
- increased quality standards imposed by lenders and investors; and
- increased regulation

We are responding to these trends as follows:

Lower lending volume. Beginning in late 2009, we focused our marketing and sales efforts on our on-demand SaaS Encompass offering, and particularly our SaaS Encompass success-based pricing model, in contrast to our on-premise license model. In our on-demand SaaS Encompass offering, the customer does not pay the significant up-front licensing fee associated with our license model, which we believe is particularly attractive in the present climate of the residential mortgage origination market. Our SaaS Encompass success-based pricing model builds on this value proposition by aligning the customers payments for our software solutions with their own receipts of revenues. SaaS Encompass success-based pricing customers are composed of new Encompass customers and users that have converted from our licensed Encompass software or flat monthly per-user hosted offerings. At June 30, 2012 and December 31, 2011, we had 32,114 and 24,252 Active SaaS Encompass Users, respectively, which are mortgage origination professionals who have used our SaaS Encompass software at least once within the preceding 90 days. SaaS Encompass revenues represented 45%, 43% and 36% of our revenues for the three and six month periods ended June 30, 2012 and year ended December 31, 2011, respectively. We typically generate greater revenues per user through our on-demand SaaS Encompass offering than through our on-premise license offering.

Greater focus on operational efficiencies. Mortgage originators have experienced decreased profitability as a result of reduced mortgage originations. By automating many of the functions of mortgage origination, we enable our users to process quality loans more effectively. This reduces the cost of originating a loan and lowers the risk of buy back from investors of poorly originated or documented loans.

Significant market shift from mortgage brokerages to mortgage lenders. The industry has experienced a significant decline in the number of mortgage brokerages and an increase in the relative importance of mortgage lenders. We focus significant research and development effort on providing Encompass functionality for mortgage lenders. In addition, we have hired sales personnel focused on sales of our solutions to mortgage lenders rather than mortgage brokerages. We believe this shift toward lender users will provide us increased opportunities because mortgage lenders typically use more sophisticated and comprehensive software solutions to run their businesses and use more services and effect more transactions on the Ellie Mae Network.

Increased investor and lender quality standards imposed by lenders and investors. Encompass software is designed to automate and streamline the process of originating mortgages to satisfy increased quality requirements of investors. Relevant features of Encompass software include enabling customers management to impose processing rules and formats, milestone and process reminders, automated population of forms with accurate data, accurate and automated transmission of loan files and data from originators to investors and lenders.

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Increased regulation. Regulatory reforms that have significantly increased the complexity and importance of regulatory compliance. We offer Encompass Compliance Service, which automatically checks loan files for compliance with the myriad of federal, state and local regulations and alerts users to possible violations of these regulations. In addition, we have a staff of attorneys and work with compliance experts who help assure that documents prepared using our software and processes recommended by Encompass work flow comply with applicable rules and regulations.

On August 15, 2011, we completed the acquisition of DMD, a mortgage lending automation business. The acquisition was to expand the client base and gain market share.

Operating Metrics

Revenue per Average Active Encompass User and SaaS Encompass Revenue per Average Active SaaS Encompass User are key operational metrics we use to evaluate our business, determine allocation of our resources and make decisions regarding corporate strategy. The Revenue per Average Active Encompass User metric is calculated by dividing total revenues by Average Active Encompass Users during the period. The SaaS Encompass Revenue per Average Active SaaS Encompass User metric is calculated by dividing total SaaS Encompass Revenues by Average Active SaaS Encompass Users during the period. We focus on these metrics to determine our success in leveraging our user base to increase our revenues. We track Active Encompass Users and Active SaaS Encompass Users as well as related revenues generated by each group at the end of a period to gauge the degree of our market penetration.

The components used to calculate these metrics are defined below.

Active Encompass Users. An Active Encompass User is a mortgage origination professional who has used Encompass software at least once within a 90-day period preceding the measurement date. An Encompass user is a mortgage origination professional working at a mortgage lender, such as a mortgage bank, commercial bank, thrift or credit union, which sources and funds loans and generally sells these funded loans to investors; or a mortgage brokerage, who typically processes and submits loan files to a mortgage lender or mega lender that funds the loan.

Average Active Encompass Users. Average Active Encompass Users during a period is calculated by averaging the monthly Active Encompass Users during a period.

Active SaaS Encompass Users. An Active SaaS Encompass User is a mortgage origination professional who has used the SaaS Encompass system at least once within a 90-day period preceding the measurement date.

Average Active SaaS Encompass Users. Average Active SaaS Encompass Users during a period is calculated by averaging the monthly active SaaS Encompass users during a period.

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The following table shows these operating metrics as of and for the three and six months ended June 30, 2012 and 2011:

	Three months ended June 30, 2012	Three months ended June 30, 2011	Six months ended June 30, 2012	Six months ended June 30, 2011
Revenues (in thousands):				
Total revenues	$ 23,569	$ 11,464	$ 44,475	$ 22,067
Total SaaS Encompass revenues	$ 10,713	$ 3,686	$ 19,091	$ 7,222
Users at end of period:				
Active Encompass users	62,487	50,637	62,487	50,637
Active SaaS Encompass users	32,114	18,587	32,114	18,587
Active SaaS Encompass users as a percentage of active Encompass users	51%	37%	51%	37%
Average users during period:				
Active Encompass users	61,394	50,610	59,167	50,822
Active SaaS Encompass users	31,171	17,394	29,349	16,703
Active SaaS Encompass users as a percentage of active Encompass users	51%	34%	50%	33%
Revenue per average user during period:				
Revenue per average active Encompass user	$ 384	$ 227	$ 752	$ 434
SaaS Encompass revenue per average active SaaS Encompass user	$ 344	$ 212	$ 650	$ 432

Source of Revenues

We generate revenue primarily from transaction-based fees and fees for software and related services. We re-categorized our revenues beginning with the first quarter of 2012 to better align with our strategic plan. Accordingly, our revenues are now described as on-demand and on-premise revenues. Sales taxes assessed by governmental authorities are excluded from revenue.

On-demand Revenues

Our revenues are comprised of on-demand and on-premise revenues. On-demand revenues are revenues generated from software subscriptions we host that customers access through the Internet and revenues from customers that have opted to self-host a portion of the software but pay fees based on a per closed loan, or success, basis subject to monthly base fees, which we refer to as success-based pricing. On-demand revenues also include software services that are sold transactionally and Ellie Mae Network transaction fees.

In general, we recognize revenue for monthly subscription fees, including monthly base fees, on a straigh