ENVIRONMENTAL TECTONICS CORP
Form 10-Q
July 12, 2010

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended May 28, 2010
Commission File Number 1-10655
ENVIRONMENTAL TECTONICS CORPORATION

Pennsylvania	23-1714256
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

County Line Industrial Park
Southampton, Pennsylvania 18966
(Address of principal executive offices, Zip Code)
Registrant s telephone number, including area code (215) 355-9100

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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted, pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files).

Yes þ No o

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

Large Accelerated Filer o	Accelerated Filer o	Non-accelerated Filer o (Do not check if a smaller reporting company)	Smaller reporting company þ

Indicate by check mark whether the registrant is a shell company (as defined on Rule 12b-2 of the Exchange Act).

Yes o No þ

As of July 9, 2010, there were 9,086,999 shares of the registrant s common stock issued and outstanding.

Index

When used in this Quarterly Report on Form 10-Q, except where the context otherwise requires, the terms we , us , our , ETC and the Company refer to Environmental Tectonics Corporation and its subsidiaries.

Table of Contents

PART I FINANCIAL INFORMATION
Item 1. Financial Statements (unaudited)

Environmental Tectonics Corporation
Condensed Consolidated Income Statements
(unaudited)
(in thousands, except share and per share information)

	Thirteen week periods ended May 28, 2010	May 29, 2009
Net sales	$ 12,121	$ 9,581
Cost of goods sold	6,991	5,154
Gross profit	5,130	4,427
Operating expenses:		
Selling and marketing	1,102	1,254
General and administrative	1,463	1,602
Research and development	324	228
	2,889	3,084
Operating income	2,241	1,343
Other expenses:		
Interest expense	228	516
Other, net	72	55
	300	571
Income before income taxes	1,941	772
Provision for income taxes		
Income before noncontrolling interest	1,941	772
Income attributable to noncontrolling interest	5	2
Net income	1,936	770
Preferred stock dividend	(577)	(235)
Income applicable to common shareholders	$ 1,359	$ 535

Per share information:		
Earnings per common share:		
Basic	$ 0.15	$ 0.06
Diluted	$ 0.09	$ 0.06
Weighted average common shares:		
Basic	9,085,000	9,054,000
Diluted	20,967,000	9,054,000

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Environmental Tectonics Corporation

Condensed Consolidated Balance Sheets
(in thousands, except share information)

	May 28, 2010 (unaudited)	February 26, 2010
ASSETS		
Cash and cash equivalents	$ 874	$ 2,408
Restricted cash	5,476	2,751
Accounts receivable, net	4,087	17,356
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	3,666	3,576
Inventories, net	4,788	5,114
Deferred tax assets, current	5,391	4,983
Prepaid expenses and other current assets	1,602	545
Total current assets	25,884	36,733
Property, plant and equipment, at cost, net	13,606	13,643
Construction in progress	440	316
Software development costs, net	837	691
Other assets	291	346
Total assets	$ 41,058	$ 51,729
LIABILITIES		
Current portion of long-term debt	$ 213	$ 285
Accounts payable trade	1,710	1,783
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	8,105	13,944
Customer deposits	1,683	1,799
Accrued interest and dividends	833	782
Other accrued liabilities	2,400	2,814
Total current liabilities	14,944	21,407
Long-term obligations, less current portion:		
Credit facility payable to bank	4,508	9,808
Other long-term debt		12
	4,508	9,820
Deferred tax liabilities	3,298	3,066

Unearned interest	19	22
Total liabilities	22,769	34,315
Commitments and contingencies		
STOCKHOLDERS EQUITY		
Cumulative convertible participating preferred stock, Series D, $.05 par value, 11,000 shares authorized; 155 shares outstanding	155	155
Cumulative convertible participating preferred stock, Series E, $.05 par value, 25,000 shares authorized; 22,741 and 23,741 shares outstanding at May 28, 2010 and February 26, 2010, respectively	22,741	23,741
Common stock, $.05 par value, 20,000,000 shares authorized; 9,086,999 and 9,083,573 shares issued and outstanding at May 28, 2010 and February 26, 2010, respectively	454	454
Additional paid-in capital	13,508	14,050
Accumulated other comprehensive income (loss)	45	(431)
Accumulated deficit	(18,657)	(20,593)
Total stockholders equity before noncontrolling interest	18,246	17,376
Noncontrolling interest	43	38
Total stockholders equity	18,289	17,414
Total liabilities and stockholders equity	$ 41,058	$ 51,729

The accompanying notes are an integral part of the condensed consolidated financial statements.

4

Table of Contents

Environmental Tectonics Corporation

Condensed Consolidated Statements of Cash Flows
(unaudited)
(in thousands)

	Thirteen week periods ended	
	May 28, 2010	**May 29, 2009**
Cash flows from operating activities:		
Net income	$ 1,936	$ 770
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	346	567
Decrease in valuation allowance for deferred tax assets	(867)	
Accretion of debt discount	55	95
Increase in allowances for accounts receivable and inventories, net	110	316
Income attributable to noncontrolling interest	5	2
Stock compensation expense	24	
Changes in operating assets and liabilities:		
Accounts receivable	13,259	(791)
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	(90)	(319)
Inventories	226	(432)
Prepaid expenses and other assets	(1,057)	214
Deferred tax assets, net	691	
Accounts payable	(73)	320
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	(5,839)	(1,337)
Customer deposits	(116)	(966)
Accrued interest and dividends	51	329
Other accrued liabilities	(417)	76
Net cash provided by (used in) operating activities	8,244	(1,156)
Cash flows from investing activities:		
Acquisition of equipment	(359)	(289)
Capitalized software development costs	(220)	(104)
Net cash used in investing activities	(579)	(393)
Cash flows from financing activities:		
(Repayment) borrowings under line of credit	(5,300)	1,400
(Repurchase) issuance of preferred stock	(1,000)	55
Issuance of common stock	10	1
Payment of preferred stock dividends	(576)	
Payments of other debt obligations	(84)	(2)
Increase in restricted cash for performance guarantee	(2,725)	(7)

Net cash (used in) provided by financing activities	(9,675)	1,447
Effect of exchange rate changes on cash	476	(131)
Net decrease in cash	(1,534)	(233)
Cash at beginning of period	2,408	520
Cash at end of period	$ 874	$ 287
Supplemental schedule of cash flow information:		
Interest paid	$ 96	$ 103
Income taxes paid	182	
Supplemental information on non-cash operating and investing activities:		
Accrued dividends on preferred stock	$ 577	$ 235

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents

Environmental Tectonics Corporation

Notes to the Condensed Consolidated Financial Statements

1. Nature of Business:

Environmental Tectonics Corporation (ETC or the Company) is principally engaged in the design, manufacture and sale of software driven products and services used to simulate and measure certain environmental conditions and to monitor the physiological effects of motion on humans in certain environmental conditions. These products and services include aircrew training systems (aeromedical, tactical combat and general), disaster management systems, entertainment products, sterilizers (steam and gas), environmental testing products, and hyperbaric chambers and other products that involve similar manufacturing techniques and engineering technologies. ETC focuses on software enhancements, product extensions, new product development and new marketplace applications. Presently, sales of the Company s products are made principally to U.S. and foreign government agencies. We operate in two primary business segments, the Training Services Group (TSG) and the Control Systems Group (CSG).

Training Services Group. This segment includes three primary product groups: aircrew training devices and related services, disaster management training and systems, and entertainment products.

Control Systems Group. This segment includes three primary product lines: sterilizers, environmental control systems, and hyperbaric chambers, along with parts and service support.

The Company s fiscal year is the 52-or 53-week annual accounting period ending the last Friday in February. Certain amounts from prior consolidated financial statements have been reclassified to conform to the presentation in fiscal 2011.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim condensed consolidated financial statements include the accounts of ETC, ETC s wholly-owned subsidiaries (i.e., Entertainment Technology Corporation, ETC International Corporation and ETC-Delaware), ETC s 99%-owned subsidiary located in London, England (i.e., ETC Europe), and ETC s 95%-owned subsidiary located in Warsaw, Poland (i.e., ETC-PZL Aerospace Industries, Ltd. (ETC-PZL)). ETC Southampton refers to the Company s corporate headquarters and main production plant located in Southampton, Pennsylvania, USA. All significant inter-company accounts and transactions have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have been prepared by ETC, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC), and reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal recurring nature.

Certain information in footnote disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America has been condensed or omitted pursuant to such rules and regulations and the financial results for the periods presented may not be indicative of the full year s results, although the Company believes the disclosures are adequate to make the information presented not misleading. These financial statements should be read in conjunction with the financial statements and the notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended February 26, 2010.

References to fiscal first quarter 2011 are references to the 13-week period ended May 28, 2010. References to fiscal first quarter 2010 are references to the 13-week period ended May 29, 2009.

Significant Accounting Policies

There have been no material changes in the Company s significant accounting policies during fiscal 2011 as compared to what was previously disclosed in the Company s Annual Report on Form 10-K for the fiscal year ended February 26, 2010.

Table of Contents

Environmental Tectonics Corporation
Notes to the Condensed Consolidated Financial Statements, continued
3. Earnings Per Common Share:

Basic earnings per share is computed on the basis of the weighted average number of common shares outstanding. Diluted earnings per share is computed on the basis of the weighted average number of common shares outstanding plus the effect of outstanding stock options and common stock warrants using the treasury stock method plus the effect of all convertible financial instruments, including subordinated debt and preferred stock, as if they had been converted at the beginning of each period presented. If the effect of the conversion of any financial instruments would be anti-dilutive, it is excluded from the diluted earnings per share calculation.

On May 28, 2010, there was $22,896,000 of cumulative convertible participating preferred stock. This consisted of the following:

$55,000 of Series D Preferred Stock convertible at $0.94 per share, equating to 58,511 shares of common stock, issued in April 2009;

$100,000 of Series D Preferred Stock convertible at $1.11 per share, equating to 90,090 shares of common stock, issued in July 2009;

$22,741,000 of Series E Preferred Stock convertible at $2.00 per share, equating to 11,370,500 shares of common stock, issued in July 2009.

On February 20, 2009, in connection with the issuance of a $2,000,000 promissory note, the Company issued warrants to purchase 143,885 shares of the Company s common stock at $1.39 per share. Additionally, on July 2, 2009, in consideration of an increase of the personal guarantee by H.F. Lenfest of the Company s PNC line of credit, the Company issued warrants to purchase 450,450 shares of the Company s common stock at $1.11 per share. (See Note 6, Long-Term Obligations and Credit Arrangements.)

On May 28, 2010 and May 29, 2009, respectively, there were options to purchase the Company s common stock totaling 269,185 and 157,652 shares at an average price of $4.53 and $5.90 per share. Due to the conversion price of these common stock options, these shares were excluded from the calculation of diluted earnings per share since the effect of their conversion would be antidulutive.

	Thirteen week period ended May 28, 2010			**Thirteen week period ended May 29, 2009**		
	Income (amounts in thousands)	**Weighted average shares**	**Per share amount**	**Income (amounts in thousands)**	**Weighted average shares**	**Per share amount**
Net income	$ 1,936			$ 770		
Less preferred stock dividends	(577)			(235)		
Basic earnings per share:						
Basic earnings available to common shareholders	$ 1,359	9,085,000	$ 0.15	$ 535	9,054,000	$ 0.06
Effect of dilutive securities:						

Preferred stock		11,519,000	
Stock options and warrants		363,000	
Diluted earnings per share:			
Basic earnings available to common shareholders	$ 1,359		
Add: Preferred stock dividend	577		
Income available to common shareholders plus effect of dilutive securities	$ 1,936	20,967,000	$ 0.09

Table of Contents

Environmental Tectonics Corporation
Notes to the Condensed Consolidated Financial Statements, continued

4. Inventories

Inventories are valued at the lower of cost or market using the first in, first out (FIFO) method and consist of the following:

	May 28, 2010 (unaudited)	February 26, 2010
	(in thousands)	
Raw materials	$	$
Work in process	4,499	4,764
Finished goods	289	350
Total	$ 4,788	$ 5,114

Inventory is presented net of an allowance for obsolescence of $2,445,000 (Raw material $124,000, Work in process $1,620,000 and Finished goods $701,000) and $2,345,000 (Raw material $138,000, Work in process $1,506,000 and Finished goods $701,000) at May 28, 2010 and February 26, 2010, respectively.

5. Accounts Receivable:

The components of accounts receivable are as follows:

	May 28, 2010 (unaudited)	February 26, 2010
	(in thousands)	
U.S. government	$ 1,010	$ 438
U.S. commercial	779	1,403
International	2,724	15,930
	4,513	17,771
Less: allowance for doubtful accounts	(426)	(415)
	$ 4,087	$ 17,356

6. Long-Term Obligations and Credit Arrangements:

Lenfest Financing Transaction

On April 24, 2009, the Company entered into a transaction (the Lenfest Financing Transaction), which was approved by shareholders on July 2, 2009, with H.F. Lenfest (Lenfest), a major shareholder and member of our Board of Directors, that provided for the following: (i) a $7,500,000 credit facility provided by Lenfest to ETC, which expires on December 31, 2012; (ii) exchange of the $10 million Subordinated Note held by Lenfest, together with all accrued interest and warrants issuable under the Subordinated Note, and all Series B Preferred Stock and Series C Preferred Stock held by Lenfest, together with all accrued dividends thereon, for a new class of preferred stock, Series E Preferred Stock, of the Company; and (iii) the guarantee by Lenfest of all of ETC s obligations to PNC Bank, National Association (PNC Bank) in connection with an increase of the Company s existing $15,000,000 revolving line of credit with PNC Bank (the 2007 PNC Credit Facility) to $20,000,000, and in connection with this guarantee, the pledge by Lenfest to PNC Bank of $10,000,000 in marketable securities.

Lenfest Credit Facility

As part of the Lenfest Financing Transaction, the Company established a credit facility in the maximum amount of $7,500,000 with Lenfest (the Lenfest Credit Facility) to be used to finance certain government projects that ETC has been awarded or is seeking to be awarded. The terms of the Lenfest Credit Facility are set forth in a Secured Credit Facility and Warrant Purchase Agreement between the Company and Lenfest, dated as of April 24, 2009 (the Lenfest Credit Agreement). In connection with the Lenfest Credit Agreement, the Company has executed, and will in the future execute, promissory notes in favor of Lenfest, in the aggregate principal amount of up to $7,500,000 (the Lenfest Credit Facility Note) based on the amount borrowed by the Company pursuant to the Lenfest Credit Agreement. Each Lenfest Credit Facility Note issued under the Lenfest Credit Facility will accrue interest at the rate of 10% per annum, payable in cash or, at the option of Lenfest, in shares of Series D Preferred Stock of the Company, as described below. The Lenfest Credit Facility expires on December 31, 2012. As of May 28, 2010, the Company had not utilized any of the $7.5 million available funding under this facility.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued
Bank Credit and Facility
Increased PNC Bank Credit Facility and Issuance of New Guarantee

On April 24, 2009, PNC Bank agreed to increase the amount of financing available under the 2007 PNC Credit Facility from $15,000,000 to $20,000,000, subject to the condition that Lenfest continue to personally guarantee all of ETC s obligations to PNC Bank (the Lenfest Guaranty) and that Lenfest pledge $10,000,000 in marketable securities as collateral security for his guarantee (the Lenfest Pledge).

Following the receipt of shareholder approval for the Lenfest Financing Transaction, ETC and PNC Bank entered into the Amended and Restated Credit Agreement (the Amended and Restated PNC Credit Agreement) and the Second Amended and Restated Reimbursement Agreement for Letters of Credit (the Amended and Restated Reimbursement Agreement). The 2007 promissory note was cancelled and replaced with the Amended and Restated Promissory Note in the principal amount of $20,000,000 (the Amended and Restated PNC Note).

In connection with the execution of the amended and restated agreements and note with PNC, ETC paid to Lenfest an origination fee of 100 shares of Series D Convertible Preferred Stock of the Company (the Series D Preferred Stock), which is equal to one percent (1%) of the market value of the $10,000,000 in marketable securities pledged by Lenfest to PNC Bank to secure ETC s obligations to PNC Bank. The 100 shares of Series D Preferred Stock have a stated value of $1,000 per share, or $100,000 in the aggregate. These shares of Series D Preferred Stock have a conversion price per share equal to $1.11, which price equaled the average closing price of ETC common stock during the 120 days prior to the issuance of such shares. Additionally, ETC will pay Lenfest annual interest equal to 2% of the amount of the Lenfest Pledge, payable in Series D Preferred Stock.

In consideration of Lenfest entering into the amended and restated guaranty, ETC issued to Lenfest warrants equal in value to ten percent (10%) of the amount of the $5,000,000 increase under the 2007 PNC Bank Credit Facility. The warrants are exercisable for seven years following issuance to purchase 450,450 shares of ETC Common Stock at an exercise price per share equal to $1.11, which price equaled the average closing price of ETC common stock during the 120 days prior to the issuance of the warrant. The Company recorded a loan origination deferred charge associated with these warrants of $487,000 using the Black-Scholes options-pricing model with the following weighted average assumptions: expected volatility of 91.9%; risk-free interest rate of 0.49%; and an expected life of seven years.

Amounts borrowed under the Amended and Restated PNC Credit Agreement can be borrowed, repaid and reborrowed from time to time until June 30, 2011. Borrowings made pursuant to the Amended and Restated PNC Credit Agreement bear interest at either the prime rate (as described in the promissory note executed pursuant to the Amended and Restated PNC Credit Agreement) plus 0.50 percentage points or the London Interbank Offered Rate (LIBOR) (as described in the Promissory Note) plus 2.50 percentage points. Additionally, ETC is obligated to pay a fee of 0.125% per year for unused but available funds under the line of credit.

Amendment to the Credit Agreement

On October 1, 2009, the Amended and Restated PNC Credit Agreement was amended to extend the maturity date to June 30, 2011. Additionally, the affirmative covenants were adjusted. The Consolidated Tangible Net Worth covenant was modified to reflect the impact on the Company s balance sheet of the Lenfest Financing Transaction. Effective with each fiscal quarter ending after October 1, 2009, the Company must maintain a minimum Consolidated Tangible Net Worth of at least $10,000,000. The EBITDA covenant was changed for fiscal periods beginning after December 1, 2009. Beginning with the first fiscal quarter ending after December 1, 2009, and for each fiscal quarter ending thereafter, the Company must maintain a minimum cumulative aggregate EBITDA of $4,000,000 for the fiscal quarter then ending and the three preceding fiscal quarters. The Company is in full compliance of its covenants as of May 28, 2010.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

As of May 28, 2010, the Company s availability under the Amended and Restated PNC Credit Agreement was approximately $14,165,000. This reflected cash borrowings of $4,300,000 and outstanding letters of credit of approximately $1,535,000.

Due to the Company s accumulated deficit, all dividends accruing for the Series D and E Preferred Stock issuances have been recorded in the accompanying financial statements as a reduction in additional paid-in capital.

Dedicated Line of Credit Agreement with PNC Bank

On November 16, 2009, the Company and PNC Bank entered into a Letter Agreement, Reimbursement Agreement, Pledge Agreement, and Amendment to Subordination Agreement (collectively, the Dedicated Line of Credit Agreement), pursuant to which the Company received a committed line of credit in the amount of $5,422,405 (the Line of Credit) which the Company used to satisfy performance bond and repayment guarantee requirements in a newly awarded contract. Use of this dedicated line of credit is restricted to funding contract performance and repayment guarantee requirements under this specific contract.

As security for the Line of Credit, ETC and H.F. Lenfest were each required to provide PNC Bank with the equivalent of $2,711,000 in the form of cash or other financial instruments. To meet this requirement, ETC has deposited cash in this amount in a restricted bank account with PNC Bank. H.F. Lenfest had guaranteed the Company s obligations under the Dedicated Line of Credit Agreement, and had pledged to PNC Bank $2,711,000 in certificated securities. Under the terms of the line, ETC was required by August 19, 2010, to place additional cash funds of $2,711,000 with PNC Bank, at which time the Lenfest guarantee would be terminated and the Lenfest securities would be returned to Lenfest.

During the first quarter of fiscal 2011, the Company fulfilled its requirement to fund the balance of the security to collateralize the committed line of credit by depositing approximately $2,711,000 in a certificate of deposit with PNC. Subsequently, Mr. Lenfest s securities were returned and his guarantee to cover the $5.4 million line was terminated.

ETC-PZL Project Financing

In September 2009, ETC-PZL, located in Warsaw, Poland, entered into a project financing agreement with a Warsaw bank to fund a research and development contract with the Polish government. The amount of this facility is $604,000 and it is being repaid in quarterly installments of approximately $70,000 which commenced in September 2009. This facility will expire in September 2011. Use of this line of credit is restricted to funding contract requirements under a specific research and development contract with the Polish government.

Long-term obligations at May 28, 2010 and February 26, 2010 consist of the following:

	May 28, 2010	February 26, 2010
	(amounts in thousands)	
Note payable to bank	$ 4,300	$ 9,600
ETC-PZL project financing	416	486
Automobile loan	5	7
Total debt obligations	4,721	10,093
Less current maturities	213	285
Long-term obligations, net of current maturities	$ 4,508	$ 9,808

Table of Contents

Environmental Tectonics Corporation
Notes to the Condensed Consolidated Financial Statements, continued

7. Fair Value of Financial Instrument

The carrying amounts of cash, accounts receivable and accounts payable approximate fair value because of the short maturity associated with these instruments. Derivative financial instruments are recorded at fair value.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The hierarchy below lists three levels of fair value based on the extent to which inputs used in measuring fair value are observable in the market. The Company categorizes each of its fair value measurements in one of these three levels based on the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1: Observable inputs such as quoted prices in active markets for identical assets of liabilities;

Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly; these include quoted prices for similar assets or liabilities in active markets and quoted prices or identical assets or liabilities in markets that are not active;

Level 3: Unobservable inputs that are supported by little or no market activity, which require the reporting entity s judgment or estimation.

The assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of financial assets and financial liabilities and their placement within the fair value hierarchy. The Company s financial liabilities that are accounted for at fair value on a recurring basis using the discounted cash flow methodology are summarized below:

	Fair Value Measurement at May 28, 2010 using:			
Liabilities	**Level 1**	**Level 2**	**Level 3**	**Total**
		(amounts in thousands)		
Credit facility payable to bank	$	$	$ 5,588	$ 5,588
ETC-PZL contract financing			392	392
Total	**$**	**$**	**$ 5,980**	**$ 5,980**

8. Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes as well as the valuation of net loss carryforwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the realizability of the related deferred tax asset.

The Company has reviewed the components of its deferred tax asset and has determined, based upon all available information, that its current and expected future operating income will more likely than not result in the realization of a portion of its deferred tax assets relating primarily to its net operating loss carryforwards. As of May 28, 2010, the Company had approximately $35.2 million of federal net loss carry forwards available to offset future income tax liabilities, beginning to expire in 2025. In addition, the Company has the ability to offset deferred tax assets against deferred tax liabilities created for such items as depreciation and amortization.

Table of Contents

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

As a result of the Company s analysis, no provision for income taxes was recorded in the Consolidated Statement of Operations for the thirteen week period ended May 28, 2010. For the thirteen week period ended May 29, 2009, the Company did not record any benefit for income taxes due to the prior operating losses and the low probability that any recorded tax receivables would ever be realized.

	(in thousands)	
	Thirteen week period ended May 28, 2010	**Thirteen week period ended May 29, 2009**
Currently payable		
Federal	$ 120	$
State		
Foreign (benefits) taxes		
	120	
Deferred:		
Federal	(120)	
State		
Foreign benefit		
	(120)	
	$	$

A reconciliation of the statutory federal income tax rate to the effective tax rate is as follows:

	Thirteen week period ended May 28, 2010	**Thirteen week period ended May 29, 2009**
Statutory income tax (benefit)	34.0%	34.0%
State income tax, net of federal tax benefit	3.8	3.8
Change in valuation allowance	(37.8)	(37.8)
	%	%

The tax effects of the primary components of the temporary differences are as follows:

	May 28,	**February 26,**

	2010	2010
	(amounts in thousands)	
Deferred tax assets:		
Net operating loss and credits	$ 15,054	$ 15,607
Vacation reserve	80	80
Inventory reserve	918	880
Receivable reserve	160	156
Warranty reserve	117	117
Compensation and other reserves	158	32
Other, net		74
	16,487	16,946
Valuation Reserve	(11,096)	(11,963)
Total current deferred tax asset	5,391	4,983
Deferred tax liabilities:		
Amortization of capitalized software	401	350
Depreciation	2,897	2,716
Total non-current deferred tax liability	3,298	3,066
Net deferred tax asset	$ 2,093	$ 1,917

During the fiscal years ended February 26, 2010 and February 27, 2009, the Company did not have any unrecognized tax benefits and accordingly did not recognize interest expense or penalties related to unrecognized tax benefits. The Company or one of its subsidiaries files income tax returns in U.S. federal jurisdiction, various states and foreign jurisdiction. The Company is no longer subject to U.S. federal tax examinations by tax authorities for the fiscal years before 2007.

Table of Contents

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued
10. Commitments and Contingencies
Mends International, Ltd.

On May 29, 2008, a Request for Arbitration was filed against the Company with the Secretariat of the International Court of Arbitration by Mends International Ltd. (Mends). Mends Request for Arbitration arose out of a February 3, 1999 contract between the Company and Mends wherein Mends purchased aeromedical equipment for sale to the Nigerian Air Force. The Company contested the arbitration case but did record a reserve in this matter. On July 1, 2010, the International Court of Arbitration issued a Partial Final Award which was within the scope of the Company s reserve and which did not have a material adverse effect on the Company s financial condition or results of operations. Additionally, the International Court of Arbitration may make an additional award to allocate the costs of the arbitration (including attorneys fees) between the parties.

Administrative Agreement with U.S. Navy

In 2007, the Company entered into a settlement agreement with the Department of the Navy to resolve litigation filed by the Company in May 2003 in connection with a contract for submarine rescue decompression chambers. As of May 14, 2008, the Company made all payments required under this settlement agreement and transferred the chambers to the Department of the Navy. From October 2, 2007 through December 12, 2007, the Company was suspended by the Department of the Navy from soliciting work for the federal government pursuant to the Federal Acquisition Regulation. However, effective December 12, 2007, the Department of the Navy lifted the Company s suspension pursuant to the execution by the Company and the Department of the Navy of an Administrative Agreement. In accordance with the Administrative Agreement, the Company has established and implemented a program of compliance reviews, audits, and reports.

Table of Contents

Environmental Tectonics Corporation
Notes to the Condensed Consolidated Financial Statements, continued
11. Segment Information (unaudited):

The Company primarily manufactures, under contract, various types of high-technology equipment which it has designed and developed. The Company considers its business activities to be divided into two segments: Training Services Group (TSG) and the Control Systems Group (CSG). Product categories included in TSG are aircrew training devices and related services, disaster management training systems, and entertainment products. CSG includes sterilizers, environmental control systems, and hyperbaric chambers, along with parts and service support. The following segment information reflects the accrual basis of accounting.

	Training Services Group (TSG)	Control Systems Group (CSG)	Corporate	Company Total
		(amounts in thousands)		
Thirteen weeks ended May 28, 2010:				
Net sales	$ 7,932	$ 4,189	$	$ 12,121
Interest expense	136	92		228
Depreciation and amortization	192	154		346
Operating income (loss)	1,409	1,110	(278)	2,241
Income tax benefit				
Identifiable assets	19,180	5,797	16,081	41,058
Expenditures for segment assets	376	81	122	579
Thirteen weeks ended May 29, 2009:				
Net sales	$ 6,915	$ 2,666	$	$ 9,581
Interest expense	299	217		516
Depreciation and amortization	150	417		567
Operating income (loss)	1,894	(170)	(381)	1,343
Income tax benefit				
Identifiable assets	7,629	5,556	22,353	35,538
Expenditures for segment assets	241	155		396

	Thirteen weeks ended May 28, 2010:	Thirteen weeks ended May 29, 2009
Reconciliation to consolidated net income (loss):		
Operating income	$ 2,241	$ 1,343
Interest expense	(228)	(516)
Other, net	(72)	(55)
Income tax benefit		
Noncontrolling interest	(5)	(2)
Net income	$ 1,936	$ 770

Approximately 68% of sales totaling $8,279,000 in the thirteen weeks ended May 28, 2010 were made to the U.S. Government under two contracts and to one international customer. Approximately 24% of sales totaling $2,296,000 in the thirteen weeks ended May 29, 2009 were made to one customer in the international pilot training product line.

Included in the segment information for the thirteen weeks ended May 28, 2010 are export sales of $5,217,000, including sales to the Korean government for $4,474,000. For the thirteen week period ended May 29, 2009, there were international sales of $5,786,000 including sales to or relating to governments or commercial accounts in Saudi Arabia ($3,327,000), Malaysia ($667,000) and Turkey ($537,000).

Segment operating income consists of net sales less applicable costs and expenses relating to these revenues. Unallocated general corporate expenses and other expenses such as letter of credit fees have been excluded from the determination of the total profit/loss for segments. Corporate home office expenses are primarily central administrative office expenses. Other expenses include banking and letter of credit fees. Property, plant and equipment associated with the Company s NASTAR Center are included in the TSG segment; the remaining property, plant and equipment are not identified with specific business segments, as these are common resources shared by all segments.

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

FORWARD LOOKING STATEMENTS

Discussions of some of the matters contained in this Quarterly Report on Form 10-Q for Environmental Tectonics Corporation may constitute forward-looking statements within the meaning of the Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended, and as such, may involve risks and uncertainties. We have based these forward-looking statements on our current expectations and projections about future events or future financial performance, which include implementing our business strategy, developing and introducing new technologies, obtaining, maintaining and expanding market acceptance of the technologies we offer, and competition in our markets. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about ETC and its subsidiaries that may cause actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements.

These forward-looking statements include statements with respect to the Company s vision, mission, strategies, goals, beliefs, plans, objectives, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance and business of the Company, including, but not limited to, (i) projections of revenues, costs of materials, income or loss, earnings or loss per share, capital expenditures, growth prospects, dividends, capital structure, other financial items and the effects of currency fluctuations, (ii) statements of our plans and objectives of the Company or its management or Board of Directors, including the introduction of new products, or estimates or predictions of actions of customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, (iv) statements of assumptions and other statements about the Company or its business, (v) statements made about the possible outcomes of litigation involving the Company, (vi) statements regarding the Company s ability to obtain financing to support its operations and other expenses, and (vii) statements preceded by, followed by or that include terminology such as may, will, should, expect, plan, anticipate, believe, estin predict, potential, intend, or continue, and similar expressions. These forward-looking statements involve risks and uncertainties which are subject to change based on various important factors. Some of these risks and uncertainties, in whole or in part, are beyond the Company s control. Factors that might cause or contribute to such a material difference include, but are not limited to, those discussed in our Annual Report on Form 10-K for the fiscal year ended February 26, 2010, in the section entitled Risks Particular to Our Business. Shareholders are urged to review these risks carefully prior to making an investment in the Company s common stock.

The Company cautions that the foregoing list of factors that could affect forward-looking statements by ETC is not exclusive. Except as required by federal securities law, the Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

In this report all references to ETC, the Company, we, us, or our, mean Environmental Tectonics Corpora and our subsidiaries.

References to fiscal first quarter 2011 are references to the 13-week period ended May 28, 2010. References to fiscal first quarter 2010 are references to the 13-week period ended May 29, 2009. References to fiscal 2011 or the 2011 fiscal year are references to the fifty-two week period ended February 25, 2011. References to fiscal 2010 or the 2010 fiscal year are references to the fifty-two week period ended February 26, 2010.

Overview

ETC was incorporated in 1969 in Pennsylvania. For over forty years, we have provided our customers with products, service and support. Innovation, continuous technological improvement and enhancement, and product quality are core values and critical to our success. We are a significant supplier and innovator in the following product areas: (1) software driven products and services used to create and monitor the physiological effects of flight; (2) high performance jet tactical flight simulation; (3) steam and gas sterilization; (4) testing and simulation devices for the automotive industry; (5) hyperbaric and hypobaric chambers; and (6) driving and disaster simulation systems.

We operate in two business segments Training Services Group (TSG) and Control Systems Group (CSG). Our core technologies in TSG include the design, manufacture and sale of training services which consists of (1) software driven products and services used to create and monitor the physiological effects of flight; (2) high performance jet tactical flight simulation, and; (3) driving and disaster simulation systems, and in CSG include: (1) steam and gas sterilization; (2) testing and simulation devices for the automotive industry, and; (3) hyperbaric and hypobaric chambers. Product categories included in TSG are Aircrew Training Systems (ATS) and flight simulators, disaster management systems and entertainment applications. CSG includes sterilizers, environmental control devices and hyperbaric chambers along with parts and service support. Revenue and other financial information regarding our segments may be found in Note 11 Business Segment Information of the Notes to the Condensed Consolidated Financial Statements.

The following factors had an impact on our financial performance, cash flow and financial position for the fiscal quarter ended May 28, 2010:

Increased production under U.S. Government contracts

The Base Realignment and Closure (BRAC) Act passed in 2005 by Congress mandated base closures and consolidations through all the U.S. defense services. As a result of this Act, in the past two years we have been awarded two major contracts for pilot training. Our fiscal 2011 opening backlog of firm orders included approximately $48 million for two significant contracts from the U.S. Navy for a research disorientation trainer and the U.S. Air Force to provide a high performance training and research human centrifuge. As a result of engineering and production activity on these two contracts, sales to the U.S. Government increased by $2.2 million in our Training Services Group during the current fiscal quarter versus the prior fiscal quarter. On June 12, 2010, we were awarded an additional $38.3 million contract by the U. S. Air Force to provide a suite of altitude chambers. Although at the current time we have a significant sales backlog with the U.S. Government for equipment to being procured under the BRAC Act, given the current domestic economic conditions and political environment, it should not be assumed that any additional contracts will be awarded to us.

Exchange of long term debt, establishment of additional facility, and increase in bank line

On April 24, 2009, we entered into a transaction with H. F. Lenfest, a member of our Board of Directors and a significant shareholder, that provided for the following: (i) a $7,500,000 credit facility to be provided by Lenfest to ETC; (ii) exchange of the Subordinated Note held by Lenfest, together with all accrued interest and warrants issuable under the Subordinated Note, and all Series B Preferred Stock and Series C Preferred Stock held by Lenfest, together with all accrued dividends thereon, for a new class of preferred stock, Series E Preferred Stock, of the Company; and (iii) an increase of the existing $15,000,000 revolving line of credit with PNC Bank to $20,000,000. Having adequate cash from operations and additional availability under new and existing credit lines allowed us to effectively and efficiently execute on our contracts. Additionally, we expect to be adequately cash funded throughout fiscal 2011.

Positive impact of income taxes

During the first quarter of fiscal 2011, no income tax provision was recorded due to our utilization of significant net operating loss carryforwards. We use the asset and liability method of accounting for income taxes. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes as well as the valuation of net loss carryforwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the realizability of the related deferred tax asset.

Continued expanded use of our NASTAR Center

Our National Aerospace Training and Research (NASTAR) Center, which opened in fiscal 2008, is an integrated pilot training center offering a complete range of aviation training and research support for military aviation, civil aviation and the emerging commercial space market. The NASTAR Center houses state of the art equipment including the ATFS-400, a GYROLAB GL-2000 Advanced Spatial Disorientation Trainer, a Hypobaric Chamber, an Ejection Seat Trainer, and a Night Vision and Night Vision Goggle Training System. These products represent over forty years of pioneering development and training solutions for the most rigorous stresses encountered during high performance aircraft flight including the effects of altitude exposure, High G-force exposure, spatial disorientation and escape from a disabled aircraft.

During the past two fiscal years we have been successful in utilizing the NASTAR Center for research, space training and as a showroom to market our Authentic Tactical Fighting System technology. We feel that demonstrating tactical flight simulation in our NASTAR Center has been highly instrumental in our obtaining significant orders for our Aircrew Training Systems products.

Going forward, we are hopeful for expanded research aimed at examining the effectiveness of using centrifuge based simulation for Upset Recovery Training (URT) for commercial airline pilots. Loss of control in flight is a major cause factor in loss of life and hull damage aircraft accidents. Modern day commercial aviation currently has no requirement for training of pilots to deal with these situations, commonly referred to as upsets. Realistic training for responding to and recovering from upsets, or URT, requires more than a non-centrifuged based simulator because non-centrifuge-based simulators do not reproduce the physiological stresses and disorientation that a pilot experiences during an actual upset. We believe our GYROLAB simulator series is an answer to providing pilots with the dynamic environment necessary for effective training.

Table of Contents

Continued capital and consulting spending to enhance and market worldwide our Authentic Tactical Fighting Systems (ATFS) and other technologies.

During the past two fiscal years we have spent over $4.8 million (including $2.3 million in fiscal 2010) in capital, software development and consulting expenses. Most of this spending has been related to our pilot training simulation equipment. This includes engineering costs to improve the technical abilities of our ATFS line of products, validation effort associated with Upset Recovery Training, and consulting arrangements. Going forward, we expect spending to be significant for these efforts.

Common stock dilution.

As a result of our aforementioned refinancing transaction with H. F. Lenfest, our average fully diluted shares have increased by approximately 11.8 million shares. Given our positive financial performance, this increase in equivalent common shares has a dilutive impact on our earnings per share.

Critical Accounting Policies

The discussion and analysis of the Company s financial condition and results of operation are based upon the Company s condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these condensed consolidated financial statements requires the Company to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the Company s condensed financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that reflect significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. For a detailed discussion on the application of these and other accounting policies, see Note 2 to the Consolidated Financial Statements, Summary of Significant Accounting Policies in the Company s Annual Report on Form 10-K for the fiscal year ended February 26, 2010.

Table of Contents

Results of Operations

Thirteen weeks ended May 28, 2010 compared to thirteen weeks ended May 29, 2009

We have historically experienced significant variability in our quarterly revenue, earnings and other operating results, and our performance may fluctuate significantly in the future.

Summary Table of Results

	13 weeks ended May 28, 2010	13 weeks ended May 29, 2009	Variance $	Variance %
	(amounts in thousands)		( ) =Unfavorable	
Sales:				
Domestic	$ 2,918	$ 1,959	$ 959	49.0%
US Government	3,986	1,836	2,150	117.1
International	5,217	5,786	(569)	(9.8)
Total Sales	12,121	9,581	2,540	26.5
Gross Profit	5,130	4,427	703	15.9
Selling and marketing expenses	1,102	1,254	152	12.1
General and administrative expenses	1,463	1,602	139	8.7
Research and development expenses	324	228	(96)	(42.1)
Operating income	2,241	1,343	898	66.9
Interest expense, net	228	516	288	55.8
Other expense, net	72	55	(17)	(30.9)
Income taxes				n/a
Noncontrolling interest	5	2	(3)	(150.0)
Net income	$ 1,936	$ 770	$1,166	151.4%
Net income per common share (basic)	$ 0.15	$ 0.06	$ 0.09	150.0%
Net income per common share (diluted)	$ 0.09	$ 0.06	$ 0.03	50.0%

Net Income

The Company had a net income of $1,936,000 or $0.15 per share (basic) and $0.09 (diluted) during the first quarter of fiscal 2011 compared to net income of $770,000 or $0.06 per share (basic and diluted), for the first quarter of fiscal 2010, representing an improvement of $1,166,000, 151.4%. The improvement reflected a significant increase in gross profit (reflecting the higher sales level) coupled with lower operating expenses and interest expense. Increased research and development expenses acted as a partial offsets.

Table of Contents

Sales

The following schedule presents the Company s sales by segment, business unit and geographic area:

	(amounts in thousands)							
	Thirteen week period ended May 28, 2010				Thirteen week period ended May 29, 2009			
Segment sales:	**Domestic**	**USG**	**Inter-national**	**Total**	**Domestic**	**USG**	**Inter-national**	**Total**
Training Services Group:								
Pilot Training Services	$ 1	$4,003	$3,733	$ 7,737	$ 36	$1,345	$3,916	$5,297
Simulation			96	96	201		1,144	1,345
ETC-PZL and other	33		66	99	91		182	273
Total	$ 34	$4,003	$3,895	$ 7,932	$ 328	$1,345	$5,242	$6,915
Control Systems Group:								
Environmental	$ 108	$ (17)	$ 977	$ 1,068	$ 374	$ 491	$ 269	$1,134
Sterilizers	1,725			1,725	218			218
Hyperbaric	610	`	199	809	628	`	183	811
Service and spares	441		146	587	411		92	503
Total	2,884	(17)	1,322	4,189	1,631	491	544	2,666
Company total	$2,918	$3,986	$5,217	$12,121	$1,959	$1,836	$5,786	$9,581

Sales for the first quarter of fiscal 2011 were $12,121,000 as compared to $9,581,000 for the first quarter of fiscal 2010, an increase of $2,540,000 or 26.5%. As the table indicates, significant increases were realized in the U.S. Government and Domestic markets offset in part in by a decline in International sales.

Domestic Sales

Domestic sales in the first quarter of fiscal 2011 were **$**2,918,000 as compared to $1,959,000 in the first quarter of fiscal 2010, an increase of $959,000 or 49.0%, reflecting a significant increase in the sterilizer product line (up $1,507,000), of our Control Systems Group, partially offset by declines in most other product areas. Domestic sales represented 24.1% of the Company s total sales in the first quarter of fiscal 2011, as compared to 20.4% for the first quarter of fiscal 2010.

U.S. Government sales in the first quarter of fiscal 2011 were $3,986,000 as compared to $1,836,000 in the first quarter of fiscal 2010, an increase of $2,150,000 or 117.1%, and represented 32.9% of total sales in the first quarter of fiscal 2011 versus 19.2% for the first quarter of fiscal 2010. This increase is the result of sales of the Company s Pilot Training Systems products under significant contracts from the U.S. Navy for a research disorientation trainer and the U.S. Air Force to provide a high performance training and research human centrifuge.

International Sales

International sales, which include sales in the Company s subsidiary in Poland, for the first quarter of fiscal 2011, were $5,217,000 as compared to $5,786,000 in the first quarter of fiscal 2010, a decrease of $569,000 or 9.8%, and represented 43.0% of total sales, as compared to 60.4% in the first quarter of fiscal 2009. International performance reflected lower simulation sales (down $1,048,000) primarily for a contract in the Middle East which was completed in fiscal 2010. For the thirteen week period ended May 28, 2010, there were sales to the Korean government for $4,474,000. For the thirteen week period ended May 29, 2009, there were sales to or relating to governments or commercial accounts in Saudi Arabia ($3,327,000), Malaysia ($667,000) and Turkey ($537,000).

Fluctuations in sales to international countries from year to year primarily reflect percentage of completion (POC) revenue recognition on the level and stage of development and production on multi-year long-term contracts.

Gross Profit

Gross profit for the first quarter of fiscal 2011 was $5,130,000 as compared to $4,427,000 in the first quarter of fiscal 2010, an increase of $703,000 or 15.9%. As a percentage of sales, gross profit for the first quarter of fiscal 2011 was 42.3% compared to 46.2% for the same period a year ago. The gross margin dollar increase followed the sales increase in both governmental and domestic sales partially offset by the reduction in higher margin international sales. The 3.9 percentage point reduction in the gross margin rate as a percentage of sales primarily reflected reductions in the ATS and simulation product areas.

Selling and Marketing Expenses

Selling and marketing expenses for the first quarter of fiscal 2011 were $1,102,000 as compared to $1,254,000 in the first quarter of fiscal 2010, a decrease of $152,000 or 12.1%. This decrease primarily reflected reduced bid and proposal expenses and reduced commissions on the mix shift in sales in the current quarter to U.S. Government sales.

Table of Contents

General and Administrative Expenses

General and administrative expenses for the first quarter of fiscal 2011 were $1,463,000 as compared to $1,602,000 in the first quarter of fiscal 2011, a decrease of $139,000, 8.7%. The reduction was comprised of lower spending for legal fees and bad debt expense.

Research and Development Expenses

Research and development expenses, which are charged to operations as incurred, were $324,000 for the first quarter of fiscal 2011 as compared to $228,000 for the first quarter of fiscal 2010. The prior quarter reflected higher grant funds from the Turkish Government. Most of the Company s research efforts, which were and continue to be a significant cost of its business, are included in cost of sales for applied research for specific contracts, as well as research for feasibility and technology updates.

Interest Expense

Interest expense for the first quarter of fiscal 2011 was $228,000 as compared to $516,000 for the first quarter of fiscal 2010, representing a decrease of $288,000 or 55.8%, reflecting reduced bank borrowing and the July 2009 exchange of a $10 million convertible note for preferred stock.

Other Expense, Net

Other expense, net, was $72,000 for the first quarter of fiscal 2011 versus $55,000 for the first quarter of fiscal 2010. These expenses consist primarily of bank and letter of credit fees as well as foreign currency exchange gains or losses.

Income Taxes

Due to the utilization of net operating loss carry forwards available the Company did not record an income tax expense on the income in the current fiscal quarter.

The Company has reviewed the components of its deferred tax asset and has determined, based upon all available information, that its current and expected future operating income will more likely than not result in the realization of a portion of its deferred tax assets relating primarily to its net operating loss carryforwards. As of May 28, 2010, the Company had approximately $35.2 million of federal net loss carry forwards available to offset future income tax liabilities, beginning to expire in 2025. In addition, the Company has the ability to offset deferred tax assets against deferred tax liabilities created for such items as depreciation and amortization.

Liquidity and Capital Resources

The Company s liquidity position and borrowing availability improved significantly during the first quarter of 2011. Cash flow from operations was a positive $8,244,000. Working capital (current assets less current liabilities) was $10,940,000 and the Company s current ratio (current assets divided by current liabilities) was 1.72. The Company repaid over $5 million under its line of credit agreement and repurchased $1,000,000 of Series E Preferred Stock from Lenfest. This positive performance primarily reflected the net income in the period and milestone payment collections under long term contracts.

On April 24, 2009, we entered into a transaction with H. F. Lenfest, a member of our Board of Directors and a significant shareholder, that provides for the following: (i) a $7,500,000 credit facility to be provided by Lenfest to ETC; (ii) exchange of the Subordinated Note held by Lenfest, together with all accrued interest and warrants issuable under the Subordinated Note, and all Series B Preferred Stock and Series C Preferred Stock held by Lenfest, together with all accrued dividends thereon, for a new class of preferred stock, Series E Preferred Stock, of the Company; and (iii) an increase of the existing $15,000,000 revolving line of credit with PNC Bank to $20,000,000. Having adequate cash from operations and additional availability under new and existing credit lines allowed us to effectively and efficiently execute on our contracts. Additionally, we expect to be adequately cash funded throughout fiscal 2011. As of May 28, 2010, the Company had not utilized any of the $7.5 million available funding under the Lenfest credit facility.

The schedule below presents the Company s available borrowings under its existing credit facilities (amounts in thousands):

	Total Facility	Amount Borrowed	Amount Available	Total Facility	Amount Borrowed	Amount Available

Credit facility*		**As of May 28, 2010:**			**As of February 26, 2010:**	
PNC line of credit	$20,000	$ 5,835	$14,165	$20,000	$11,128	$ 8,872
Lenfest credit line	7,500		7,500	7,500		7,500
Dedicated line of credit	5,422	5,422		5,422	5,422	
Total	$32,922	$11,257	$21,665	$32,922	$16,550	$16,372

* See Note 6 Long-tem Debt and Credit Arrangements in the Notes to the Condensed Consolidated Financial Statements.

Net cash provided by (used for) operating activities:

Cash provided by operations is driven by income from sales of our products offset by the timing of receipts and payments in the ordinary course of business.

During the first quarter of fiscal 2011, we generated $8,244,000 of cash from operating activities versus a usage of $1,156,000 for the first quarter of fiscal 2010, an improvement of $9,400,000. Cash generated in the current period primarily reflected significantly improved operating results, customer progress payments under long-term POC contracts, and non-cash expenses of depreciation and amortization. These items were offset in part by a reduction in billings in excess of costs under long-term POC contracts as well as an increase in prepaid commissions resulting from payments received under POC contracts that have not been recognized as revenue.

Net cash used for investing activities:

Cash used for investing activities primarily relates to funds used for capital expenditures in property and equipment. These uses of cash are offset by sales and borrowings under our credit facilities. The Company s investing activities used $579,000 in the first quarter of fiscal 2011 and consisted primarily of costs for the continued construction activities and the manufacturing of demonstration simulators for our NASTAR Center coupled with higher software enhancements for our Advanced Tactical Fighter Systems technology.

Net cash used for financing activities:

The Company s financing activities used $9,675,000 of cash during the first quarter of fiscal 2011. This primarily reflected the repayments under the Company s bank line, and the repurchase of $1,000,000 of Series E Preferred Stock from and payments of Series D and E Preferred Stock dividends to H.F. Lenfest.

Outlook

We expect to use our cash, cash equivalents and credit facilities for working capital and general corporate purposes, products, product rights, technologies, property, plant and equipment, the payment of contractual obligations, including scheduled interest payments on our credit facilities and dividends on our preferred stock, the potential acquisition of businesses, and/or the purchase, redemption or retirement of our credit facilities and preferred stock. We expect that net sales of our currently marketed products should allow us to continue to generate positive operating cash flow in fiscal 2011. At this time, however, we cannot accurately predict the effect of certain developments on our anticipated rate of sales growth in 2012 and beyond, because of factors such as the degree of market acceptance, the impact of competition, the effectiveness of our sales and marketing efforts, and the outcome of our efforts to develop our products.

Backlog

Below is a breakdown of the Company s May 28, 2010 and February 26, 2010 sales backlog (amounts in thousands except percentages):

8. Bank Term Loan Payable

The Company s $5.0 million revolving credit facility was amended in August 2011, extending its term and adjusting certain other financial terms and covenants. Unless earlier payment is required by an event of default, all principal and unpaid interest will be due and payable on August 31, 2016. At the Company s option, the Revolving Credit Facility (the Credit Agreement) bears interest at either the prime rate less 1.00% or the London Interbank Offered Rate (LIBOR) plus the applicable LIBOR margin. The applicable LIBOR margin is based on the ratio of total funded debt to earnings before interest, other income and expense, income taxes, depreciation, and amortization (EBITDA) for the preceding four fiscal quarters. As of September 30, 2014, the applicable LIBOR margin was 1.25%.

The Company is also required to pay an unused line fee on the daily unused amount of the Credit Agreement at a per annum rate based on the ratio of total funded debt to EBITDA for the preceding four fiscal quarters. As of September 30, 2014, the per annum unused line fee rate was 0.20%.

At September 30, 2014 and December 31, 2013 there were no amounts outstanding under the Credit Agreement. Pursuant to the Credit Agreement, there was a $1.0 million standby letter of credit (Letter of Credit) related to the Company s corporate headquarters lease outstanding at September 30, 2014, bringing the Company s available borrowings on the $5.0 million facility to $4.0 million.

Borrowings under the Credit Agreement are collateralized by a security interest in substantially all assets of the Company. Covenants governing the Credit Agreement include the maintenance of certain financial ratios. At September 30, 2014, the Company was in compliance with all covenants under the Credit Agreement.

In the third quarter of 2014, the Company paid $0.7 million in cash as a security deposit on its corporate headquarters lease. The Letter of Credit, which was also being held against the lease, was cancelled in October 2014.

9. Commitments and Contingencies

Operating Leases

The Company conducts its operations in leased office facilities under various noncancelable operating lease agreements that expire through January 2020. In August 2009, the Company entered into an agreement to lease approximately 87,875 square feet of office space in Newton, Massachusetts. The lease commenced in February 2010 and has a term of ten years. The Company is receiving certain rent concessions over the life of the lease. In November 2010, the Newton lease was amended to include an additional 8,400 square feet of office space. The amended lease commenced in March 2011 and runs concurrently with the term of the original lease. The Company is receiving certain rent concessions over the life of the amended lease.

Certain of the Company s operating leases include lease incentives and escalating payment amounts and are renewable for varying periods. The Company is recognizing the related rent expense on a straight-line basis over the term of the lease taking into account the lease incentives and escalating lease payments.

Future minimum lease payments under the Company s noncancelable operating leases at September 30, 2014 are as follows:

Years Ending December 31:	**Minimum Lease Payments (Unaudited)**
2014 (October 1st December 31st)	$ 1,126
2015	3,998
2016	4,048
2017	3,705
2018	3,831
Thereafter	4,405
	$ 21,113

The Company had an irrevocable standby letter of credit outstanding in the aggregate amount of $1.0 million as of September 30, 2014 that supported the lease the Company entered into in 2009 for its corporate headquarters.

In the third quarter of 2014, the Company paid $0.7 million in cash as a security deposit on its corporate headquarters lease. The Letter of Credit, which was also being held against the lease, was cancelled in October 2014.

Net Worth Tax Contingency

In late March 2010, the Company received a letter from the Department of Revenue of the Commonwealth of Massachusetts (the MA DOR) requesting documentation demonstrating that TSC has been classified by the MA DOR as a Massachusetts security corporation. Following subsequent correspondence with the MA DOR and a settlement conference on March 22, 2011, the Company received a Notice of Assessment from the MA DOR with respect to additional excise taxes

13

on net worth related to TSC. Based on the Company s previous assessment that it was probable that the MA DOR would require an adjustment to correct TSC s tax filings such that it will be treated as a Massachusetts business corporation for the applicable years, the Company has recorded a liability representing its best estimate at that time of the potential net worth tax exposure. The tax benefits available to a Massachusetts security corporation are comprised of (i) a different rate structure (1.32% on gross investment income vs. 9.5% on net income) (See Note 13) and (ii) exemption from the 0.26% excise tax on net worth. On August 17, 2011, the Company filed Applications for Abatement with the MA DOR. On January 6, 2012, the Company filed Petitions for Formal Procedure with the Massachusetts Appellate Tax Board. A trial took place on April 29, 2014; as of the date of this report no decision has been rendered. As of September 30, 2014 the Company has recorded a liability of approximately $260 to account for the tax differential in all open years, including penalties and interest.

Litigation

From time to time and in the ordinary course of business, the Company may be subject to various claims, charges, and litigation. At September 30, 2014 and December 31, 2013, the Company did not have any pending claims, charges, or litigation that it expects would have a material adverse effect on its consolidated financial position, results of operations, or cash flows.

10. Comprehensive Income (Loss)

Comprehensive income (loss) includes all changes in equity during a period, except those resulting from investments by stockholders and distributions to stockholders. For the three and nine months ended September 30, 2014 and 2013 the Company s comprehensive income (loss) is as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2014	2013	2014	2013
	(Unaudited)			
Net income (loss)	$ 938	$ 577	$ 2,376	$ (1,836)
Other comprehensive (loss) income:				
Unrealized (loss) gain on investments (net of tax effect of $(2), $14, $(4) and $4, respectively)	(4)	27	(7)	8
Unrealized (loss) gain on foreign currency exchange	(181)	(31)	(156)	264
Other comprehensive (loss) income	(185)	(4)	(163)	272
Total comprehensive income (loss)	$ 753	$ 573	$ 2,213	$ (1,564)

11. Stock-Based Compensation

Stock Option Plans

In September 1999, the Company approved a stock option plan (the 1999 Plan) that provides for the issuance of up to 12,384,646 shares of common stock incentives. The 1999 Plan provides for the granting of incentive stock options (ISOs), nonqualified stock options (NSOs), and stock grants. These incentives may be offered to the Company s employees, officers, directors, consultants, and advisors. ISOs may not be granted at less than fair market value on the date of grant, as determined by the Company s Board of Directors (the Board). Each option shall be exercisable at such times and subject to such terms as determined by the Board; grants generally vest over a four year period, and expire no later than ten years after the grant date.

In April 2007, the Board approved the 2007 Stock Option and Incentive Plan (the 2007 Plan), which was approved by the stockholders of the Company and became effective upon the consummation of the Company s IPO in May 2007. Effective upon the consummation of the IPO, no further awards were made pursuant to the 1999 Plan, but any outstanding awards under the 1999 Plan remain in effect and continue to be subject to the terms of the 1999 Plan. The 2007 Plan allows the Company to grant ISOs, NSOs, stock appreciation rights, deferred stock awards, restricted stock and other awards. Under the 2007 Plan, stock options may not be granted at less than fair market value on the date of grant, and grants generally vest over a four year period. Stock options granted under the 2007 Plan expire no later than ten years after the grant date. The Company has reserved for issuance an aggregate of 2,911,667 shares of common stock under the 2007 Plan plus an additional annual increase to be added automatically on January 1 of each year, beginning on January 1, 2008, equal to the lesser of (a) 2% of the outstanding number of shares of common stock (on a fully-diluted basis) on the immediately preceding December 31 and (b) such lower number of shares as may be determined by the Company s compensation committee. The number of shares available for issuance under the 2007 Plan is subject to adjustment in the event of a stock split, stock

Table of Contents

dividend or other change in capitalization. Generally, shares that are forfeited or canceled from awards under the 2007 Plan also will be available for future awards. To date, approximately 6.7 million shares have been added to the 2007 Plan in accordance with the automatic annual increase. In addition, shares subject to stock options returned to the 1999 Plan, as a result of their expiration, cancellation or termination, are automatically made available for issuance under the 2007 Plan. As of September 30, 2014 a total of 1,615,872 shares were available for grant under the 2007 Plan.

Accounting for Stock-Based Compensation

The Company uses the Black-Scholes option pricing model to calculate the grant-date fair value of an award.

As there was no public market for the Company s common stock prior to the Company s IPO in May 2007 and, until recently, limited historical information on the volatility of its common stock since the date of the Company s IPO, the Company has historically determined the volatility for options granted based on an analysis of the historical volatility of the Company s stock and reported data for a peer group of companies that issued options with substantially similar terms. Beginning in 2013, the expected volatility of options granted has been determined using a weighted average of the historical volatility of the Company s stock for a period equal to the expected life of the option. The expected life of options has been determined utilizing the simplified method. The risk-free interest rate is based on a zero coupon United States treasury instrument whose term is consistent with the expected life of the stock options. The Company has not paid and does not anticipate paying cash dividends on its shares of common stock; therefore, the expected dividend yield is assumed to be zero.

A summary of the stock option activity under the Company s stock option plan for the nine months ended September 30, 2014 is presented below:

Year-to-Date Activity	Options Outstanding	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
		(Unaudited)		
Options outstanding at December 31, 2013	4,467,248	$ 7.30		
Granted				
Exercised	(408,490)	5.41		
Forfeited				
Cancelled	(26,052)	8.30		
Options outstanding at September 30, 2014	4,032,706	$ 7.49	2.6	$ 6,795
Options exercisable at September 30, 2014	4,019,581	$ 7.49	2.6	$ 6,772
Options vested or expected to vest at	4,031,277	$ 7.49	2.6	$ 6,792

September 30, 2014 (1)

(1) In addition to the vested options, the Company expects a portion of the unvested options to vest at some point in the future. Options expected to vest is calculated by applying an estimated forfeiture rate to the unvested options.

During the nine months ended September 30, 2014 and 2013, the total intrinsic value of options exercised (i.e. the difference between the market price at exercise and the price paid by the employee to exercise the options) was $0.9 million and $1.2 million, respectively, and the total amount of cash received from exercise of these options was $2.2 million and $0.9 million, respectively. The total grant date fair value of stock options granted after January 1, 2006 that vested during the nine months ended September 30, 2014 and 2013 was $0.1 million and $0.5 million, respectively.

Restricted Stock Awards

Restricted stock awards are valued at the market price of a share of the Company s common stock on the date of grant. A summary of the restricted stock award activity under the 2007 Plan for the nine months ended September 30, 2014 is presented below:

Table of Contents

Year-to-Date Activity	Shares	Weighted-Average Grant Date Fair Value Per Share (Unaudited)	Aggregate Intrinsic Value
Nonvested outstanding at December 31, 2013	2,777,500	$ 5.26	
Granted	559,477	7.97	
Vested	(691,560)	5.06	
Forfeited	(37,500)	5.57	
Nonvested outstanding at September 30, 2014	2,607,917	$ 5.90	$ 22,402

The total grant-date fair value of restricted stock awards that vested during the nine months ended September 30, 2014 and 2013 was $3.5 million and $3.3 million, respectively.

As of September 30, 2014, there was $12.7 million of total unrecognized compensation expense related to stock options and restricted stock awards which is expected to be recognized over a weighted average period of 2.2 years.

12. Stockholders Equity

Reserved Common Stock

As of September 30, 2014, the Company has reserved 8,460,246 shares of common stock for options outstanding and restricted stock awards that have not been issued as well as those available for grant under stock option plans.

Common Stock Repurchase Programs

On August 5, 2014, the Company announced that, on August 4, 2014, its Board of Directors authorized a $20 million stock repurchase program (the 2014 Program). The Company is authorized to repurchase the Company s common stock from time to time on the open market or in privately negotiated transactions. The timing and amount of any shares repurchased will be determined based on an evaluation of market conditions and other factors. The Company may elect to implement a Rule 10b5-1 trading plan to make such purchases, which would permit shares to be repurchased when the Company might otherwise be precluded from doing so under insider trading laws. The 2014 Program may be suspended or discontinued at any time.

On August 3, 2012, the Company s Board of Directors authorized a $20 million stock repurchase program (the 2012 Program) authorizing the Company to repurchase its common stock from time to time on the open market or in privately negotiated transactions. The timing and amount of any shares repurchased was determined based on an evaluation of market conditions and other factors. The Company elected to implement a Rule 10b5-1 trading plan to make such purchases, which permits shares to be repurchased when the Company might otherwise be precluded from doing so under insider trading laws. The 2012 Program was terminated immediately prior to the commencement of the tender offer on September 25, 2013 (as described below).

During the quarter ended September 30, 2014 the Company repurchased 311,522 shares of common stock for $2.7 million pursuant to the 2014 Program. During the nine months ended September 30, 2013 the Company repurchased

2,610,279 shares of common stock for $12.4 million pursuant to the 2012 Program. Repurchased shares are recorded under the cost method and are reflected as treasury stock in the accompanying Consolidated Balance Sheets. All repurchased shares were funded with cash on hand.

Secondary Offering

In May 2014, the Company completed a secondary public offering of 5,750,000 shares of common stock at a price of $6.25 per share. All of the shares sold in the secondary public offering were sold by selling stockholders and the Company did not receive any proceeds from the offering. The Company incurred fees of approximately $0.5 million related to legal, accounting and other fees in connection with the secondary public offering, which are included in general and administrative expenses in the Statement of Operations and Comprehensive Income (Loss).

Table of Contents

Tender Offer

On September 25, 2013, the Company commenced a tender offer to purchase up to 6.5 million shares of its common stock, representing approximately 16.79% of the shares of TechTarget s common stock issued and outstanding at that time, at a price of $5.00 per share. On September 23, 2013, the last reported sale price of the Company s common stock was $4.79 per share.

The tender offer expired on October 24, 2013. In accordance with applicable SEC regulations and the terms of the tender offer, the Company exercised the right to purchase additional shares and based on the final tabulation by Computershare Trust Company, N.A., the Depositary for the tender offer, the Company accepted for purchase 7,100,565 shares of its common stock for a total cost of $35.5 million. Repurchased shares were recorded under the cost method and are reflected as treasury stock in the accompanying Consolidated Balance Sheets. The total cost of the tender offer was $35.6 million, which includes approximately $0.1 million in costs directly attributable to the purchase.

13. Income Taxes

The Company s effective income tax rate was 36.7% and 38.7% for the nine months ended September 30, 2014 and 2013, respectively. The effective income tax rate is based upon the estimated annual effective tax rate in compliance with ASC 740, *Income Taxes*, and other related guidance. The Company updates the estimate of its annual effective tax rate at the end of each quarterly period. The Company s estimate takes into account estimations of annual pre-tax income, the geographic mix of pre-tax income and its interpretations of tax laws.

The Company s practice is to recognize interest and/or penalties related to income tax matters in income tax expense. These amounts were not material in the nine months ended September 30, 2014.

In March 2010, the Company received a letter from the MA DOR requesting documentation demonstrating that TSC, a wholly-owned subsidiary of the Company, has been classified by the MA DOR as a Massachusetts security corporation. Based on subsequent correspondence with the MA DOR, the Company determined that it was more likely than not that the MA DOR would require an adjustment to correct TSC s tax filings such that it will be treated as a Massachusetts business corporation for the applicable years. The tax benefit available to a Massachusetts security corporation is a lower income tax rate. The Company recorded a tax reserve for approximately $0.4 million. The tax benefits available to a Massachusetts security corporation are comprised of (i) a different rate structure (1.32% on gross investment income vs. 9.5% on net income) and (ii) exemption from the 0.26% excise tax on net worth (see Note 9). On August 17, 2011, the Company filed Applications for Abatement with the MA DOR. On January 6, 2012, the Company filed Petitions under Formal Procedure with the Massachusetts Appellate Tax Board. A trial took place on April 29, 2014; no decision has been rendered as of the date of this report. As of September 30, 2014 the Company has recorded a liability of approximately $670 to account for the tax differential in all open years, which includes penalties and interest for the potential state income tax liability arising from the difference between the income tax rates applicable to security corporations and business corporations in Massachusetts.

There are no income tax examinations currently in process with the exception of the matter noted above related to the MA DOR.

14. Segment Information

The Company views its operations and manages its business as one operating segment based on factors such as how the Company manages its operations and how its executive management team reviews results and makes decisions on how to allocate resources and assess performance.

Geographic Data

Net sales to unaffiliated customers by geographic area* were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
		(Unaudited)		
United States	$ 20,859	$ 17,794	$ 59,256	$ 51,998
International	5,573	4,317	16,301	12,759
Total	$ 26,432	$ 22,111	$ 75,557	$ 64,757

Table of Contents

Long-lived assets by geographic area were as follows:

	September 30, 2014 (Unaudited)	December 31, 2013
United States	$ 100,450	$ 101,241
International	6,495	7,344
Total	$ 106,945	$ 108,585

* based on current customer billing address; does not consider the geo-targeted, or target audience, location of the campaign

Table of Contents

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the consolidated financial statements and accompanying notes included elsewhere in this Quarterly Report on Form 10-Q. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those discussed below and elsewhere in this Quarterly Report on Form 10-Q, particularly under the heading Risk Factors.

Overview

Background

We are a leading provider of specialized online content and brand advertising that brings together buyers and sellers of corporate information technology (IT) products. We sell customized marketing programs that enable IT vendors to reach corporate IT decision makers who are actively researching specific purchases. In addition we offer a number of data analytics solutions that help our customers more efficiently target their sales efforts.

IT professionals have become increasingly specialized, and rely on our network of over 150 websites, each of which focuses on a specific IT sector such as storage, security or networking, for key decision support information tailored to their specific areas of responsibility. We work with our advertising customers to develop customized marketing programs, often providing them with multiple offerings in order to target their desired audience of IT professionals more effectively. Our service offerings address the lead generation, project opportunity information, and branding objectives of our advertising customers. In the nine months ended September 30, 2014, lead generation and branding remained our primary sources of revenue, while project opportunity information, driven by growth in our IT Deal Alert products, contributed approximately 20% of online revenue as compared with approximately 3% for the same period in 2013.

We enable IT professionals to navigate the complex and rapidly-changing IT landscape where purchasing decisions can have significant financial and operational consequences. Our content strategy includes three primary sources which IT professionals use to assist them in their pre-purchase research: independent content provided by our professionals, vendor-generated content provided by our customers and user-generated, or peer-to-peer, content. In addition to utilizing our independent content, registered members are able to conduct their pre-purchase research by accessing extensive vendor content across our network of websites. Our network of websites also allows users to seamlessly interact and contribute content, which is highly valued by IT professionals during their research process.

We have a large and growing base of registered members, which totaled over 14.9 million as of September 30, 2014. The targeted nature of our user base enables IT vendors to reach a specialized audience efficiently because our content is highly segmented and aligned with the IT vendors specific products. Since our founding in 1999, we have developed a broad customer base. During 2013, we delivered advertising campaigns for approximately 1,200 customers.

Executive Summary

Our revenue for the three months ended September 30, 2014 grew approximately 20%, to $26.4 million, when compared with the same period in 2013. This growth was primarily driven by two factors: continued growth of international revenue from our online products, and further adoption of our new IT Deal Alert offering. Both of these factors remain key areas of focus for our management team, and we believe they may contribute to our continued revenue growth. IT Deal Alert is a suite of services that leverages our proprietary audience activity data to enable us to identify purchase intent among our audience of IT professionals. At the same time, our international business is benefitting from the continued shift in adoption of online tools from traditional print sources by IT professionals in overseas markets.

During the third quarter of 2014, we made further progress on our strategy to grow our business and increase the reach of our offerings by continuing to execute on our strategic plans for the roll-out of IT Deal Alert and the continued expansion of our direct international capabilities.

Our key strategic initiatives include:

Product IT Deal Alert revenues (including international IT Deal Alert revenue of $0.7 million which is also included in international revenues discussed below) were approximately $4.8 million in the quarter, up from approximately $0.6 million in the third quarter of 2013. In the third quarter of 2014 we had over 175 active

Table of Contents

customers utilizing our IT Deal Alert service; this is up from 150 customers in the second quarter of 2014. We continue to receive very positive feedback from customers on the service and expect IT Deal Alert to be a meaningful growth driver in the remainder of 2014 and into 2015.

Geographic During the quarter approximately 29% of our revenues were derived from international geo-targeted campaigns (international), where our target audience is outside North America. International revenue (which also includes international IT Deal Alert revenue of $0.7 million as discussed above) increased in excess of 28% in the three months ended September 30, 2014 as compared to the same period a year ago. We believe that our integrated product offering across regions continues to resonate with international marketers and is contributing to our successful results. We plan on continuing to invest in these capabilities as we seek opportunities to increase our global reach; we are now offering our Qualified Sales Opportunities in the UK, Europe, and APAC. Core (non-IT Deal Alert) online has stabilized and we believe the stabilization will continue.

Revenue growth for the three month period ended September 30, 2014 as compared to the same period in 2013 was as follows:

	Three months ended September 30,		Growth rate
	2014	2013	
	(unaudited) ($ s in thousands)		
Total Online	$ 24,218	$ 18,830	29%
Total Online by Geographic Area:			
North America:			
North America Core Online	12,477	12,344	1%
North America IT Deal Alert	4,102	565	626%
Total North America Online	16,579	12,909	28%
International:			
International Core Online	6,986	5,861	19%
International IT Deal Alert	653	60	988%
Total International Online	7,639	5,921	29%
Total Online by Product:			
Core Online:			
North America Core Online	12,477	12,344	1%
International Core Online	6,986	5,861	19%
Total Core Online	19,463	18,205	7%
IT Deal Alert:			
North America IT Deal Alert	4,102	565	626%
International IT Deal Alert	653	60	988%
Total IT Deal Alert	4,755	625	661%
Total Events	2,214	3,281	-33%

Total Revenues	$ 26,432	$ 22,111	20%

Business Trends

The following discussion highlights key trends affecting our business.

Macro-economic Conditions and Industry Trends. Because most of our customers are IT vendors, the success of our business is intrinsically linked to the health, and subject to the market conditions, of the IT industry. In the three months ended September 30, 2014, we did not see any meaningful improvement in the IT market and many of our customers continue to be revenue-challenged. As a result, marketing budgets continue to be under pressure and our growth was driven in large part by the return on the investments we made during the downturn in our direct international operations and our new data subscription product, IT Deal Alert, which is driving market share gains for us. While we will continue to invest in these growth areas, management will continue to carefully control discretionary spending such as travel and entertainment, and the filling of new and replacement positions, in an effort to maintain profit margins and cash flow.

Customer Segments. In the three months ended September 30, 2014, our year-over-year revenue from our top 12 global customers increased by approximately 30%, our mid-sized customers (our next largest 100 customers) increased by approximately 18% and our smaller customers increased by approximately 29%. Although all three segments showed year-over-year growth, all three segments continued to report a challenging environment. This translated into our customers remaining cautious with their marketing expenditures.

Sources of Revenues

We sell advertising programs to IT vendors targeting a specific audience within a particular IT sector or sub-sector. We maintain multiple points of contact with our customers to provide support throughout their organizations and their customers IT sales cycles. As a result, our customers often run multiple advertising programs with us in order to target their desired audience of IT professionals more effectively. There are multiple factors that can impact our customers advertising objectives and spending with us, including but not limited to, IT product launches, increases or decreases to their advertising budgets, the timing of key industry marketing events, responses to competitor activities and efforts to address specific marketing objectives such as creating brand awareness or generating sales leads. Our services are generally delivered under short-term contracts that run for the length of a given advertising program, typically less than six months. In the three months ended September 30, 2014, lead generation and branding remained our primary sources of revenue, while project opportunity information, driven by growth in our IT Deal Alert products, contributed approximately 18% of total revenue as compared with approximately 3% for the same period in 2013.

We use both online and event offerings to provide IT vendors with numerous touch points to reach key IT decision makers and to provide IT professionals with highly specialized content across multiple forms of media. We are experienced in assisting advertisers to develop custom advertising programs that maximize branding and ROI. The following is a description of the services we offer:

Online. Online revenue represented 92% and 85% of total revenues for the three months ended September 30, 2014 and 2013, respectively and 93% and 89% of total revenues for the nine months ended September 30, 2014 and 2013, respectively. Our network of websites forms the core of our content platform. Our websites provide IT professionals with comprehensive decision support information tailored to their specific areas of responsibility and purchasing decisions. Through our websites, we offer a variety of online media offerings to connect IT vendors to IT professionals. Our lead generation offerings allow IT vendors to maximize ROI by capturing qualified sales leads from the distribution and promotion of content to our audience of IT professionals. All of our lead generation campaigns offer the Activity Intelligence Dashboard, a technology platform that gives our customers marketers and sales representatives a real-time view of their prospects, which includes insights on the research activities of technology buying teams, including at an account level. Lead generation offerings may also include an additional service, TechTarget Re-Engage (formerly called Nurture & Qualify), which helps both technology marketers and their sales teams to identify highly active prospects, detect emerging projects, retarget interested buying teams, and accelerate engagement with specific accounts.

Our lead generation offerings may also include the syndication of the following:

White Papers. White papers are technical documents created by IT vendors to describe business or technical problems which are addressed by the vendors products or services. As part of a lead generation campaign, we post white papers on our relevant websites and our users receive targeted promotions about these content assets. Prior to viewing white papers, our registered members and visitors supply their corporate contact information and agree to receive further information from the vendor. The corporate contact and other qualification information for these leads are supplied to the vendor in real time through our proprietary lead management software.

Webcasts, Podcasts, Videocasts and Virtual Trade Shows. Webcasts, podcasts, videocasts, virtual trade shows and similar content bring informational sessions directly to attendees desktops and mobile devices. As is the case with white papers, our users supply their corporate contact and qualification information to the webcast, podcast, videocast or virtual trade show sponsor when they view or download the content. Sponsorship includes access to the registrant information and visibility before, during and after the event.

Table of Contents

Our branding offerings provide IT vendors exposure to targeted audiences of IT professionals actively researching information related to their products and services and include display advertising (including banners) and custom offerings. Display advertising can be purchased on specific websites within our network and against specific technology segments. These offerings give IT vendors the ability to increase their brand awareness to highly specialized IT sectors.

Our other offerings include the following:

IT Deal Alert. IT Deal Alert is a suite of services for advertisers that leverages the detailed purchase intent data that we collect about end-user IT organizations. Through proprietary scoring methodologies, we use this data to help advertisers identify and prioritize accounts whose content consumption around specific IT topics indicates that they are in-market for a particular product or service. We also use the data directly to identify and further profile accounts upcoming purchase plans.

IT Deal Alert: Qualified Sales Opportunities is a product that profiles specific in-progress purchase projects, including information on scope and purchase considerations.

IT Deal Alert: Account Watch is an annual subscription service powered by our Activity Intelligence platform which integrates with salesforce.com. The breadth and depth of our targeted content allows IT Deal Alert: Account Watch to identify active technology projects based on the activity of serious buyers in approximately 80 technology-specific segments.

Custom Content Creation. In support of our advertisers lead generation programs, we will sometimes create white papers, case studies, webcasts, videos or even entire microsites to our customers specifications through our Custom Media team. These customized content assets are then promoted to our audience in the context of the advertisers lead generation programs. Our custom offerings allow customers to have content or entire microsites created that focus on topics related to their marketing objectives and include promotion of these vehicles to our users, which includes IT professionals and buyers of IT products.

Content Sponsorships. IT vendors, or groups of vendors, pay us to sponsor independent editorially created content vehicles on specific technology topics where the registrant information is then provided to all participating sponsors. In some cases, these vehicles are supported by multiple sponsors in a single segment, with the registrant information provided to all participating sponsors. Because these offerings are editorially driven, advertisers get the benefit of association with independently created content as well as access to qualified sales leads that are researching the topic.

List Rentals. We also offer IT vendors the ability to message registered members on topics related to their interests by renting our e-mail and postal lists of registered members, which is organized using specific criteria such as company size, geography or job title.

Third Party Revenue Sharing Arrangements. We have revenue sharing arrangements with certain third parties to allow for the licensing of our online content, for the renting of our database of opted-in e-mail subscribers and to allow advertising from customers of certain third parties to be made available to our website visitors. In each of these arrangements we are paid a share of the resulting revenue.

Events. Events revenue represented 8% and 15% of total revenues for the three months ended September 30, 2014 and 2013, respectively and 7% and 11% of total revenues for the nine months ended September 30, 2014 and 2013, respectively. Most of our media groups operate revenue-generating events. The majority of our events are free to IT professionals and are sponsored by IT vendors. Attendees are pre-screened based on event-specific criteria such as sector-specific budget size, company size, or job title. We offer three types of events: multi-day conferences, single-day seminars and custom events. Multi-day conferences provide independent content provided by our professionals to our attendees and allow vendors to purchase exhibit space and other sponsorship offerings that enable interaction with the attendees. We also hold single-day seminars on various topics in major cities. These seminars provide independent content provided by our professionals on key sub-topics in the sectors we serve, are free to qualified attendees, and offer multiple vendors the ability to interact with specific, targeted audiences actively focused on buying decisions. Our custom events differ from our seminars in that they are exclusively sponsored by a single IT vendor and the content is driven primarily by the sole sponsor.

Cost of Revenues, Operating Expenses and Other

Expenses consist of cost of online and event revenues, selling and marketing, product development, general and administrative, depreciation, amortization and net interest and other expenses. Personnel-related costs are a significant component of each of these expense categories except for depreciation and amortization related expenses.

Cost of Online Revenue. Cost of online revenues consist primarily of: salaries and related personnel costs; member acquisition expenses (primarily keyword purchases from leading Internet search sites); freelance writer expenses; website hosting costs; vendor expenses associated with the delivery of webcast, podcast, videocast and similar content, and list rental offerings; stock-based compensation expenses; facility expenses and other related overhead.

Cost of Events Revenue. Cost of events revenues consist primarily of: facility expenses, including food and beverages for the event attendees as well as office space; salaries and related personnel costs; travel-related expenses; event speaker expenses; stock-based compensation expenses; and other related overhead.

Selling and Marketing. Selling and marketing expenses consist primarily of: salaries and related personnel costs; sales commissions; travel-related expenses; stock-based compensation expenses; facility expenses and related overhead. Sales commissions are recorded as expense when earned by the employee, based on recorded revenue.

Product Development. Product development includes the creation and maintenance of our network of websites, advertiser offerings and technical infrastructure. Product development expense consists primarily of salaries and related personnel costs; stock-based compensation expenses; facility expenses and other related overhead.

General and Administrative. General and administrative expenses consist primarily of: salaries and related personnel costs; facility expenses and related overhead; accounting, legal and other professional fees; and stock-based compensation expenses.

Depreciation. Depreciation expense consists of the depreciation of our property and equipment. Depreciation of property and equipment is calculated using the straight-line method over their estimated useful lives, ranging from two to ten years.

Amortization of Intangible Assets. Amortization of intangible assets expense consists of the amortization of intangible assets recorded in connection with our acquisitions. Separable intangible assets that are not deemed to have an indefinite life are amortized over their estimated useful lives, which range from three to ten years, using methods that are expected to reflect the estimated pattern of economic use.

Interest and Other Income (Expense), Net. Interest income (expense), net consists primarily of interest income earned on cash, cash equivalents and short and long-term investments less any interest expense incurred. We historically have invested our cash in money market accounts, municipal bonds and government agency bonds. Other income (expense), net consists of non-operating gains or losses, primarily related to foreign currency exchange.

Application of Critical Accounting Policies and Use of Estimates

The discussion of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates, judgments and assumptions that affect the reported amount of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue, long-lived assets, goodwill, allowance for doubtful accounts, stock-based compensation, contingent liabilities, self-insurance accruals and income taxes. We based our estimates of the carrying value of certain assets and liabilities on historical experience and on various other assumptions that we believe to be reasonable. In many cases, we could reasonably have used different accounting policies and estimates. In some cases, changes in the accounting estimates are reasonably likely to occur from period to period. Our actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect our more significant judgments used in the preparation of our consolidated financial statements. See the notes to our consolidated financial statements for information about these critical accounting policies as well as a description of our other accounting policies.

Table of Contents

Revenue Recognition

We generate substantially all of our revenue from the sale of targeted advertising campaigns which we deliver via our network of websites and events. In all cases, we recognize revenue 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.

The majority of our online media sales involve multiple product offerings. Although each of our online media offerings can be sold separately, most of our online media sales involve multiple online offerings. Because objective evidence of fair value does not exist for all elements in our bundled product offerings, we use a best estimate of selling price of individual deliverables in the arrangement in the absence of vendor-specific objective evidence or other third-party evidence of fair value. We establish best estimates considering multiple factors including, but not limited to, class of client, size of transaction, available media inventory, pricing strategies and market conditions. We believe the use of the best estimate of selling price allows revenue recognition in a manner consistent with the underlying economics of the transaction. We apply a relative selling price method to allocate arrangement consideration at the inception of the arrangement to each deliverable in a multiple element arrangement. Revenue is then recognized as delivery occurs.

We evaluate all deliverables of an arrangement at inception and each time an item is delivered, to determine whether they represent separate units of accounting. Based on this evaluation, the arrangement consideration is measured and allocated to each of these elements.

Online Media. Lead generation campaigns all offer the Activity Intelligence Dashboard. For duration-based campaigns, revenue is recognized ratably over the duration of the campaigns, which is typically less than six months. Lead generation offerings may also include an additional service, TechTarget Re-Engage (formerly called Nurture & Qualify), in which case revenue is recognized ratably over the period of the campaign as a combined unit of accounting. As part of these offerings, we guarantee a minimum number of qualified leads to be delivered over the course of the advertising campaign. We determine the content necessary to achieve performance guarantees. Scheduled end dates of advertising campaigns sometimes need to be extended, pursuant to the terms of the arrangement, to satisfy lead guarantee obligations. We estimate a revenue reserve necessary to adjust revenue recognition for extended advertising campaigns. These estimates are based on our experience in managing and fulfilling these offerings. The customer has cancellation privileges which generally require advance notice by the customer and require proportional payment by the customer for the portion of the campaign period that has been provided. Additionally, we offer sales incentives to certain customers, primarily in the form of volume rebates, which are classified as a reduction of revenues and are calculated based on the terms of the specific customer s contract. We accrue for these sales incentives based on contractual terms and historical experience.

We recognize revenue from cost per lead advertising in the period during which the leads are delivered, which is typically less than six months.

Revenue for other significant online media offerings is recognized as follows:

IT Deal Alert. This suite of products includes Qualified Sales Opportunities and Account Watch. Qualified Sales Opportunities revenue is recognized when the opportunity is delivered to the customer; Account Watch revenue is recognized ratably over the duration of the service.

Custom Content Creation. Custom content revenue is recognized when the creation is completed and delivered to the customer, with the exception of microsites which are recognized over the period during which they are live.

Content Sponsorships. Content sponsorship revenue is recognized ratably over the period in which the related content vehicle is available on our websites.

List Rentals. List rental revenue is recognized in the period in which delivery of the list is made to our customers.

Banners. Banner revenue is recognized in the period in which the banner impressions, engagements or clicks occur.

Third Party Revenue Sharing Arrangements. Revenue from third-party revenue sharing arrangements is recognized on a net basis in the period in which the services are performed. For certain third-party agreements where we are the primary obligor, revenue is recognized on a gross basis in the period in which the services are performed.

Event Sponsorships. We recognize sponsorship revenue from events in the period in which the event occurs. The majority of our events are free to qualified attendees; however, certain events are based on a paid attendee model. We recognize revenue for paid attendee events upon completion of the event.

Amounts collected or billed prior to satisfying the above revenue recognition criteria are recorded as deferred revenue.

Long-Lived Assets

Our long-lived assets consist primarily of property and equipment, capitalized software, goodwill and other intangible assets. Goodwill and other intangible assets have arisen principally from our acquisitions. The amount assigned to intangible assets is subjective and based on our estimates of the future benefit of the intangible assets using accepted valuation techniques, such as discounted cash flow and replacement cost models. Our long-lived assets, other than goodwill, are amortized over their estimated useful lives, which we determine based on the consideration of several factors including the period of time the asset is expected to remain in service. Intangible assets are amortized over their estimated useful lives, which range from three to ten years, using methods of amortization that are expected to reflect the estimated pattern of economic use. Consistent with our determination that we have only one reporting segment, we have determined that there is only one reporting unit and test goodwill for impairment at the entity level. We evaluate the carrying value and remaining useful lives of long-lived assets, other than goodwill, whenever indicators of impairment are present. We evaluate the carrying value of goodwill annually using the two step process required by ASC 350, *Intangibles Goodwill and Other* (ASC 350). The first step of the impairment test is to identify potential impairment by comparing the reporting unit s fair value with its net book value (or carrying amount), including goodwill. The fair value is estimated based on a market value approach. If the fair value of the reporting unit exceeds its carrying amount, the reporting unit s goodwill is not considered to be impaired and the second step of the impairment test is not performed. Whenever indicators of impairment are present, we would perform the second step and compare the implied fair value of the reporting unit s goodwill, as defined by ASC 350, to its carrying value to determine the amount of the impairment loss, if any. As of December 31, 2013, the date of our last annual goodwill impairment review, there were no indications of impairment based on our step one analysis, and our estimated fair value exceeded our carrying value by a significant margin. There were no indications of impairment in our goodwill or intangible assets at September 30, 2014.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, short-term and long-term investments, accounts receivable, accounts payable and contingent consideration. Due to their short-term nature and liquidity, the carrying value of these instruments with the exception of contingent consideration approximates their estimated fair values. The fair value of contingent consideration was estimated using a discounted cash flow method.

Allowance for Doubtful Accounts

We offset gross trade accounts receivable with an allowance for doubtful accounts. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our existing accounts receivable. We review our allowance for doubtful accounts on a regular basis, and all past due balances are reviewed individually for collectability. Account balances are charged against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Provisions for doubtful accounts are recorded in general and administrative expense. If our historical collection experience does not reflect our future ability to collect outstanding accounts receivable, our future provision for doubtful accounts could be materially affected. To date, we have not incurred any write-offs of accounts receivable significantly different than the amounts reserved.

The allowance for doubtful accounts was $1.1 million at September 30, 2014 and $0.9 million at December 31, 2013.

Stock-Based Compensation

We measure stock-based compensation at the grant date based on the fair value of the award and recognize stock-based compensation in our results of operations using the straight-line method over the vesting period of the award or using the accelerated method if the award is contingent upon performance goals. We use the Black-Scholes option pricing model to determine the fair value of stock option awards.

Table of Contents

As there was no public market for our common stock prior to our initial public offering in May 2007 and, as until recently, there has been limited historical information on the volatility of our common stock since the date of our initial public offering, we historically determined the volatility for options granted based on an analysis of the historical volatility of our stock and reported data for a peer group of companies that issued options with substantially similar terms. Beginning in 2013, the expected volatility of options granted has been determined using a weighted average of the historical volatility of our stock for a period equal to the expected life of the option. The risk-free interest rate is based on a zero coupon United States treasury instrument whose term is consistent with the expected life of the stock options. We have not paid and do not anticipate paying cash dividends on our shares of common stock; therefore, the expected dividend yield is assumed to be zero.

Internal-Use Software and Website Development Costs

We capitalize costs of materials, consultants and compensation and related expenses of employees who devote time to the development of internal-use software and website applications and infrastructure involving developing software to operate our websites. However, we expense as incurred website development costs for new features and functionalities since it is not probable that they will result in additional functionality until they are both developed and tested with confirmation that they are more effective than the current set of features and functionalities on our websites. Our judgment is required in determining the point at which various projects enter the state at which costs may be capitalized, in assessing the ongoing value of the capitalized costs and in determining the estimated useful lives over which the costs are amortized, which is generally three years. To the extent that we change the manner in which we develop and test new features and functionalities related to our websites, assess the ongoing value of capitalized assets or determine the estimated useful lives over which the costs are amortized, the amount of website development costs we capitalize and amortize in future periods would be impacted. We review capitalized internal-use software and website development costs for recoverability whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. We would recognize an impairment loss only if the carrying amount of the asset is not recoverable and exceeds its fair value. We capitalized internal-use software and website development costs of $0.8 million and $0.9 million for the three months ended September 30, 2014 and 2013, respectively, and $2.5 million and $2.9 million for the nine months ended September 30, 2014 and 2013, respectively.

Income Taxes

We are subject to income taxes in both the United States and foreign jurisdictions, and we use estimates in determining our provision for income taxes. We recognize deferred tax assets and liabilities based on temporary differences between the financial reporting and income tax bases of assets and liabilities using statutory rates.

Our deferred tax assets are comprised primarily of book to tax differences on stock-based compensation, timing of deductions for deferred rent and accrued expenses, and net operating loss (NOL) carryforwards. As of December 31, 2013, we had state NOL carryforwards of approximately $25.9 million, which may be used to offset future taxable income. The NOL carryforwards expire through 2034. We also had foreign NOL carryforwards of $0.9 million, which may be used to offset future taxable income in foreign jurisdictions until they expire, through 2018.

Net Income (Loss) Per Share

We calculate basic earnings per share (EPS) by dividing earnings available to common shareholders for the period by the weighted average number of common shares and vested, undelivered restricted stock awards. Because the holders of unvested restricted stock awards do not have nonforfeitable rights to dividends or dividend equivalents, we do not consider these awards to be participating securities that should be included in our computation of earnings per share under the two-class method. Diluted EPS is computed using the weighted-average number of common shares and vested, undelivered restricted stock awards during the period, plus the dilutive effect of potential future issuances of common stock relating to stock option programs and other potentially dilutive securities using the treasury stock method. In calculating diluted EPS, the dilutive effect of stock options and restricted stock awards is computed using the average market price for the respective period. In addition, the assumed proceeds under the treasury stock method include the average unrecognized compensation expense and assumed tax benefit of stock options and restricted stock awards that are in-the-money. This results in the assumed buyback of additional shares, thereby reducing the dilutive impact of stock options.

Table of Contents

Results of Operations

The following table sets forth our results of operations for the periods indicated:

	Three Months Ended September 30, 2014		2013		Nine Months Ended September 30, 2014		2013	
	(unaudited) ($ in thousands)							
Revenues:								
Online	$ 24,218	92%	$ 18,830	85%	$ 69,950	93%	$ 57,676	89%
Events	2,214	8	3,281	15	5,607	7	7,081	11
Total revenues	26,432	100	22,111	100	75,557	100	64,757	100
Cost of revenues:								
Online	5,949	23	5,514	25	18,188	24	17,580	27
Events	805	3	1,221	5	2,331	3	2,984	5
Total cost of revenues	6,754	26	6,735	30	20,519	27	20,564	32
Gross profit	19,678	74	15,376	70	55,038	73	44,193	68
Operating expenses:								
Selling and marketing	10,964	41	8,773	40	30,717	41	26,986	42
Product development	1,854	7	1,680	8	5,201	7	5,097	8
General and administrative	3,628	14	3,722	17	10,864	14	10,307	16
Depreciation	1,024	4	961	4	3,025	4	2,818	4
Amortization of intangible assets	451	2	474	2	1,356	2	1,756	3
Total operating expenses	17,921	68	15,610	71	51,163	68	46,964	73
Operating income (loss)	1,757	7	(234)	(1)	3,875	5	(2,771)	(4)
Interest (expense) income, net	(18)	*	21	*	(39)	*	15	*
Other (expense) income, net	(212)	(1)	127	1	(82)	*	(240)	*
Income (loss) before provision for (benefit from) income taxes	1,527	6	(86)	*	3,754	5	(2,996)	(5)
Provision for (benefit from) income taxes	589	2	(663)	(3)	1,378	2	(1,160)	(2)
Net income (loss)	$ 938	4%	$ 577	3%	$ 2,376	3%	$ (1,836)	(3)%

* Not meaningful

Comparison of Three Months Ended September 30, 2014 and 2013

Revenues

	Three Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited) ($ in thousands)			
Revenues:				
Online	$ 24,218	$ 18,830	$ 5,388	29%
Events	2,214	3,281	(1,067)	(33)
Total revenues	$ 26,432	$ 22,111	$ 4,321	20%

Online. The increase in online revenue was primarily attributable to a $4.1 million increase in revenues from new product offerings, primarily IT Deal Alert, and international growth.

27

Table of Contents

Events. The decrease in events revenue is primarily due to a reduction in the number of conferences held during the period, primarily caused by a multi-day conference held in the third quarter of 2013 that will be held in the fourth quarter of 2014, offset in part by an increase in custom and seminar revenues.

Cost of Revenues and Gross Profit

	Three Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited)			
	($ in thousands)			
Cost of revenues:				
Online	$ 5,949	$ 5,514	$ 435	8%
Events	805	1,221	(416)	(34)
Total cost of revenues	$ 6,754	$ 6,735	$ 19	*%
Gross profit	$ 19,678	$ 15,376	$ 4,302	28%
Gross profit percentage	74%	70%		

Cost of Online Revenues. The increase in cost of online revenues was primarily due to costs related to new product offerings.

Cost of Events Revenues. The decrease in cost of events revenues was primarily related to a conference that was held in the third quarter of 2013 but will not be held until the fourth quarter of 2014.

Gross Profit. Our gross profit is equal to the difference between our revenues and our cost of revenues for the period. Gross profit for the third quarter of 2014 was 74% as compared to 70% in the third quarter of 2013. The increase in online gross profit was $5.0 million, primarily attributable to the increase in online revenue, offset in part by a decrease in events gross profit, primarily as a result of the conference that was moved to the fourth quarter. Because the majority of our costs are fixed, we expect our gross profit to fluctuate from period to period based on changes in the total revenues for the period. The relative contribution of online and events revenues to our total revenues will also cause fluctuation in our gross profit from period to period.

Operating Expenses and Other

	Three Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited)			
	($ in thousands)			
Operating expenses:				

Selling and marketing	$ 10,964	$ 8,773	$ 2,191	25%
Product development	1,854	1,680	174	10
General and administrative	3,628	3,722	(94)	(3)
Depreciation	1,024	961	63	7
Amortization of intangible assets	451	474	(23)	(5)
Total operating expenses	$ 17,921	$ 15,610	$ 2,311	15%
Interest (expense) income, net	$ (18)	$ 21	$ (39)	(186)%
Other (expense) income, net	$ (212)	$ 127	$ (339)	(267)%
Provision for (benefit from) income taxes	$ 589	$ (663)	$ 1,252	189%

Selling and Marketing. Selling and marketing expenses increased for the three months ended September 30, 2014 as compared to the three months ended September 30, 2013 due to increased investment in product innovation as well as variable compensation-related expenses caused by the increase in revenues and increased costs due to international expansion.

Product Development. The increase in product development expense was primarily caused by a reduction in the amount of these costs that were capitalized in the third quarter of 2014 as compared with the third quarter of 2013 as resources were allocated to non-capitalized projects based on company priorities.

Table of Contents

General and Administrative. The decrease in general and administrative expense for the three months ended September 30, 2014 compared with the same period in the prior year was primarily due to reductions in certain employee-related and corporate expenses and professional fees, offset in part by an increase in bad debt expense.

Depreciation and Amortization of Intangible Assets. Depreciation expense and amortization of intangible assets expense were both relatively flat quarter over quarter.

Interest Expense, Net. The increase in interest expense, net, is due to the amortization of a discount on installment payments related to the purchase of LeMagIT in the fourth quarter of 2012.

Other Income (Expense), Net. The change in other income (expense), net, related to fluctuations in foreign currency exchange rates.

Provision for Income Taxes. Our effective income tax rate was 38.6% and 812.8% for the three months ended September 30, 2014 and 2013, respectively. The lower rate in the three months ended September 30, 2014 as compared to the three months ended September 30, 2013 is primarily due to differences in the mix of pre-tax income and non-deductible stock-based compensation. The effective income tax rate is based upon the estimated annual effective tax rate in compliance with ASC 740, *Income Taxes*, and other related guidance. We update the estimate of our annual effective tax rate at the end of each quarterly period. Our estimate takes into account estimations of annual pre-tax income, the mix of pre-tax income and interpretations of tax laws. The third quarter of 2014 income tax rate was based on projections for the year.

Comparison of Nine Months Ended September 30, 2014 and 2013

Revenues

	Nine Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited)			
	($ in thousands)			
Revenues:				
Online	$ 69,950	$ 57,676	$ 12,274	21%
Events	5,607	7,081	(1,474)	(21)
Total revenues	$ 75,557	$ 64,757	$ 10,800	17%

Online. The increase in online revenue was primarily attributable to an $11.2 million increase in revenues from new product offerings, primarily IT Deal Alert, and international growth.

Events. The decrease in events revenue is primarily due to a reduction in the number of conferences held during the period, primarily caused by a multi-day conference held in the third quarter of 2013 that will be held in the fourth quarter of 2014, offset in part by an increase in seminars.

Cost of Revenues and Gross Profit

	Nine Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited)			
	($ in thousands)			
Cost of revenues:				
Online	$ 18,188	$ 17,580	$ 608	3%
Events	2,331	2,984	(653)	(22)
Total cost of revenues	$ 20,519	$ 20,564	$ (45)	*%
Gross profit	$ 55,038	$ 44,193	$ 10,845	25%
Gross profit percentage	73%	68%		

Cost of Online Revenues. The increase in cost of online revenues was primarily due to costs related to new product offerings.

Cost of Events Revenues. The decrease in cost of events revenues was primarily due to decreases in variable direct and employee-related costs related to a conference that was held in the third quarter of 2013 but will not be held until the fourth quarter of 2014.

Gross Profit. Our gross profit is equal to the difference between our revenues and our cost of revenues for the period. Gross profit for the first nine months of 2014 was 73% as compared to 68% in the first nine months of 2013. The increase in online gross profit was $11.7 million, primarily attributable to the increase in online revenue, offset in part by a decrease in events gross profit, primarily as a result of the conference that was moved to the fourth quarter. Because the majority of our costs are fixed, we expect our gross profit to fluctuate from period to period based on changes in the total revenues for the period. The relative contribution of online and events revenues to our total revenues will also cause fluctuation in our gross profit from period to period.

Operating Expenses and Other

	Nine Months Ended September 30,			
	2014	2013	Increase (Decrease)	Percent Change
	(Unaudited)			
	($ in thousands)			
Operating expenses:				
Selling and marketing	$ 30,717	$ 26,986	$ 3,731	14%
Product development	5,201	5,097	104	2
General and administrative	10,864	10,307	557	5
Depreciation	3,025	2,818	207	7
Amortization of intangible assets	1,356	1,756	(400)	(23)
Total operating expenses	$ 51,163	$ 46,964	$ 4,199	9%
Interest (expense) income, net	$ (39)	$ 15	$ (54)	(360)%
Other (expense), net	$ (82)	$ (240)	$ 158	66%
Provision for (benefit from) income taxes	$ 1,378	$ (1,160)	$ 2,538	(219)%

Selling and Marketing. Selling and marketing expenses increased year over year, primarily due to increased investment in product innovation as well as variable compensation-related expenses caused by the increase in revenues and increased costs due to international expansion.

Product Development. The increase in product development expense was primarily caused by a reduction in the amount of these costs that were capitalized year over year as some resources were allocated to non-capitalized projects due to company priorities, offset in part by a reduction in compensation and allocated costs due to reduced headcount year over year.

General and Administrative. The increase in general and administrative expense for the nine months ended September 30, 2014 compared to the same period in 2013 was primarily due to fees related to a secondary public offering in the second quarter of 2014.

Depreciation and Amortization of Intangible Assets. The increase in depreciation expense is related to an increase in our fixed asset base, primarily as a result of our continued investment in internal-use software development costs and computer equipment. The decrease in amortization of intangible assets expense was attributable to certain intangible assets becoming fully amortized during 2013.

Interest (Expense) Income, Net. The increase in interest expense, net, is due to the amortization of a discount on installment payments related to the purchase of LeMagIT in the fourth quarter of 2012.

Other Income (Expense), Net. The change in other income (expense), net, related to fluctuations in foreign currency exchange rates.

Provision for Income Taxes. Our effective income tax rate was 36.7% and 38.7% for the first nine months of 2014 and 2013, respectively. The lower rate in the nine months ended September 30, 2014 as compared to the nine months ended September 30, 2013 is primarily due to differences in the mix of pre-tax income and non-deductible stock-based compensation. The effective income tax rate is based upon the estimated annual effective tax rate in compliance with ASC 740, *Income Taxes*, and other related guidance. We update the estimate of our annual effective tax rate at the end of each quarterly period. Our estimate takes into account estimations of annual pre-tax income, the mix of pre-tax income and interpretations of tax laws. The income tax rate for the first nine months of 2014 was based on projections for the year.

Table of Contents

Seasonality

The timing of our revenues is affected by seasonal factors. Our revenues are seasonal primarily as a result of the annual budget approval process of many of our customers, the normal timing at which our customers have their new product introductions, and the historical decrease in advertising and events activity in summer months. Events revenue may vary depending on which quarters we produce the event, which may vary when compared to previous periods. The timing of revenues in relation to our expenses, much of which does not vary directly with revenue, has an impact on the cost of online revenues, selling and marketing, product development, and general and administrative expenses as a percentage of revenue in each calendar quarter during the year.

The majority of our expenses are personnel-related and include salaries, stock-based compensation, benefits and incentive-based compensation plan expenses. As a result, we have not experienced significant seasonal fluctuations in the timing of our expenses period to period.

Liquidity and Capital Resources

Resources

At September 30, 2014, we had $45.8 million of working capital, and our cash and cash equivalents totaled $25.8 million. Our cash, cash equivalents and investments increased $8.6 million during the first nine months of fiscal 2014, primarily from cash generated by our operations and financing activities, primarily from option exercises, offset by the repurchase of shares and our investing activity, primarily from purchases of property and equipment. We believe that our existing cash, cash equivalents, and investments, our cash flow from operating activities and available bank borrowings will be sufficient to meet our anticipated cash needs for at least the next 12 months. Our future working capital requirements will depend on many factors, including the operations of our existing business, our potential strategic expansion internationally, future acquisitions we might undertake, and the expansion into complementary businesses. To the extent that our cash and cash equivalents, investments and cash flow from operating activities are insufficient to fund our future activities, we may need to raise additional funds through bank credit arrangements or public or private equity or debt financings. We also may need to raise additional funds in the event we determine in the future to effect one or more additional acquisitions of businesses.

	September 30, 2014 (Unaudited)	December 31, 2013
	($ in thousands)	
Cash, cash equivalents and investments	$ 42,390	$ 33,772
Accounts receivable, net	$ 23,481	$ 22,116

Cash, Cash Equivalents and Investments

Our cash, cash equivalents and investments at September 30, 2014 were held for working capital purposes and were invested primarily in money market accounts, municipal bonds and government agency bonds. We do not enter into investments for trading or speculative purposes.

Accounts Receivable, Net

Our accounts receivable balance fluctuates from period to period, which affects our cash flow from operating activities. The fluctuations vary depending on the timing of our service delivery and billing activity, cash collections, and changes to our allowance for doubtful accounts. We use days sales outstanding, (DSO), as a measurement of the quality and status of our receivables. We define DSO as net accounts receivable at period end divided by total revenue for the applicable period, multiplied by the number of days in the applicable period. DSO was 82 days for the quarter ended September 30, 2014 and 86 days at December 31, 2013. The decrease in DSO is primarily due to the timing of payments from customers and mix of customers and products.

Table of Contents

Cash Flows

	Nine Months Ended September 30,	
	2014	2013
	(Unaudited) ($ in thousands)	
Net cash provided by operating activities	$ 12,902	$ 6,768
Net cash used in investing activities(1)	$ (3,017)	$ (3,609)
Net cash used in financing activities	$ (964)	$ (10,876)

(1) Cash used in investing activities is shown net of investment activity of $1.5 million and ($11.4) million for the nine months ended September 30, 2014 and 2013, respectively.

Operating Activities

Cash provided by operating activities primarily consists of net income (loss) adjusted for certain non-cash items including depreciation and amortization, the provision for bad debt, stock-based compensation, deferred income taxes, and the effect of changes in working capital and other activities. Cash provided by operating activities for the first nine months of 2014 was $12.9 million compared to cash provided by operating activities of $6.8 million in the comparable period in 2013. The increase in cash provided by operating activities was primarily a result of changes in operating assets and liabilities of $(0.7) million in the first nine months of 2014 compared to $(2.0) million in the first nine months of 2013. Significant components of the changes in assets and liabilities included an increase in prepaids and other current assets of $1.6 million in 2014 compared to an increase of $3.7 million in 2013, primarily caused by increases in tax-related receivables in the first nine months of 2013, a decrease in other liabilities of $0.1 million in 2014 compared to a decrease of $1.6 million in 2013, and an increase in income taxes payable of $2.1 million during the first nine months of 2014 compared to a decrease of $0.7 million in the first nine months of 2013, offset in part by a decrease of $0.2 million in accrued expenses during the first nine months of 2014 compared to an increase of $1.8 million in the first nine months of 2013, and an increase in deferred revenue of $3.0 in 2014 compared to an increase of $4.5 million in 2013. The increase in cash provided by operating activities is also a result of a change in net income of $2.4 million during the first nine months of 2014 compared to a $1.8 million net loss during the first nine months of 2013.

Investing Activities

Cash used in investing activities in the nine months ended September 30, 2014, net of investment activity, was $3.0 million for the purchase of property and equipment made up primarily of website development costs, computer equipment and related software and internal-use development costs.

Equity Financing Activities

We received proceeds from the exercise of stock options in the amounts of $2.2 million and $1.0 million in the nine months ended September 30, 2014 and 2013, respectively.

On August 4, 2014, our Board of Directors authorized a $20 million stock repurchase program (the 2014 Program). Under the 2014 Program, we are authorized to repurchase our common stock from time to time on the open market or in privately negotiated transactions. The timing and amount of any shares repurchased will be determined based on an evaluation of market conditions and other factors. We may elect to implement a Rule 10b5-1 trading plan to make such purchases, which would permit shares to be repurchased when we might otherwise be precluded from doing so under insider trading laws. The 2014 Program may be suspended or discontinued at any time. The 2014 Program is funded with cash on hand.

On August 3, 2012, our Board of Directors authorized a $20 million stock repurchase program (the 2012 Program). We were authorized to repurchase our common stock from time to time on the open market or in privately negotiated transactions. The timing and amount of any shares of common stock repurchased was determined based on an evaluation of market conditions and other factors. We elected to implement a Rule 10b5-1 trading plan to make such purchases, which permits shares of common stock to be repurchased when we might otherwise be precluded from doing so under insider trading laws. The 2012 Program was terminated immediately prior to the commencement of a tender offer on September 25, 2013.

During the three months ended September 30, 2014 we repurchased 311,522 shares of common stock for approximately $2.7 million pursuant to the 2014 Program. During the nine months ended September 30, 2013 we repurchased 2,610,279 shares of common stock for approximately $12.4 million pursuant to the 2012 Program. All repurchased shares were funded with cash on hand.

Tender Offer

On September 25, 2013, we commenced a tender offer to purchase up to 6.5 million shares of our common stock at a price of $5.00 per share. The tender offer expired on October 24, 2013. In accordance with applicable SEC regulations and the terms of the tender offer, we exercised the right to purchase additional shares of common stock and accepted for purchase 7,100,565 shares of our common stock for a total cost of $35.6 million, which includes approximately $0.1 million in fees and expenses. Pursuant to the terms of the tender offer, we purchased 2,250,000 shares of common stock from entities affiliated with Technology Crossover Ventures and 2,300,040 shares of common stock from entities affiliated with Polaris Venture Partners.

Secondary Offering

In May 2014, we completed a secondary public offering of 5,750,000 shares of common stock at a price of $6.25 per share. All of the shares sold in the secondary public offering were sold by selling stockholders and we did not receive any proceeds from the offering. We incurred fees of approximately $0.5 million related to legal, accounting, and other fees in connection with the secondary public offering, which is included in general and administrative expenses in the Statement of Operations and Comprehensive Income (Loss).

Term Loan and Credit Facility Borrowings

In August 2006, we entered into a credit agreement (the Credit Agreement) with a commercial bank, which included a $10.0 million term loan (the Term Loan) and a $20.0 million revolving credit facility (the Revolving Credit Facility). The Credit Agreement was amended in August 2007, in December 2008, in December 2009 and again in August 2011. The amendment in 2009 reduced the Revolving Credit Facility to $5.0 million. We paid off the remaining balance of the Term Loan in December 2009. The amendment in August 2011 extended the term of the facility and adjusted certain other financial terms and covenants.

The Revolving Credit Facility matures on August 31, 2016. Unless earlier payment is required by an event of default, all principal and unpaid interest will be due and payable on August 31, 2016. At our option, the Revolving Credit Facility bears interest at either the prime rate less 1.00% or the London Interbank Offered Rate (LIBOR) plus the applicable LIBOR margin. The applicable LIBOR margin is based on the ratio of total funded debt to EBITDA for the preceding four fiscal quarters. As of September 30, 2014, the applicable LIBOR margin was 1.25%.

We are also required to pay an unused line fee on the daily unused amount of our Revolving Credit Facility at a per annum rate based on the ratio of total funded debt to EBITDA for the preceding four fiscal quarters. As of September 30, 2014, unused availability under the Revolving Credit Facility totaled $4.0 million and the per annum unused line fee rate was 0.20%.

As of September 30, 2014 and December 31, 2013 there were no amounts outstanding under the revolving loan portion of our Revolving Credit Facility. There was a $1.0 million standby letter of credit (Letter of Credit) related to our corporate headquarters lease that was outstanding at September 30, 2014, bringing our available borrowings on the $5.0 million facility to $4.0 million. In the third quarter of 2014, we paid $0.7 million in cash as a security deposit on our corporate headquarters lease. The Letter of Credit, which was also being held against the lease, was cancelled in October 2014.

Borrowings under the Credit Agreement are collateralized by a security interest in substantially all of our assets. Covenants governing the Credit Agreement include the maintenance of certain financial ratios. As of September 30, 2014, we were in compliance with all covenants under the Credit Agreement.

Capital Expenditures

We have made capital expenditures primarily for computer equipment and related software needed to host our websites, internal-use software development costs, as well as for leasehold improvements and other general purposes to support our growth. Our capital expenditures totaled $3.0 million and $3.6 million for the nine month periods ended September 30, 2014 and 2013. A majority of our capital expenditures in the first nine months of 2014 were internal-use development costs and, to a lesser extent, computer equipment and related software. We are not currently party to any purchase contracts related to future capital expenditures.

Table of Contents

Contractual Obligations and Commitments

As of September 30, 2014, our principal commitments consist of obligations under leases for office space. The offices are leased under non-cancelable operating lease agreements that expire through 2020. The following table sets forth our commitments to settle contractual obligations in cash as of September 30, 2014:

	Payments Due By Period				
	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	More than 5 Years
			(Unaudited)		
			($ in thousands)		
Operating leases	$ 21,113	$ 4,121	$ 7,829	$ 7,660	$ 1,503

At September 30, 2014, we had a Letter of Credit outstanding in the aggregate amount of $1.0 million. In the third quarter of 2014, we paid $0.7 million in cash as a security deposit on our corporate headquarters lease. The Letter of Credit, which was also being held against the lease, was cancelled in October 2014.

See Note 5 to the Consolidated Financial Statements for information regarding future payments related to the LeMagIT acquisition.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Recent Accounting Pronouncements

See Note 2 to the Consolidated Financial Statements for recent accounting pronouncements that could have an effect on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in foreign exchange rates and interest rates. We do not hold or issue financial instruments for trading purposes.

Foreign Currency Exchange Risk

We currently have subsidiaries in London, England; Hong Kong; Australia; Singapore; Munich, Germany and Paris, France. Additionally, we have a wholly foreign-owned enterprise formed under the laws of the People s Republic of China, and a VIE in Beijing, PRC. Approximately 21% of our revenues for the quarter ended September 30, 2014 were derived from customers with billing addresses outside of the United States and our foreign exchange gains/losses were not significant. We currently believe our exposure to foreign currency exchange rate fluctuations is financially immaterial and therefore have not entered into foreign currency hedging transactions. We continue to review this issue and may consider hedging certain foreign exchange risks through the use of currency futures or options in the future.

Interest Rate Risk

At September 30, 2014, we had cash, cash equivalents and investments totaling $42.4 million. These amounts were invested primarily in money market accounts, municipal bonds and government agency bonds. The cash, cash equivalents and investments were held for working capital purposes. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of these investments, we believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. Declines in interest rates, however, would reduce future investment income.

Our exposure to market risk also relates to the amount of interest expense we must pay under our revolving credit facility. The advances under this credit facility bear a variable rate of interest determined as a function of the lender s prime rate or LIBOR. At September 30, 2014, there were no amounts outstanding under our revolving credit facility.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Company is required to maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in its reports under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and that such information is accumulated and communicated to management, including the Company s Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer) as appropriate, to allow timely decisions regarding required disclosure.

As of September 30, 2014, management, under the supervision of the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes to our internal control over financial reporting that occurred during the quarter ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

We are not currently a party to any material legal proceedings and we are not aware of any pending or threatened litigation against us that could have a material adverse effect on our business, operating results or financial condition. On January 6, 2012, the Company filed Petitions under Formal Procedure with the Massachusetts Appellate Tax Board in connection with the classification of the Company s wholly-owned subsidiary, TechTarget Securities Corporation, and assessments made by the Massachusetts Department of Revenue, as described in Note 9 in the accompanying consolidated financial statements. A trial took place on April 29, 2014; no decision has been rendered as of the date of this report.

Item 1A. Risk Factors

The following discussion highlights certain risks that may affect future operating results and share price. These are the risks and uncertainties we believe are most important for our existing and potential stockholders to consider. Additional risks and uncertainties not presently known to us, which we currently deem immaterial or which are similar to those faced by other companies in our industry or business in general, may also impair our business operations. If any of the following risks or uncertainties actually occurs, our business, financial condition and operating results would likely suffer.

Risks Relating to Our Business

Because we depend on our ability to generate revenues from the sale of advertising campaigns, fluctuations in advertising spending could have an adverse effect on our operating results.

The primary source of our revenues is the sale of advertising campaigns to our customers. Our advertising revenues accounted for substantially all of our total revenues for the three months ended September 30, 2014. We believe that advertising spending on the Internet, as in traditional media, fluctuates significantly as a result of a variety of factors, many of which are outside of our control. These factors include:

- variations in expenditures by advertisers due to budgetary constraints;
- the cancellation or delay of projects by advertisers;
- the cyclical and discretionary nature of advertising spending;
- general economic conditions, as well as economic conditions specific to the Internet and online and offline media industry; and
- the occurrence of extraordinary events, such as natural disasters and international or domestic political and economic unrest.

Table of Contents

Because all of our customers are in the IT industry, our revenues are subject to characteristics of the IT industry that can affect advertising spending by IT vendors.

The IT industry is characterized by, among other things, volatile quarterly results, uneven sales patterns, short product life cycles, rapid technological developments and frequent new product introductions and enhancements. As a result, our customers advertising budgets, which are often viewed as discretionary expenditures, may increase or decrease significantly over a short period of time. In addition, the advertising budgets of our customers may fluctuate as a result of:

- weakness in corporate IT spending, resulting in a decline in IT advertising spending, a continued trend that we have seen and that may continue;

- increased concentration in the IT industry as a result of consolidations, leading to a decrease in the number of current and prospective customers, as well as an overall reduction in advertising;

- reduced spending by combined entities following such consolidations;

- the timing of advertising campaigns around new product introductions and initiatives; and

- economic conditions specific to the IT industry.

Our future growth will depend in large part on continued increased sales of our IT Deal Alert product suite.

In 2013, we began selling a new suite of products called IT Deal Alert, which is based on our Activity Intelligence analytics. The IT Deal Alert product suite currently consists of Qualified Sales Opportunities and, as announced in March 2014, Account Watch. Our increase in revenues in the first nine months of 2014, compared to the comparable period of 2013, was, in part, attributable to sales of IT Deal Alert products. We expect that IT Deal Alert, as well as the expansion of our IT Deal Alert product offerings, will be major components of our future growth. The failure of our IT Deal Alert products to meet anticipated sales levels, our inability to continue to expand successfully our IT Deal Alert product suite, or the failure of our current or new IT Deal Alert Products to achieve and then maintain widespread customer acceptance would likely have a material adverse effect on our business and financial results. In addition, competitors may develop a service or application that is similar to our IT Deal Alert product suite, which may also result in reduced sales levels for our product offerings.

There are a number of risks associated with expansion of our business internationally that could adversely affect our business.

Approximately 21% of our revenues for the three months ended September 30, 2014 were derived from customers with billing addresses outside of the United States and approximately 29% of our revenues were derived from geo-targeted campaigns, where our target audience is outside North America. We have license and other arrangements in various countries, and maintain direct presences in the United Kingdom, France, Singapore and Australia, as well as operations in China, and Spanish, French, Portuguese and German language websites.

In addition to facing many of the same challenges we face domestically, there are additional risks and costs inherent in expanding our business in international markets, including:

- limitations on our activities in foreign countries where we have granted rights to existing business partners;
- continuation of the trend among our foreign-based customers to transition from print to online advertising;
- the adaptation of our websites and advertising programs to meet local needs and to comply with local legal and regulatory requirements;
- our foreign-based competitors having greater resources and longer established relationships with local advertisers;
- varied, unfamiliar and unclear legal and regulatory restrictions, as well as unforeseen changes in legal and regulatory requirements;
- more restrictive data protection regulation, which may vary by country;
- more extensive labor regulation, which may vary by country;
- difficulties in staffing and managing multinational operations;
- difficulties in finding appropriate foreign licensees or joint venture partners;
- distance, language and cultural differences in doing business with foreign entities;
- foreign political and economic uncertainty;
- less extensive adoption of the Internet as an information source and increased restriction on the content of websites;
- currency exchange-rate fluctuations; and
- potential adverse tax requirements.

36

Table of Contents

As a result, we may face difficulties and unforeseen expenses in expanding our business internationally and, even if we attempt to do so, we may be unsuccessful, which could harm our business, operating results and financial condition.

There are substantial uncertainties regarding the interpretation and application of the laws and regulations of the People s Republic of China, or PRC, including, but not limited to, the laws and regulations governing our business in the PRC, and the enforcement and performance of the contractual arrangements between our wholly-owned subsidiary, TechTarget (Beijing) Information Technology Consulting Co., Ltd, or TTGT China, and our affiliated Chinese entity, Keji Wangtuo (Beijing) Information Technology Co., Ltd, or Keji Wangtuo, and its shareholders. We are considered a foreign person under PRC law. As a result, we are subject to PRC law limitations on foreign ownership of companies engaged in value-added telecommunications services, including internet-related services, and advertising. Accordingly, we operate our websites and our online advertising business in China through Keji Wangtuo, a company wholly-owned by two citizens of the PRC; we have no equity ownership interest in Keji Wangtuo. Keji Wangtuo holds the licenses and approvals necessary to operate our websites and online advertising business in China. Through our wholly-owned subsidiary, TTGT China, we have contractual arrangements with Keji Wangtuo and its shareholders that allow us to substantially control and operate Keji Wangtuo and give us the economic benefit of those operations. We cannot be sure that we will be able to enforce these contracts. In addition, such contractual arrangements may not prove as effective in exercising control over Keji Wangtuo as direct ownership. Although we believe we are in compliance with current PRC regulations, we cannot be sure that the Chinese government would agree that our operating and equity arrangements with Keji Wangtuo comply with Chinese law. If the Chinese government determines that we are not in compliance with applicable law, it could revoke our business and operating licenses, require us to discontinue or restrict our operations, restrict our right to collect revenues, block our websites in China, require us to restructure our Chinese operations, impose additional conditions or requirements with which we may not be able to comply, impose restrictions on our business operations or on our customers, or take other regulatory or enforcement actions against us that could be harmful to our business in China.

The general economic, business or industry conditions may adversely affect our business, as well as our ability to forecast financial results.

The domestic and international economies have continued to experience ongoing instability and inconsistent, unpredictable growth. This period of instability has been magnified by factors including changes in the availability of credit, volatile business and consumer confidence and fluctuating unemployment. These and other macro-economic conditions have contributed to unpredictable changes in the global economy and expectations of future global economic growth. If the economic climate in the United States and abroad remains as it is or deteriorates, our customers or potential customers could reduce or delay their purchases of our offerings, which would adversely impact our revenues and our ability to sell our offerings, collect customer receivables and, ultimately, our profitability. Additionally, future economic conditions continue to have a high degree of inherent uncertainty. As a result, it continues to be difficult to estimate the level of growth or contraction for the economy as a whole, as well as for the various sectors of the economy, such as the IT market. Because all components of our budgeting and forecasting are dependent upon estimates of growth or contraction in the IT market and demand for our offerings, the prevailing economic uncertainties continue to render accurate estimates of future income and expenditures very difficult to make. We cannot predict the duration of current economic conditions or the duration or strength of an economic recovery, worldwide in the IT industry or in any of the different segments of the IT industry. Further adverse changes may occur as a result of global, domestic or regional economic conditions, changing consumer confidence, unemployment, declines in stock markets, or other factors affecting economic conditions generally. These changes may negatively affect the sales of our offerings, increase exposure to losses from bad debts, increase the cost and decrease the availability of financing, or increase the risk of loss on investments. Any recent growth we have experienced internationally would be negatively affected by any future global downturn.

Lingering effects of financial market instability and continued uncertain conditions in the United States and global economies have in the past and could in the future adversely affect our revenues and operating results.

We believe that the lingering effects of the instability affecting the financial markets and any further deterioration in the current business climate within the United States and/or certain other geographic regions in which we do business have had, and could continue to have, a negative impact on our revenue growth and operating results. Because all of our clients are in the IT industry, the success of our business is intrinsically linked to the health, and subject to market conditions, of the IT industry, and regional, domestic and global economic conditions. In turn, many of our customers have reassessed and will, for the foreseeable future, be likely to continue to scrutinize their spending on advertising campaigns. Prior market downturns in the IT industry have resulted in declines in advertising spending, which can cause longer sales cycles, deferral or delay of purchases by IT vendors and generally reduced expenditures for advertising and related services. Our revenues and profitability depend on the overall demand for advertising services from our customers. We believe that demand for our offerings has been in the past, and could be in the future, disproportionately affected by fluctuations, disruptions, instability or downturns in the economy and the IT industry, which may cause customers and potential customers to exit the industry or delay, cancel or reduce any planned expenditures for our advertising offerings. Furthermore, competitors have and may continue to respond to market conditions by lowering prices and attempting to lure away our customers and prospects to lower cost offerings. In addition, any slowdown in the formation of new IT companies, or decline in the growth of existing IT companies, may cause a decline in demand for our offerings.

Our quarterly operating results are subject to fluctuations, and these fluctuations may adversely affect the trading price of our common stock.

We have experienced fluctuations in our quarterly revenues and operating results. Our quarterly revenues and operating results may fluctuate from quarter to quarter due to a number of factors, many of which are outside of our control. In addition to the factors described elsewhere in this Risk Factors section, these factors include:

- the spending priorities and advertising budget cycles of specific advertisers;
- the addition or loss of advertisers;
- the addition of new sites and services by us or our competitors; and
- seasonal fluctuations in advertising spending, based on product launch schedules, annual budget approval processes for our customers and the historical decrease in advertising and events activity in the summer months.

Due to such risks, you should not rely on quarter-to-quarter comparisons of our results of operations as an indicator of our future results. Due to the foregoing factors, it is also possible that our results of operations in one or more quarters may fall below the expectations of investors and/or securities analysts. In such an event, the trading price of our common stock is likely to decline.

Our revenues are primarily derived from short-term contracts that may not be renewed.

The primary source of our revenues is the sale of advertising to our customers, and we expect that this will continue to be the case for the foreseeable future. Our advertising contracts are primarily short-term, typically six months or less, and are generally subject to termination without substantial penalty by the customer at any time, generally with minimal notice requirements. We cannot assure you that our current customers will fulfill their obligations under their existing contracts, continue to participate in our existing programs beyond the terms of their existing contracts or enter into any additional contracts for new programs that we offer. In addition, our efforts to enter into longer term arrangements with customers for our IT Deal Alert services may not be successful. If a significant number of advertisers or a few large advertisers decided not to continue advertising on our websites or conducting or sponsoring events, we could experience a rapid decline in our revenues over a relatively short period of time.

If we are unable to deliver content and services that attract and retain users, our ability to attract advertisers may be affected, which could in turn have an adverse effect on our revenues.

Our future success depends on our continued ability to deliver original and compelling content and services to attract and retain users. Our user base is composed of corporate IT professionals who demand specialized websites and events tailored to the sectors of the IT products for which they are responsible and that they purchase. Our content and services may not be attractive to a sufficient number of users to attract advertisers and generate revenues consistent with our estimates. We also may not develop new content or services in a timely or cost-effective manner. Our ability to develop and produce this specialized content successfully is subject to numerous uncertainties, including our ability to:

- anticipate and respond successfully to rapidly changing IT developments and preferences to ensure that our content remains timely and interesting to our users;
- attract and retain qualified editors, writers and technical personnel;
- fund new development for our programs and other offerings;
- successfully expand our content offerings into new platform and delivery mechanisms; and
- promote and strengthen the brands of our websites and our name.

If we are not successful in maintaining and growing our user base, our ability to retain and attract advertisers may be affected, which could in turn have an adverse effect on our revenues.

Table of Contents

Our inability to sustain our historical advertising rates could adversely affect our operating results.

The market for advertising has fluctuated over the past few years. If we are unable to maintain historical pricing levels for advertising on our websites and for sponsorships at our events, our revenues could be adversely affected.

Competition for advertisers is intense, and we may not compete successfully, which could result in a material reduction in our market share, the number of our advertisers and our revenues.

We compete for potential advertisers with a number of different types of offerings and companies, including: broad-based media outlets, such as television, newspapers and business periodicals that are designed to reach a wide audience; general purpose portals and search engines; and offline and online offerings of media companies that produce content specifically for IT professionals, including International Data Group, United Business Media, QuinStreet and CNet. Advertisers may choose our competitors over us not only because they prefer our competitors online and events offerings to ours but also because advertisers prefer to utilize other forms of advertising offered by our competitors that are not offered by us and/or to diversify their advertising expenditures. Many of our current and potential competitors have longer operating histories, larger customer bases, greater brand recognition and significantly greater financial, marketing and other resources than we have. As a result, we could lose market share to our competitors in one or more of our businesses and our revenues could decline.

We depend upon Internet search engines to attract a significant portion of the users who visit our websites, and if we were listed less prominently in search result listings, our business and operating results would be harmed.

We derive a significant portion of our website traffic from users who search for IT purchasing content through Internet search engines, such as Google, MSN, Bing and Yahoo!. A critical factor in attracting users to our websites is whether we are prominently displayed in response to an Internet search relating to IT content. Search result listings are determined and displayed in accordance with a set of formulas or algorithms developed by the particular Internet search engine. The algorithms determine the order of the listing of results in response to the user s Internet search. From time to time, search engines revise their algorithms. In some instances, these modifications may cause our websites to be listed less prominently in unpaid search results, which will result in decreased traffic from search engine users to our websites. Our websites may also become listed less prominently in unpaid search results for other reasons, such as search engine technical difficulties, search engine technical changes and changes we make to our websites. In addition, search engines have deemed the practices of some companies to be inconsistent with search engine guidelines and have decided not to list their websites in search result listings at all. If we are listed less prominently or not at all in search result listings for any reason, traffic to our websites will likely decline, which could harm our operating results. If we decide to attempt to replace this traffic, we may be required to increase our marketing expenditures, which also could harm our operating results.

We may not innovate at a successful pace, which could harm our operating results.

Our industry is rapidly adopting new technologies and standards to create and satisfy the demands of users and advertisers. It is critical that we continue to innovate by anticipating and adapting to these changes to ensure that our content-delivery, lead generation and IT Deal Alert products platforms and services remain effective and interesting to our users, advertisers and partners. In addition, we may discover that we must make significant expenditures to achieve these goals. If we fail to accomplish these goals, we may lose users and the advertisers that seek to reach those users, which could harm our operating results. Existing and planned efforts to develop new products, including any subscription-based offerings, may be costly and ultimately not successful.

We may be unable to continue to build awareness of our brands, which could negatively impact our business and cause our revenues to decline.

Building and maintaining recognition of our brands is critical to attracting and expanding our online user base and attendance at our events. We intend to continue to build existing brands and introduce new brands that will resonate with our targeted audiences, but we may not be successful. In order to promote these brands, in response to competitive pressures or otherwise, we may find it necessary to increase our marketing budget, hire additional marketing and public relations personnel or otherwise increase our financial commitment to creating and maintaining brand loyalty among our clients. If we fail to promote and maintain our brands effectively, or incur excessive expenses attempting to promote and maintain our brands, our business and financial results may suffer.

If we do not retain our key personnel, our ability to execute our business strategy will be adversely affected.

Our continued success depends to a significant extent upon the recruitment, retention and effective succession of our executive officers and key management. Our management team has significant industry experience and would be difficult to replace. These individuals possess sales, marketing, financial and administrative skills that are critical to the operation of our business. The competition for these employees is intense. The loss of the services of one or more of our key personnel could have a material adverse effect on our operating results.

We may not be able to attract, hire and retain qualified personnel cost-effectively, which could impact the quality of our content and services and the effectiveness and efficiency of our management, resulting in increased costs and losses in revenues.

Our success depends on our ability to attract, hire and retain qualified technical, editorial, sales and marketing, customer support, financial and accounting and other managerial personnel at commercially reasonable rates. The competition for personnel in the industries in which we operate is intense. Our personnel may terminate their employment at any time for any reason. Loss of personnel may also result in increased costs for replacement hiring and training. If we fail to attract and hire new personnel or retain and motivate our current personnel, we may not be able to operate our businesses effectively or efficiently, serve our customers properly or maintain the quality of our content and services. In particular, our success depends in significant part on maintaining and growing an effective sales force. This dependence involves a number of challenges, including:

- the need to hire, integrate, motivate and retain additional sales and sales support personnel;
- the need to train new sales personnel, many of whom lack sales experience when they are hired; and
- competition from other companies in hiring and retaining sales personnel.

We may fail to identify or successfully acquire and integrate businesses, products and technologies that would otherwise enhance our service offerings to our customers and users, and as a result our revenues may decline or fail to grow.

We have acquired, and in the future may acquire or invest in, complementary businesses, products or technologies. Acquisitions and investments involve numerous risks including:

- difficulty in assimilating the operations and personnel of acquired businesses;
- potential disruption of our ongoing businesses and distraction of our management and the management of acquired companies;
- difficulty in incorporating acquired technology and rights into our offerings and services;

unanticipated expenses related to technology and other integration;

potential failure to achieve additional sales and enhance our customer bases through cross marketing of the combined company s services to new and existing customers;

potential detrimental impact to our pricing based on the historical pricing of any acquired business with common clients and the market generally;

potential litigation resulting from our business combinations or acquisition activities; and

potential unknown liabilities associated with the acquired businesses.

Our inability to integrate any acquired business successfully, or the failure to achieve any expected synergies, could result in increased expenses and a reduction in expected revenues or revenue growth. As a result, our stock price could fluctuate or decline. In addition, we cannot assure you that we will be successful in expanding into complementary sectors in the future, which could harm our business, operating results and financial condition.

The costs associated with potential acquisitions or strategic partnerships could dilute your investment or adversely affect our results of operations.

In order to finance acquisitions, investments or strategic partnerships, we may use equity securities, debt, cash, or a combination of the foregoing. Any issuance of equity securities or securities convertible into equity may result in substantial dilution to our existing stockholders, reduce the market price of our common stock, or both. Any debt financing is likely to have financial and other covenants that could have an adverse impact on our business if we do not achieve our projected results. In addition, the related increases in expenses could adversely affect our results of operations.

Table of Contents

We have limited protection of our intellectual property and could be subject to infringement claims that may result in costly litigation, the payment of damages or the need to revise the way we conduct our business.

Our success and ability to compete are dependent in part on the strength of our proprietary rights, on the goodwill associated with our trademarks, trade names and service marks, and on our ability to use United States and foreign laws to protect them. Our intellectual property includes, among other things, our original content, our editorial features, logos, brands, domain names, the technology that we use to deliver our services, the various databases of information that we maintain and make available by license, and the appearances of our websites. We claim common law protection on certain names and marks that we have used in connection with our business activities. Although we have applied for and obtained registration of some of our marks in countries outside of the United States where we do business, we have not been able to obtain registration of all of our key marks in such jurisdictions, in some cases due to prior registration or use by third parties employing similar marks. In addition to United States and foreign laws, we rely on confidentiality agreements with our employees and third parties and protective contractual provisions to safeguard our intellectual property. Policing our intellectual property rights worldwide is a difficult task, and we may not be able to identify infringing users, or, if identified, stop them from continuing to infringe our intellectual property. We cannot be certain that third-party licensees of our content will always take actions to protect the value of our proprietary rights and reputation. Intellectual property laws and our agreements may not be sufficient to prevent others from copying or otherwise obtaining and using our content or technologies. In addition, others may develop non-infringing technologies that are similar or superior to ours. In seeking to protect our marks, copyrights, domain names and other proprietary rights, or in defending ourselves against claims of infringement that may be with or without merit, we could face costly litigation and the diversion of our management s attention and resources. These claims could result in the need to develop alternative trademarks, content or technology or to enter into costly royalty or licensing agreements, which could have a material adverse effect on our business, results of operations and financial condition. We may not have, in all cases, conducted formal evaluations to confirm that our technology and services do not or will not infringe upon the intellectual property rights of third parties. As a result, we cannot be certain that our technology, offerings, services or online content do not or will not infringe upon the intellectual property rights of third parties. If we were found to have infringed on a third-party s intellectual property rights, the value of our brands and our business reputation could be impaired, and our business could suffer.

Our business could be harmed if we are unable to correspond with existing and potential users by e-mail.

We use e-mail as a significant means of communicating with our existing users. The laws and regulations governing the use of e-mail for marketing purposes continue to evolve, and the growth and development of the market for commerce over the Internet may lead to the adoption of additional legislation and/or changes to existing laws. If new laws or regulations are adopted, or existing laws and regulations are interpreted and/or amended or modified to impose additional restrictions on our ability to send e-mail to our users or potential users, we may not be able to communicate with them in a cost-effective manner. In addition to legal restrictions on the use of e-mail, Internet service providers and others typically attempt to block the transmission of unsolicited e-mail, commonly known as spam. If an Internet service provider or software program identifies e-mail from us as spam, we could be placed on a restricted list that would block our e-mail to users or potential users who maintain e-mail accounts with these Internet service providers or who use these software programs. If we are unable to communicate by e-mail with our users and potential users as a result of legislation, blockage or otherwise, our business, operating results and financial condition could be harmed.

Changes in laws and standards relating to data collection and use, and the privacy of Internet users and other data could impair our efforts to maintain and grow our audience and thereby decrease our advertising revenue.

We collect information from our users who register on our websites or for services or respond to surveys. Subject to each user s permission (or right to decline, which we refer to as an opt-out , a practice that may differ across our various websites, depending on the applicable needs and requirements of different countries laws), we may use this information to inform our users of services that they have indicated may be of interest to them. We may also share this information with our advertising clients for registered members who have elected to receive additional promotional materials and have granted us permission to share their information with third parties. We also collect information on our registered members and users based on their activity on our sites. The United States federal and various state governments have adopted or proposed limitations on the collection, distribution and use of personal information of Internet users. Additionally, several foreign jurisdictions, including the European Union, and the United Kingdom, and Canada, have adopted legislation (including directives or regulations) that may increase the requirements for collecting, or limit our collection and use of, information from Internet users in these jurisdictions. In addition, growing public concern about privacy, data security and the collection, distribution and use of personal information has led to self-regulation of these practices by the Internet advertising and direct marketing industry, and to increased federal and state regulation. In addition, in May 2014, the Obama administration released a report that advocates a framework to address online consumer privacy. Among other things, the report renews calls for privacy legislation based on a Consumer Privacy Bill of Rights. The proposed Consumer Bill of Rights would notably allow consumers the right to exercise control over the collection and use of personal data, including the ability to access and correct personal data, for such personal data to be collected and used in accordance with easily understandable privacy and security policies and expect the secure and responsible handling of personal data. The Obama administration has asked the United States Department of Commerce to work with industry, privacy advocates and other stakeholders to draft legislative text to implement the principles outlined in the White House report. Because many of the proposed laws or regulations are in their early stages, we cannot yet determine the impact these regulations may have on our business over time. Although, to date, our efforts to comply with applicable federal and state laws and regulations have not hurt our business, additional, more burdensome laws or regulations, including more restrictive consumer privacy and data security laws, could be enacted or applied to us or our customers. Such laws or regulations could impair our ability to collect user information that helps us to provide more targeted advertising to our users and detailed lead data to our advertising clients, thereby impairing our ability to maintain and grow our audience and maximize advertising revenue from our clients. Additionally, the FTC and many state attorneys general are applying federal and state consumer protection laws to require that the online collection, use and dissemination of data, and the presentation of website content, comply with certain standards for notice, choice, security and access. Courts may also adopt these developing standards. In many cases, the specific limitations imposed by these standards are subject to interpretation by courts and other governmental authorities. A few states have also introduced legislation that, if enacted, would restrict or prohibit behavioral advertising within the state. In the absence of a federal law pre-empting their enforcement, such state legislation would likely have the practical effect of regulating behavioral advertising nationwide because of the difficulties behind implementing state-specific policies or identifying the location of a particular user. In the event of additional legislation in this area, our ability to effectively target our users may be limited. We believe that we are in compliance with applicable consumer protection laws that apply to us, but a determination by a state or federal agency or court that any of our practices do not meet these laws and regulations could create liability to us, result in adverse publicity and affect negatively our businesses. New interpretations of these standards could also require us to incur additional costs and restrict our business operations.

As we deploy new products, we will need to update our privacy policy to describe any relevant changes to our practices. Failure to do so could give rise to federal or state enforcement actions or lawsuits that could materially affect our business. In addition, several foreign governmental bodies, including the European Union, the United Kingdom, and Canada have regulations dealing with the collection and use of personal information obtained from their citizens. Regulations in these territories have focused on the collection, use, disclosure and security of information that may be used to identify or that actually identifies an individual, such as an e-mail address or a name. Further, within the European Union, certain member state data protection authorities regard IP addresses as personal information, and legislation in the European Union requires informed consent for the placement of a cookie on a user device. We believe that we are in material compliance with such regulations as applicable to us; however, such regulations and laws may be modified and new laws may be enacted in the future. Further, data protection authorities may interpret existing laws in new ways. Any such developments (or developments stemming from enactment or modification of other laws) or the failure to anticipate accurately the application or interpretation of these laws could create liability to us, result in adverse publicity and negatively affect our businesses.

United States and European lawmakers and regulators have recently expressed concern over the use of third party cookies or web beacons for the purpose of online behavioral advertising, and efforts to address these uses may result in broader requirements that would apply to research activities, including understanding our users Internet usage. Such actions may have a chilling effect on businesses that collect or use online usage information generally or substantially increase the cost of maintaining a business that collects or uses online usage information, increase regulatory scrutiny and increase the potential of class action lawsuits. In response to marketplace concerns about the usage of third party cookies and web beacons to track user behaviors, the major browser applications have enabled features that allow the user to limit the collection of certain data. These developments could impair our ability to collect user information that helps us provide more targeted advertising to our users. In addition, several browser applications, including but not limited to Microsoft s Internet Explorer, Mozilla Firefox, Google Chrome and Apple s Safari browser contain tracking protection features and options that allow users to opt out of ad-tracking cookies and in certain cases block behavioral tracking from specified websites. In the event users implement these tracking features and options, they have the potential to affect our business negatively.

Increased exposure from loss of personal information could impose significant additional costs on us.

Many states and foreign jurisdictions in which we operate have enacted regulations requiring us to notify customers in the event that certain customer information is accessed, or believed to have been accessed, without authorization and in some cases also develop proscriptive policies to protect against such unauthorized access. Such notifications can result in private causes of action being filed against us. Additionally, increasing regulatory demands are requiring us to provide protection of personal information to prevent identity theft and the disclosure of sensitive information. Should we experience a loss of protected data, efforts to regain compliance and address penalties imposed by such regulatory regimes could increase our costs.

Table of Contents

Changes in regulations could adversely affect our business and results of operations.

It is possible that new laws and regulations or new interpretations of existing laws and regulations in the United States and elsewhere will be adopted covering issues affecting our business, including:

- privacy, data security and use of personally identifiable information;
- copyrights, trademarks and domain names; and
- marketing practices such as behavioral advertising, e-mail or direct marketing.

Increased government regulation, or the application of existing laws to online activities, could:

- decrease the growth rate of the Internet;
- reduce our revenues;
- increase our operating expenses; or
- expose us to significant liabilities.

Furthermore, the relationship between regulations governing domain names and laws protecting trademarks and similar proprietary rights is still evolving. Therefore, we might be unable to prevent third parties from acquiring domain names that infringe or otherwise decrease the value of our trademarks and other proprietary rights. Any impairment in the value of these important assets could cause our stock price to decline. We cannot be sure what effect any future material noncompliance by us with these laws and regulations or any material changes in these laws and regulations could have on our business, operating results and financial condition.

As a creator and a distributor of content over the Internet, we face potential liability for legal claims based on the nature and content of the materials that we create or distribute.

Due to the nature of content published on our online network, including content placed on our online network by third parties, and as a creator and distributor of original content and research, we face potential liability based on a variety of theories, including defamation, negligence, copyright or trademark infringement, or other legal theories based on the nature, creation or distribution of this information. Such claims may also include, among others, claims that by providing hypertext links to websites operated by third parties, we are liable for wrongful actions by those third parties through these websites. Similar claims have been brought, and sometimes successfully asserted, against online services. It is also possible that our users could make claims against us for losses incurred in reliance on information provided on our networks. In addition, we could be exposed to liability in connection with material posted to our Internet sites by third parties. For example, many of our sites offer users an opportunity to post comments and opinions that are not moderated. Some of this user-generated content may infringe on third-party intellectual property rights or privacy rights or may otherwise be subject to challenge under copyright laws. Such claims, whether brought in the United States or abroad, could divert management time and attention away from our business and result in significant cost to investigate and defend, regardless of the merit of these claims. In addition, if we become subject to these types of claims and are not successful in our defense, we may be forced to pay substantial damages. Our insurance may not adequately protect us against these claims. The filing of these claims may also damage our reputation as a high quality provider of unbiased, timely analysis and result in client cancellations or overall decreased demand for our services.

We may be liable if third parties or our employees misappropriate our users confidential business information.

We currently retain confidential information relating to our users in secure database servers. Although we observe security measures throughout our operations, we cannot assure you that we will be able to prevent individuals from gaining unauthorized access to these database servers. Any unauthorized access to our servers, or abuse by our employees, could result in the theft of confidential user information. If confidential information is compromised, we could lose customers or become subject to liability or litigation and our reputation could be harmed, any of which could materially and adversely affect our business and results of operations.

Our business, which is dependent on centrally located communications and computer hardware systems, is vulnerable to natural disasters, telecommunication and systems failures, terrorism and other problems, which could reduce traffic on our networks or websites and result in decreased capacity for advertising space.

Our operations are dependent on our communications systems and computer hardware, all of which are located in data centers operated by third parties. These systems could be damaged by fire, floods, earthquakes, power loss, telecommunication failures and similar events. Our insurance policies have limited coverage levels for loss or damages in these events and may not adequately compensate us for any losses that may occur. In addition, terrorist acts or acts of war

Table of Contents

may cause harm to our employees or damage our facilities, our clients, our clients customers and vendors, or cause us to postpone or cancel, or result in dramatically reduced attendance at, our events, which could adversely impact our revenues, costs and expenses and financial position. We are predominantly uninsured for losses and interruptions to our systems or cancellations of events caused by terrorist acts and acts of war.

Our systems may be subject to slower response times and system disruptions that could adversely affect our revenues.

Our ability to attract and maintain relationships with users, advertisers and strategic partners depends on the satisfactory performance, reliability and availability of our Internet infrastructure. Our Internet advertising revenues relate directly to the number of advertisements and other marketing opportunities delivered to our users. System interruptions or delays that result in the unavailability of Internet sites or slower response times for users would reduce the number of advertising impressions and leads delivered. This could reduce our revenues as the attractiveness of our sites to users and advertisers decreases. Our insurance policies provide only limited coverage for service interruptions and may not adequately compensate us for any losses that may occur due to any failures or interruptions in our systems. Further, we do not have multiple site capacity for all of our services in the event of any such occurrence.

We may experience service disruptions for the following reasons:

- occasional scheduled maintenance;
- equipment failure;
- volume of visits to our websites that exceed our infrastructure s capacity; and
- natural disasters, telecommunications failures, power failures, other system failures, maintenance, viruses, hacking or other events outside of our control.

In addition, our networks and websites must accommodate a high volume of traffic and deliver frequently updated information. They have experienced in the past, and may experience in the future, slower response times or decreased traffic for a variety of reasons. There have been instances where our online networks as a whole, or our websites individually, have been inaccessible. Also, slower response times, which have occurred more frequently, can result from general Internet problems, routing and equipment problems involving third-party Internet access providers, problems with third-party advertising servers, increased traffic to our servers, viruses and other security breaches, many of which problems are out of our control. In addition, our users depend on Internet service providers and online service providers for access to our online networks or websites. Those providers have experienced outages and delays in the past, and may experience outages or delays in the future. Moreover, our Internet infrastructure might not be able to support continued growth of our online networks or websites. Any of these problems could result in less traffic to our networks or websites or harm the perception of our networks or websites as reliable sources of information. Less traffic on our networks and websites or periodic interruptions in service could have the effect of reducing demand for advertising on our networks or websites, thereby reducing our advertising revenues.

Our networks may be vulnerable to unauthorized persons accessing our systems, viruses and other disruptions, which could result in the theft of our proprietary information and/or disrupt our Internet operations making our

websites less attractive and reliable for our users and advertisers.

Internet usage could decline if any well-publicized compromise of security occurs. Hacking involves efforts to gain unauthorized access to information or systems or to cause intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment. Hackers, if successful, could misappropriate proprietary information or cause disruptions in our service. We may be required to expend capital and other resources to protect our websites against hackers. Our online networks could also be affected by computer viruses or other similar disruptive problems, and we could inadvertently transmit viruses across our networks to our users or other third parties. Any of these occurrences could harm our business or give rise to a cause of action against us. Providing unimpeded access to our online networks is critical to servicing our customers and providing superior customer service. Our inability to provide continuous access to our online networks could cause some of our customers to discontinue purchasing advertising programs and services and/or prevent or deter our users from accessing our networks. Our activities and the activities of third-party contractors involve the storage and transmission of proprietary and personal information. Accordingly, security breaches could expose us to a risk of loss or litigation and possible liability. We cannot assure that contractual provisions attempting to limit our liability in these areas will be successful or enforceable, or that other parties will accept such contractual provisions as part of our agreements.

Table of Contents

If we do not maintain proper and effective disclosure controls and procedures and internal controls over financial reporting, our ability to produce accurate financial statements could be impaired, which could adversely affect our operating results, our ability to operate our business and investors views of us.

Ensuring that we have adequate disclosure controls and procedures, including internal financial and accounting controls and procedures, in place to help ensure that we can produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. On an ongoing basis, both we and our independent auditors document and test our internal controls and procedures in connection with the requirements of Section 404 of the Sarbanes-Oxley Act and, as part of that documentation and testing, identify areas for further attention and improvement. Implementing any appropriate changes to our internal controls may entail substantial costs in order to modify our existing accounting systems, take a significant period of time to complete and distract our officers, directors and employees from the operation of our business. These changes may not, however, be effective in maintaining the adequacy of our internal controls, and any failure to maintain that adequacy, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and could materially impair our ability to operate our business. In addition, investors perceptions that our internal controls are inadequate or that we are unable to produce accurate financial statements may seriously affect our stock price.

Our ability to raise capital in the future may be limited.

Our business and operations may consume resources faster than we anticipate. In the future, we may need to raise additional funds to expand our sales and marketing and service development efforts or to make acquisitions. Additional financing may not be available on favorable terms, if at all. If adequate funds are not available on acceptable terms, we may be unable to fund the expansion of our sales and marketing and research and development efforts or take advantage of acquisition or other opportunities, which could seriously harm our business and operating results. If we incur debt, the debt holders would have rights senior to common stockholders to make claims on our assets and the terms of any debt could restrict our operations, including our ability to pay dividends on our common stock. Furthermore, if we issue additional equity securities, stockholders will experience dilution, and the new equity securities could have rights senior to those of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, our stockholders bear the risk of our future securities offerings reducing the market price of our common stock and diluting their interest.

The impairment of a significant amount of goodwill and intangible assets on our balance sheet could result in a decrease in earnings and, as a result, our stock price could decline.

In the course of our operating history, we have acquired assets and businesses. Some of our acquisitions have resulted in the recording of a significant amount of goodwill and/or intangible assets on our financial statements. We had approximately $94.0 million of goodwill and $3.5 million of net intangible assets as of September 30, 2014. The goodwill and/or intangible assets were recorded because the fair value of the net tangible assets acquired was less than the purchase price. We may not realize the full value of the goodwill and/or intangible assets. As such, we evaluate goodwill and other intangible assets with indefinite useful lives for impairment on an annual basis or more frequently if events or circumstances suggest that the asset may be impaired. We did not have any intangible assets with indefinite lives as of September 30, 2014 or December 31, 2013. We evaluate other intangible assets subject to amortization whenever events or changes in circumstances indicate that the carrying amount of those assets may not be recoverable. If goodwill or other intangible assets are determined to be impaired, we will write off the unrecoverable portion as a charge to our earnings. If we acquire new assets and businesses in the future, as we intend to do, we may record additional goodwill and/or intangible assets. The possible write-off of the goodwill and/or intangible assets could negatively impact our future earnings and, as a result, the market price of our common stock could decline.

The trading value of our common stock may be volatile and decline substantially.

The trading price of our common stock may be volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control. In addition to the factors discussed in this Risk Factors section and elsewhere in this Annual Report, these factors include:

- our operating performance and the operating performance of similar companies;
- the overall performance of the equity markets;
- announcements by us or our competitors of acquisitions, business plans, commercial relationships or new product or service offerings;
- threatened or actual litigation;
- changes in laws or regulations relating to the provision of Internet content;
- any change in our board of directors or management;

Table of Contents

- publication of research reports about us, our competitors or our industry, or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- our sale of common stock or other securities in the future;
- large volumes of sales of our shares of common stock by existing stockholders; and
- general political and economic conditions.

In addition, the stock market in general, and historically the market for Internet-related companies in particular, has experienced price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Securities class action litigation has often been instituted against companies following periods of volatility in the overall market and in the market price of a company s securities. Such litigation, if instituted against us, could result in substantial costs, divert our management s attention and resources and harm our business, operating results and financial condition.

Provisions of our certificate of incorporation, bylaws and Delaware law could deter takeover attempts.

Various provisions in our certificate of incorporation and bylaws could delay, prevent or make more difficult a merger, tender offer, proxy contest or change of control. Our stockholders might view any transaction of this type as being in their best interest since the transaction could result in a higher stock price than the then-current market price for our common stock. Among other things, our certificate of incorporation and bylaws:

- authorize our board of directors to issue preferred stock with the terms of each series to be fixed by our board of directors, which could be used to institute a poison pill that would work to dilute the share ownership of a potential hostile acquirer, effectively preventing acquisitions that have not been approved by our board;
- divide our board of directors into three classes so that only approximately one-third of the total number of directors is elected each year;
- permit directors to be removed only for cause;
- prohibit action by written consent of our stockholders; and
- specify advance notice requirements for stockholder proposals and director nominations. In addition, with some exceptions, the Delaware General Corporation Law restricts or delays mergers and other business combinations between us and any stockholder that acquires 15% or more of our voting stock.

Future sales of shares of our common stock by existing stockholders could depress the market price of our common stock.

If our existing stockholders sell, or indicate an intent to sell, substantial amounts of our common stock in the public market, the trading price of our common stock could decline significantly. A large portion of our outstanding shares of common stock is held by our officers, directors and significant stockholders. Two of the largest percentages of our shares are owned by venture capital funds, which are typically structured to have a finite life. As these venture capital funds approach or pass the respective terms of the fund, the decision to sell or hold our stock may be based not only on the underlying investment merits of our stock but also on the requirements of their internal fund structure. Our directors, executive officers and significant stockholders beneficially own approximately 13.7 million shares of our common stock, which represents 42% of our shares outstanding as of September 30, 2014. If these additional shares are sold, or if it is perceived that they will be sold in the public market, the trading price of our common stock could decline substantially.

A limited number of stockholders will have the ability to influence the outcome of director elections and other matters requiring stockholder approval.

Our directors, executive officers and significant stockholders beneficially own approximately 42% of our outstanding common stock. These stockholders, if they act together, could exert substantial influence over matters requiring approval by our stockholders, including the election of directors, the amendment of our certificate of incorporation and bylaws and the approval of mergers or other business combination transactions. This concentration of ownership may discourage, delay or prevent a change in control of our company, which could deprive our stockholders of an opportunity to receive a premium for their stock as part of a sale of our company and might reduce our stock price. These actions may be taken even if they are opposed by other stockholders.

Table of Contents

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Sales of Unregistered Securities

None.

(b) Use of Proceeds from Registered Securities

None.

(c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table provides information about purchases by the Company during the quarter ended September 30, 2014 of equity securities that are registered by the Company pursuant to Section 12 of the Exchange Act.

Period	Total Number of Shares Purchased	Average Price Paid Per Share *	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
July 1, 2014 July 31, 2014		$		$
August 1, 2014 August 31, 2014	311,522	$ 8.49	311,522	$ 17,347,004
September 1, 2014 September 30, 2014		$		$ 17,347,004
Total (2)	311,522	$ 8.49	311,522	$ 17,347,004

(1) On August 5, 2014, the Board of Directors announced the approval of a Stock Repurchase Program (the 2014 Program), which authorized the Company to purchase up to $20 million of shares of its common stock from time to time on the open market or in privately negotiated transactions.

(2) All shares were repurchased under the 2014 Program.

* Price excludes commission of approximately $0.03 per share.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

The exhibits listed in the Exhibit Index immediately preceding the exhibits are filed as part of this Quarterly Report on Form 10-Q and such Exhibit Index is incorporated herein by reference.

Table of Contents

SIGNATURES

Pursuant to the requirements 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.

TECHTARGET, INC

(Registrant)

Date: November 7, 2014	By:	/s/ GREG STRAKOSCH Greg Strakosch, *Chief Executive Officer* *(Principal Executive Officer)*
Date: November 7, 2014	By:	/s/ JANICE KELLIHER Janice Kelliher, *Chief Financial Officer and Treasurer* *(Principal Accounting and Financial Officer)*

48

Table of Contents

Exhibit Index

Exhibit No.	Description of Exhibit
31.1	Certification of Greg Strakosch, Chief Executive Officer of TechTarget, Inc., pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, dated November 7, 2014.
31.2	Certification of Janice Kelliher, Chief Financial Officer and Treasurer of TechTarget, Inc., pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, dated November 7, 2014.
32.1	Certifications of Greg Strakosch, Chief Executive Officer of TechTarget, Inc. and Janice Kelliher, Chief Financial Officer and Treasurer of TechTarget, Inc. pursuant to 18 U.S.C. Section 1350, dated November 7, 2014.
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

* Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets as of September 30, 2014 and December 31, 2013, (ii) Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended September 30, 2014 and September 30, 2013, (iii) Consolidated Statements of Cash Flows for the nine months ended September 30, 2014 and September 30, 2013 and (iv) Notes to Consolidated Financial Statements.