

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2020

OR

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

For the transition period from _____ to _____

Commission File Number: 001-38107

ShotSpotter, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or other jurisdiction of
incorporation or organization)
7979 Gateway Blvd., Suite 210
Newark, California
(Address of principal executive offices)

47-0949915
(I.R.S. Employer
Identification No.)

94560
(Zip Code)

Registrant's telephone number, including area code: (510) 794-3100

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, par value \$0.005 per share	SSTI	The Nasdaq Capital Market

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

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

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
Emerging growth company	<input checked="" type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of October 31, 2020, the registrant had 11,441,762 shares of common stock, \$0.005 par value per share, outstanding.

Table of Contents

	<u>Page</u>
PART I.	
	<u>FINANCIAL INFORMATION</u>
Item 1.	<u>Condensed Consolidated Financial Statements</u> 2
	<u>Condensed Consolidated Balance Sheets</u> 2
	<u>Condensed Consolidated Statements of Operations</u> 3
	<u>Condensed Consolidated Statements of Comprehensive Income</u> 4
	<u>Condensed Consolidated Statements of Stockholders' Equity</u> 5
	<u>Condensed Consolidated Statements of Cash Flows</u> 7
	<u>Notes to Condensed Consolidated Financial Statements</u> 8
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 18
Item 3.	<u>Qualitative and Quantitative Disclosures About Market Risk</u> 31
Item 4.	<u>Controls and Procedures</u> 31
PART II.	
	<u>OTHER INFORMATION</u>
Item 1A.	<u>Risk Factors</u> 32
Item 6.	<u>Exhibits</u> 58
	<u>Exhibit Index</u> 59
	<u>Signatures</u> 60

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

ShotSpotter, Inc.
Condensed Consolidated Balance Sheets
(In thousands)

	<u>September 30, 2020</u> (Unaudited)	<u>December 31, 2019</u>
Assets		
Current assets		
Cash and cash equivalents	\$ 28,666	\$ 24,550
Accounts receivable and contract asset	6,866	13,883
Prepaid expenses and other current assets	2,286	1,764
Total current assets	37,818	40,197
Property and equipment, net	15,359	16,556
Operating lease right-of-use assets	761	556
Goodwill	1,379	1,379
Intangible assets, net	226	249
Other assets	1,343	1,634
Total assets	<u>\$ 56,886</u>	<u>\$ 60,571</u>
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 818	\$ 1,179
Deferred revenue, short-term	20,388	26,360
Accrued expenses and other current liabilities	4,241	4,885
Total current liabilities	25,447	32,424
Deferred revenue, long-term	255	598
Other liabilities	456	298
Total liabilities	26,158	33,320
Stockholders' equity		
Preferred stock	—	—
Common stock	57	57
Additional paid-in capital	125,113	122,907
Accumulated deficit	(94,134)	(95,579)
Accumulated other comprehensive loss	(308)	(134)
Total stockholders' equity	30,728	27,251
Total liabilities and stockholders' equity	<u>\$ 56,886</u>	<u>\$ 60,571</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Operations
(In thousands, except share and per share data)
(Unaudited)

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
Revenues	\$ 11,350	\$ 9,984	\$ 33,085	\$ 29,837
Costs				
Cost of revenues	4,745	4,019	13,440	12,300
Impairment of property and equipment	161	—	161	—
Total costs	<u>4,906</u>	<u>4,019</u>	<u>13,601</u>	<u>12,300</u>
Gross profit	6,444	5,965	19,484	17,537
Operating expenses				
Sales and marketing	2,400	2,426	7,237	7,494
Research and development	1,375	1,358	4,104	4,026
General and administrative	2,040	1,803	6,627	5,669
Total operating expenses	<u>5,815</u>	<u>5,587</u>	<u>17,968</u>	<u>17,189</u>
Operating income	<u>629</u>	<u>378</u>	<u>1,516</u>	<u>348</u>
Other income (expense), net				
Interest income, net	3	131	101	335
Other expense, net	(58)	(70)	(173)	(179)
Total other income (expense), net	<u>(55)</u>	<u>61</u>	<u>(72)</u>	<u>156</u>
Income before income taxes	574	439	1,444	504
Provision (benefit) for income taxes	8	(7)	(1)	33
Net income	<u>\$ 566</u>	<u>\$ 446</u>	<u>\$ 1,445</u>	<u>\$ 471</u>
Net income per share, basic	<u>\$ 0.05</u>	<u>\$ 0.04</u>	<u>\$ 0.13</u>	<u>\$ 0.04</u>
Net income per share, diluted	<u>\$ 0.05</u>	<u>\$ 0.04</u>	<u>\$ 0.12</u>	<u>\$ 0.04</u>
Weighted average shares used in computing net income per share, basic	11,423,079	11,449,946	11,383,860	11,275,195
Weighted average shares used in computing net income per share, diluted	11,727,112	11,917,382	11,718,770	11,865,319

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Comprehensive Income
(In thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Net income	\$ 566	\$ 446	\$ 1,445	\$ 471
Other comprehensive income (loss):				
Change in foreign currency translation adjustment, net	29	(91)	(174)	(69)
Comprehensive income	<u>\$ 595</u>	<u>\$ 355</u>	<u>\$ 1,271</u>	<u>\$ 402</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Stockholders' Equity
(In thousands, except share data)
(Unaudited)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Par Value				
Balance at December 31, 2019	11,314,150	\$ 57	\$ 122,907	\$ (95,579)	\$ (134)	\$ 27,251
Exercise of stock options	17,543	—	57	—	—	57
Issuance of common stock in connection with exercise of warrants	46,939	—	—	—	—	—
Issuance of common stock from RSUs vested	20,297	—	—	—	—	—
Stock-based compensation	—	—	887	—	—	887
Other comprehensive loss	—	—	—	—	(227)	(227)
Net income	—	—	—	13	—	13
Balance at March 31, 2020	<u>11,398,929</u>	<u>\$ 57</u>	<u>\$ 123,851</u>	<u>\$ (95,566)</u>	<u>\$ (361)</u>	<u>\$ 27,981</u>
Exercise of stock options	26,562	—	41	—	—	41
Issuance of common stock from RSUs vested	22,754	—	—	—	—	—
Issuance of common stock from ESPP purchase	21,431	—	408	—	—	408
Repurchase of common stock	(74,520)	—	(1,615)	—	—	(1,615)
Stock-based compensation	—	—	1,163	—	—	1,163
Other comprehensive income	—	—	—	—	24	24
Net income	—	—	—	866	—	866
Balance at June 30, 2020	<u>11,395,156</u>	<u>\$ 57</u>	<u>\$ 123,848</u>	<u>\$ (94,700)</u>	<u>\$ (337)</u>	<u>\$ 28,868</u>
Exercise of stock options	40,565	—	69	—	—	69
Issuance of common stock from RSUs vested	6,041	—	—	—	—	—
Stock-based compensation	—	—	1,196	—	—	1,196
Other comprehensive income	—	—	—	—	29	29
Net income	—	—	—	566	—	566
Balance at September 30, 2020	<u>11,441,762</u>	<u>\$ 57</u>	<u>\$ 125,113</u>	<u>\$ (94,134)</u>	<u>\$ (308)</u>	<u>\$ 30,728</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Stockholders' Equity
(In thousands, except share data)
(Unaudited)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Par Value				
Balance at December 31, 2018	10,864,722	\$ 55	\$ 114,618	\$ (97,377)	\$ (149)	\$ 17,147
Exercise of stock options	177,408	1	218	—	—	219
Issuance of common stock upon secondary offering, net of costs	250,000	1	10,553	—	—	10,554
Issuance of common stock from RSUs vested	28,790	—	—	—	—	—
Stock-based compensation	—	—	754	—	—	754
Other comprehensive loss	—	—	—	—	(13)	(13)
Net loss	—	—	—	(362)	—	(362)
Balance at March 31, 2019	<u>11,320,920</u>	<u>\$ 57</u>	<u>\$ 126,143</u>	<u>\$ (97,739)</u>	<u>\$ (162)</u>	<u>\$ 28,299</u>
Exercise of stock options	65,960	—	129	—	—	129
Issuance of common stock in connection with exercise of warrants	12,225	—	51	—	—	51
Issuance of common stock from ESPP purchase	53,508	—	642	—	—	642
Issuance of common stock from RSUs vested	24,072	—	—	—	—	—
Stock-based compensation	—	—	905	—	—	905
Other comprehensive income	—	—	—	—	35	35
Net income	—	—	—	387	—	387
Balance at June 30, 2019	<u>11,476,685</u>	<u>\$ 57</u>	<u>\$ 127,870</u>	<u>\$ (97,352)</u>	<u>\$ (127)</u>	<u>\$ 30,448</u>
Exercise of stock options	58,806	1	94	—	—	95
Repurchase of common stock	(120,000)	(1)	(3,465)	—	—	(3,466)
Issuance of common stock in connection with exercise of warrants	13,873	—	20	—	—	20
Issuance of common stock from RSUs vested	2,814	—	—	—	—	—
Stock-based compensation	—	—	716	—	—	716
Other comprehensive loss	—	—	—	—	(91)	(91)
Net income	—	—	—	446	—	446
Balance at September 30, 2019	<u>11,432,178</u>	<u>\$ 57</u>	<u>\$ 125,235</u>	<u>\$ (96,906)</u>	<u>\$ (218)</u>	<u>\$ 28,168</u>

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2020	2019
Cash flows from operating activities:		
Net income	\$ 1,445	\$ 471
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property and equipment	3,975	3,576
Amortization of intangible assets	71	65
Impairment of property and equipment	161	—
Stock-based compensation	3,246	2,375
Loss on disposal of property and equipment	3	—
Provision for accounts receivable	41	—
Changes in operating assets and liabilities:		
Accounts receivable and contract asset	6,976	8,482
Prepaid expenses and other assets	(273)	(303)
Accounts payable	(185)	(617)
Accrued expenses and other current liabilities	(336)	(73)
Deferred revenue	(6,315)	(2,825)
Net cash provided by operating activities	<u>8,809</u>	<u>11,151</u>
Cash flows from investing activities:		
Purchase of property and equipment	(3,132)	(3,672)
Investment in intangible and other assets	(46)	(59)
Net cash used in investing activities	<u>(3,178)</u>	<u>(3,731)</u>
Cash flows from financing activities:		
Payment of contingent consideration liability	(347)	—
Proceeds from issuance of common stock in public offering	—	11,247
Payment of line of credit costs	(4)	—
Payments of offering costs	—	(445)
Proceeds from exercise of stock options	167	443
Repurchases of common stock	(1,615)	(3,466)
Proceeds from exercise of warrants	—	71
Proceeds from employee stock purchase plan	408	642
Net cash provided by (used in) financing activities	<u>(1,391)</u>	<u>8,492</u>
Increase in cash and cash equivalents	4,240	15,912
Effect of exchange rate on cash and cash equivalents	(124)	(52)
Cash and cash equivalents at beginning of year	24,550	10,278
Cash and cash equivalents at end of period	<u>\$ 28,666</u>	<u>\$ 26,138</u>
Supplemental cash flow disclosures:		
Purchases of property and equipment included in accounts payable	\$ 143	\$ 26

See accompanying notes to condensed consolidated financial statements.

ShotSpotter, Inc.
Notes to Condensed Consolidated Financial Statements

Note 1. Organization and Description of Business

ShotSpotter, Inc. (the “Company”) provides precision-policing solutions for law enforcement to help prevent and reduce gun violence and make cities, campuses and facilities safer. The company’s flagship product, ShotSpotter Flex, is the leading outdoor gunshot detection, location and forensic system trusted by over 110 cities. ShotSpotter SecureCampus and ShotSpotter SiteSecure are designed to help law enforcement and security personnel serving universities, corporate campuses and key infrastructure or transportation centers mitigate risk and enhance security by notifying authorities of a potential outdoor gunfire incident. ShotSpotter Connect (formerly ShotSpotter Missions) uses machine learning-driven analysis to help strategically plan directed patrol missions and tactics for maximum crime deterrence. ShotSpotter Labs is the Company’s effort to support innovative uses of its technology to help protect wildlife and the environment. The Company offers its solutions on a SaaS-based subscription model to its customers.

The Company’s principal executive offices are located in Newark, California. The Company has four wholly owned subsidiaries in South Africa, Colombia, Brazil and Mexico.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and note disclosures normally included in the consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated financial statements include the results of the Company and its wholly owned subsidiaries. All significant intercompany transactions have been eliminated upon consolidation.

The accompanying condensed consolidated financial statements and related financial information should be read in conjunction with the consolidated financial statements filed with the Company’s Annual Report on Form 10-K for the year ended December 31, 2019 (“Annual Report”).

In the opinion of management, the accompanying condensed consolidated financial statements reflect all normal recurring adjustments necessary to present fairly the financial position, results of operations, comprehensive income, equity statement and cash flows for the interim periods, but are not necessarily indicative of the results of operations or cash flows to be anticipated for the full year 2020 or any future period. The Company has evaluated subsequent events occurring after the date of the condensed consolidated financial statements for events requiring recording or disclosure in the condensed consolidated financial statements.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates its significant estimates, including the valuation of accounts receivable, the lives and realization of tangible and intangible assets, stock-based compensation expense, customer life, accounting for revenue recognition, and income taxes including deferred taxes and valuation allowance. Management bases its estimates on historical experience and on various other market-specific and relevant assumptions it believes to be reasonable under the circumstances. Actual results could differ from those estimates and such differences could be material to the Company’s financial position and results of operations.

The Company records net deferred tax assets to the extent the Company believes these assets will more likely than not be realized. In making such a determination, the Company considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies, and results of recent operations. In the event the Company determines that it would be able to realize its deferred assets in the future in excess of their net recorded amount, the Company makes an adjustment to the deferred tax asset valuation allowance, which would reduce the provision for income taxes.

Concentrations of Risk

Credit Risk – Financial instruments that potentially subject the Company to concentration of credit risk consisted primarily of cash and cash equivalents and accounts receivable from trade customers. The Company maintains its cash deposits at three domestic and two international financial institutions. The Company is exposed to credit risk in the event of default by a financial institution to the extent that cash and cash equivalents are in excess of the amount insured by the Federal Deposit Insurance Corporation. The Company generally places its cash and cash equivalents with high-credit quality financial institutions. To date, the Company has not experienced any losses on its cash and cash equivalents.

Concentration of Accounts Receivable – At September 30, 2020, two customers accounted for 21% and 11% of the Company’s total accounts receivable. At December 31, 2019, one customer accounted for 55% of the Company’s total accounts receivable.

Concentration of Revenues – For the three months ended September 30, 2020, two customers accounted for 18% and 13% of the Company’s total revenues. For the three months ended September 30, 2019, two customers accounted for 20% and 14% of the Company’s total revenues.

For the nine months ended September 30, 2020, two customers accounted for 18% and 13% of the Company’s total revenues. For the nine months ended September 30, 2019, two customers accounted for 20% and 14% of the Company’s total revenues.

Concentration of Suppliers – The Company relies on a limited number of suppliers and contract manufacturers. In particular, a single supplier is currently the sole manufacturer of the Company’s proprietary sensors.

Recent Accounting Pronouncements Not Yet Effective

In December 2019, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2019-12, *Income Taxes (Topic 740)*, simplifying the accounting for income taxes by removing certain exceptions to the general principles. The guidance will be effective at the beginning of the Company’s first quarter of fiscal 2021. Early adoption of the amendments is permitted. The Company does not expect the adoption of this ASU to have any material impact on its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The amendments in this ASU replace the incurred loss impairment methodology in current GAAP with a methodology that reflects current expected credit loss (“CECL”) and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The guidance will be effective at the beginning of the Company’s first quarter of fiscal 2023. Early adoption of the amendments is permitted. The Company does not expect the adoption of this ASU to have any material impact on its condensed consolidated financial statements.

Note 3. Revenue Related Disclosures

As of December 31, 2019, the Company had total short-term and long-term deferred revenue of \$7.0 million. During the three months ended September 30, 2020, the Company recognized \$9.5 million in revenue from the beginning deferred revenue balance and \$1.8 million from new billings and added \$9.7 million to total short-term and long-term deferred revenue from new billings. During the nine months ended September 30, 2020, the Company recognized \$22.8 million in revenue from the beginning deferred revenue balance and \$10.2 million from new billings and added \$26.6 million to total short-term and long-term deferred revenue from new billings.

As of December 31, 2018, the Company had total short-term and long-term deferred revenue of \$4.2 million. During the three months ended September 30, 2019, the Company recognized \$8.8 million in revenue from the beginning deferred revenue balance and \$1.1 million from new billings and added \$8.1 million to total short-term and long-term deferred revenue from new billings. During the nine months ended September 30, 2019, the Company recognized \$20.0 million in revenue from the beginning deferred revenue balance and \$9.7 million from new billings and added \$26.8 million to total short-term and long-term deferred revenue from new billings.

As of September 30, 2020, the Company has estimated remaining performance obligations for contractually committed revenues of \$10.7 million, \$28.8 million, \$8.3 million, and \$3.1 million that will be recognized during the remainder of the year ending December 31, 2020, the years ending December 31, 2021, 2022, and the three-year period from 2023 through 2025, respectively. The timing of revenue recognition includes estimates of go-live dates for contracts not yet live. There is considerable uncertainty in the Company's estimates of go-live dates as a result of the novel strain of coronavirus (COVID-19) pandemic and resulting disruption in the Company's ability to deploy new go-live miles. See Note 12. *Commitments and Contingencies*. Contractually committed revenue includes deferred revenue as of September 30, 2020 and amounts under contract that will be invoiced after September 30, 2020.

During the three months ended September 30, 2020, the Company recognized revenues of \$11.2 million from customers in the United States, and \$0.2 million from customers in the Bahamas and South Africa. During the nine months ended September 30, 2020, the Company recognized revenues of \$32.6 million from customers in the United States, and \$0.5 million from customers in the Bahamas and South Africa.

During the three months ended September 30, 2019, the Company recognized revenues of \$9.8 million from customers in the United States and \$0.2 million from customers in South Africa and the Bahamas. During the nine months ended September 30, 2019, the Company recognized revenues of \$28.9 million from customers in the United States and \$0.9 million from customers in South Africa and the Bahamas.

Accounts Receivable, net and Contract Asset

Accounts receivable, net consist of trade accounts receivable from the Company's customers, net of allowance for doubtful accounts if deemed necessary. Accounts receivable are recorded as the invoiced amount. The Company does not require collateral or other security for accounts receivable. Contract asset consists of revenues recognized in advance of invoicing the customer.

The Company periodically evaluates the collectability of its accounts receivable and provides an allowance for potential credit losses based on the Company's historical experience. At September 30, 2020, the Company had a provision against accounts receivable of \$41,000. At December 31, 2019, the Company did not have a provision for potential credit losses as there were no estimated credit losses.

Note 4. Fair Value Measurements

In October 2018, upon the acquisition of certain technology, referred to as HunchLab, from Azavea, Inc., the Company recognized a contingent consideration liability classified within Level III of the fair value hierarchy because some of the inputs used in its measurement were neither directly nor indirectly observable. The Company estimates the fair value of the contingent consideration at the end of each reporting period based on management's estimates of (i) the probability of achieving the relevant revenue targets and (ii) the timing of achieving such targets. In January 2020, based on the relevant revenues earned during the first year of the three-year contingent consideration period, the Company paid \$0.3 million to Azavea, Inc., resulting in a reduction of the contingent consideration liability.

The changes in the fair value of contingent consideration liability for 2020 and 2019 are as follows (in thousands):

	<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>
Balance, beginning of period	\$ 750	\$ 750
Payment of contingent consideration liability	(347)	—
Balance, end of period	<u>\$ 403</u>	<u>\$ 750</u>

Note 5. Details of Certain Condensed Consolidated Balance Sheet Accounts**Prepaid expenses and other current assets (in thousands):**

	September 30, 2020	December 31, 2019
Prepaid software and licenses	\$ 473	\$ 321
Prepaid insurance	887	473
Other prepaid expenses	111	94
Deferred commissions	735	753
Other	80	123
	<u>\$ 2,286</u>	<u>\$ 1,764</u>

Other assets (long-term) (in thousands):

	September 30, 2020	December 31, 2019
Deferred commissions	\$ 1,305	\$ 1,579
Other	38	55
	<u>\$ 1,343</u>	<u>\$ 1,634</u>

Accrued expenses and other current liabilities (in thousands):

	September 30, 2020	December 31, 2019
Personnel-related accruals	\$ 3,040	\$ 2,883
Royalties payable	36	115
Professional fees	286	317
Sales/ use tax payable	56	91
Contingent consideration liability	403	750
Operating lease liabilities	381	302
Other	39	427
	<u>\$ 4,241</u>	<u>\$ 4,885</u>

Other liabilities (long-term) (in thousands):

	September 30, 2020	December 31, 2019
Operating lease liabilities	\$ 427	\$ 297
Other	29	1
	<u>\$ 456</u>	<u>\$ 298</u>

Note 6. Related Party Transactions

During the three and nine months ended September 30, 2020, the Company recognized \$60,000 and \$0.2 million, respectively, in revenues from ShotSpotter Labs projects with charitable organizations that have received donations from one of the Company's directors and one of the Company's significant stockholders. During the three and nine months ended September 30, 2019, the Company recognized \$0.1 million and \$0.4 million in revenues, respectively, from those ShotSpotter Labs projects.

Note 7. Capital Stock

Common Stock

The Company is authorized to issue 500,000,000 shares of common stock, with a par value of \$0.005 and each outstanding share of common stock is entitled to one vote.

At September 30, 2020 and December 31, 2019, there were 11,441,762 and 11,314,150 shares of common stock issued and outstanding, respectively.

Preferred Stock

The Company is authorized to issue 20,000,000 shares of preferred stock, with a par value of \$0.005. At September 30, 2020, there were no shares of preferred stock issued and outstanding.

Stock Repurchase Program

In May 2019, the Company announced that its Board of Directors (the "Board") had approved a stock repurchase program for up to \$5 million of the Company's common stock. The shares may be repurchased from time to time in open market transactions, in privately negotiated transactions or by other methods in accordance with federal securities laws. The actual timing, number and value of shares repurchased under the program will be determined by management in its discretion and will depend on a number of factors, including the market price of the Company's common stock, general market and economic conditions and applicable legal requirements. The stock repurchase program does not obligate the Company to purchase any particular amount of common stock and may be modified, suspended or discontinued at any time.

During the nine months ended September 30, 2020, the Company repurchased 74,520 shares of its common stock at an average price of \$1.65 per share for \$1.6 million. During the nine months ended September 30, 2019, the Company repurchased 120,000 shares of its common stock at an average price of \$8.86 per share for \$3.5 million. The repurchases were made in open market transactions using cash on hand, and all of the shares repurchased were retired.

At September 30, 2020, \$6.7 million remained available of this \$15 million stock repurchase program.

Note 8. Net Income per Share

The computation of basic net income per share is based on the weighted-average number of shares of common stock outstanding during each period. The computation of diluted net income per share is based on the weighted-average number of shares outstanding during the period plus, when their effect is dilutive, incremental shares consisting of shares subject to stock options, restricted stock units, employee stock purchase plan purchase rights and warrants.

The following table summarizes the computation of basic and diluted net income per share (in thousands, except share and per share data):

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
Numerator:				
Net income	\$ 566	\$ 446	\$ 1,445	\$ 471
Denominator:				
Weighted-average shares outstanding, basic	11,423,079	11,449,946	11,383,860	11,275,195
Dilutive effect of common stock equivalents	304,033	608,004	334,910	670,975
Weighted-average shares outstanding, diluted	11,727,112	11,917,382	11,718,770	11,865,319
Net income per share, basic	\$ 0.05	\$ 0.04	\$ 0.13	\$ 0.04
Net income per share, diluted	\$ 0.05	\$ 0.04	\$ 0.12	\$ 0.04

Note 9. Common Stock Warrants

At September 30, 2020, the Company had the following common stock warrants issued and outstanding:

Warrant Class	Shares	Issuance Date	Price per Share	Expiration Date
Common stock warrant	50,716	February 2014	\$ 0.1700	February 2021

Note 10. Equity Incentive Plans

2017 Equity Incentive Plan

In May 2017, the Board and the Company's stockholders approved the 2017 Equity Incentive Plan (the "2017 Plan"), which became effective in connection with the Company's initial public offering of common stock ("IPO"). The 2017 Plan provides for the issuance of stock options, restricted stock units and other awards to employees, directors and consultants of the Company. A total of 2,413,659 shares of the Company's common stock were initially reserved for issuance under the 2017 Plan, which is the sum of (1) 900,000 shares, (2) the number of shares reserved for issuance under the 2005 Plan (as defined below) at the time the 2017 Plan became effective and (3) shares subject to stock options or other stock awards under the 2005 Plan that would have otherwise been returned to the 2005 Plan (up to a maximum of 1,314,752 shares). Under an "evergreen" provision, the number of shares of common stock reserved for issuance under the 2017 Plan will automatically increase on January 1 of each year, beginning on January 1, 2018 and ending on and including January 1, 2027, by 5% of the total number of shares of our capital stock outstanding on December 31 of the preceding calendar year or a lesser number of shares determined by the Board. In accordance with the evergreen provision, the number of shares of common stock reserved for issuance under the 2017 Plan was automatically increased on January 1, 2020 by 565,707 shares, which was equal to 5% of the total number of shares of capital stock outstanding on December 31, 2019.

2005 Stock Plan

In February 2005, the Company adopted the 2005 Stock Plan, as amended in January 2010 and November 2012 (the "2005 Plan"). Under the 2005 Plan provisions, the Company was authorized to grant incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock units, and shares of restricted stock.

Following the effectiveness of the 2017 Plan in connection with the IPO, no further grants were made under the 2005 Plan.

A summary of option activities under the 2005 Plan and 2017 Plan during the nine months ended September 30, 2020 is as follows:

	Number of Options Outstanding	Weighted Average Exercise Price
Outstanding as of December 31, 2019	617,493	\$ 17.13
Granted	244,979	\$ 31.81
Exercised	(84,670)	\$ 1.99
Canceled	(54,267)	\$ 25.95
Outstanding as of September 30, 2020	723,535	\$ 23.21

During the nine months ended September 30, 2020, the Company granted executive management restricted stock unit ("RSU") awards totaling 57,048 shares of common stock, with quarterly vesting over the next four years. The weighted average fair value of \$34.07 per unit was calculated using the closing stock price on the grant date. During the nine months ended September 30, 2020, RSU's totaling 2,247 shares of common stock were canceled.

During the nine months ended September 30, 2020, the Company granted directors RSU awards totaling 24,711 shares of common stock in accordance with the Company's non-employee director compensation policy. The weighted average fair value of \$25.90 per unit was calculated using the closing stock price on the grant date.

The number of shares available for grant under the 2017 Plan was 1,928,119 as of September 30, 2020.

2017 Employee Stock Purchase Plan

In May 2017, the Board and the Company's stockholders adopted the 2017 Employee Stock Purchase Plan ("2017 ESPP"), which became effective in connection with the Company's IPO. The 2017 ESPP allows eligible employees to purchase shares of the Company's common stock in an offering at a discount of the then-current trading price, up to the lesser of (1) 85% of the fair market value of the common stock on the first day of the IPO or (2) 85% of the fair market value of the common stock on the purchase date. The 2017 ESPP permits the maximum discounted purchase price permitted under U.S. tax rules, including a "lookback."

There were 200,000 shares of common stock initially reserved for issuance under the 2017 ESPP. In addition, the 2017 ESPP contains an "evergreen" provision which provides for an automatic annual share increase on January 1 of each year, in an amount equal to the lesser of (1) 2% of the total number of shares of common stock outstanding on December 31st of the preceding calendar year, (2) 150,000 shares or (3) such number of shares as determined by the Board. In accordance with the evergreen provision, the number of shares of common stock reserved for issuance under our 2017 ESPP was automatically increased on January 1, 2020 by 150,000 shares.

There were 21,431 shares issued under the 2017 ESPP during the nine months ended September 30, 2020. The number of shares available for grant under the 2017 ESPP was 445,192 as of September 30, 2020.

The Company accounts for employee stock purchases made under its 2017 ESPP using the estimated grant date fair value of accounting in accordance with ASC 718, *Stock Compensation*. The Company values ESPP shares using the Black-Scholes model.

Total stock-based compensation expense associated with the 2005 Plan, 2017 Plan and 2017 ESPP is recorded in the condensed consolidated statements of operations and was allocated as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Cost of revenues	\$ 292	\$ 125	\$ 788	\$ 472
Sales and marketing	344	173	925	712
Research and development	160	83	416	273
General and administrative	400	335	1,117	918
Total	<u>\$ 1,196</u>	<u>\$ 716</u>	<u>\$ 3,246</u>	<u>\$ 2,375</u>

Note 11. Leases

Operating Lease

The Company leases its principal executive offices in Newark, California, under a non-cancelable operating lease that expires in October 2021. This lease does not have significant rent escalation holidays, concessions, leasehold improvement incentives, or other build-out clauses. Further, the lease does not contain contingent rent provisions or renewal options. This lease includes both lease components (e.g., fixed payments including rent, taxes, and insurance costs) and non-lease components (e.g., common-area or other maintenance costs), which are accounted for as a single lease component as the Company has elected the practical expedient to group lease and non-lease components for all leases. Upon adoption of Topic 842 on January 1, 2019, the Company recognized an operating lease right-of-use asset of \$0.9 million and a corresponding lease liability of \$0.9 million, using a discount rate of 6%, which reflects the Company's incremental borrowing rate for a similar asset and similar term as of the date of adoption.

In April 2020, the Company executed a lease agreement for office space in Washington, DC, under a non-cancelable operating lease that expires in November 2025. This lease does not have significant rent escalation holidays, concessions, leasehold improvement incentives, or other build-out clauses. Further, the lease does not contain contingent rent provisions. The lease contains an option to extend the term for an additional five years subject to certain terms and conditions. This lease includes both lease components (e.g., fixed payments including rent, taxes, parking, and insurance costs) and non-lease components (e.g., common-area or other maintenance costs), which are accounted for as a single lease component as the Company has elected the practical expedient to group lease and non-lease components for all leases. Upon lease commencement on May 1, 2020, the Company recognized an operating lease right-of-use asset of \$0.5 million and a corresponding lease liability of \$0.5 million, using a discount rate of 3.85%, which reflects the Company's incremental borrowing rate for a similar asset and similar term as of the date of commencement.

The operating lease cost recognized for the three months ended September 30, 2020 and 2019 was \$0.1 million for each period. The operating lease cost recognized for the nine months ended September 30, 2020 and 2019 was \$0.3 million for each period.

Supplemental information related to the operating leases is as follows (in thousands):

	As of September 30, 2020	As of December 31, 2019
Assets		
Operating lease right-of-use assets	\$ 761	\$ 556
Liabilities		
Lease liabilities (short-term) <i>(presented within Accrued expenses and other current liabilities)</i>	\$ 381	\$ 302
Lease liabilities (long-term) <i>(presented within Other liabilities)</i>	427	297
Total operating lease liabilities	<u>\$ 808</u>	<u>\$ 599</u>
	<u>Nine months ended September 30, 2020</u>	<u>Nine months ended September 30, 2019</u>
Cash paid for amounts included in the measurement of lease liabilities <i>(presented within Cash flows from operating activities)</i>	\$ 274	\$ 259

Maturities of the lease liabilities at September 30, 2020 are as follows (in thousands):

2020 (remainder of year)	\$ 69
2021	402
2022	100
2023	102
2024	105
2025	90
Total lease payments, undiscounted	868
Less: imputed interest	(60)
Total	<u>\$ 808</u>

The Company does not have any finance leases.

Note 12. Commitments and Contingencies

The Company has non-cancelable data center arrangements in which the original term exceeds one year.

The following is a schedule of future minimum payments under the non-cancelable data center arrangements at September 30, 2020 (in thousands):

	Data Center Arrangements
2020 (remainder of year)	\$ 39
2021	117
2022	117
2023	39
Total	<u>\$ 312</u>

Contingencies

On August 28, 2018, Silvon S. Simmons (the "Plaintiff") amended a complaint against the City of Rochester, New York and various city employees, filed in the United States District Court, Western District of New York, to add the Company and employees as a defendant. The amended complaint alleges conspiracy to violate plaintiff's civil rights, denial of the right to a fair trial, and malicious prosecution. The Plaintiff claims that ShotSpotter colluded with the City of Rochester to fabricate and create gunshot alert evidence to secure Plaintiff's conviction. On the basis of the allegations, the Plaintiff has petitioned for compensatory and punitive damages and other costs and expenses, including attorney's fees. The Company believes that the Plaintiff's claims are without merit and is disputing them vigorously.

The Company may become subject to legal proceedings, as well as demands and claims that arise in the normal course of business. Such claims, even if not meritorious, could result in the expenditure of significant financial and management resources. The Company makes a provision for a liability relating to legal matters when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed and adjusted to include the impacts of negotiations, estimated settlements, legal rulings, advice of legal counsel, and other information and events pertaining to a particular matter.

An unfavorable outcome on any litigation matters could require payment of substantial damages, or, in connection with any intellectual property infringement claims, could require the Company to pay ongoing royalty payments or could prevent the Company from selling certain of our products. As a result, a settlement of, or an unfavorable outcome on, any of the matters referenced above or other litigation matters could have a material adverse effect on the Company's business, operating results, financial condition and cash flows.

The COVID-19 pandemic has resulted in a substantial curtailment of business activities worldwide and is causing weakened economic conditions, both in the United States and many countries abroad. As part of intensifying efforts to contain the spread of COVID-19, many companies and state, local and foreign governments have imposed restrictions, including shelter-in-place orders and travel bans. While some of these companies and jurisdictions have started to relax such restrictions, in some cases, the restrictions were put back in place after having been lifted. These factors have negatively impacted the Company's operations and results of operations for the first three quarters of 2020. The Company expects that the evolving COVID-19 pandemic, associated travel restrictions and social distancing requirements will continue to have an adverse impact on its results of operations. While the ultimate economic impact of the COVID-19 pandemic is highly uncertain, the Company expects that its business and results of operations, including its revenues, earnings and cash flows from operations, will be adversely impacted for at least the balance of 2020 and early 2021, including as a result:

- Delays in its ability to deploy new "go-live" miles attributable to company policies or customer policies designed to protect employee health in compliance with government restrictions;
- Greater funding challenges for its customer base, which may adversely affect customer contract renewals, expansion of existing customer deployments or new customer sales;
- Possible disruption to the Company's supply chain caused by distribution and other logistical issues, which may further delay its ability to deploy new go-live miles; and

- Potential decrease in productivity of its employees or that of its customers or suppliers due to travel bans or restrictions, work-from-home or shelter-in-place policies and orders.

The Company may be adversely affected by increasing social unrest, protests against racial inequality, protests against police brutality and movements such as “Defund the Police”. These events may directly or indirectly affect police agency budgets and funding available to current and potential customers. Participants in these events may also attempt to create the perception that the Company’s solutions are contributing to the “problem”, which may adversely affect the Company, its business and results of operations, including its revenues, earnings and cash flows from operations.

Note 13. Subsequent Events

On November 4, 2020, the Company entered into a definitive agreement to acquire 100% of the membership interests in LEEDS, LLC (“LEEDS”), a New Jersey-based technology company. The purchase consideration includes \$ 15.0 million in cash, \$ 2.0 million in issued stock and a contingent earnout payable in cash for up to \$ 5.0 million based on LEEDS’ revenues generated over a two-year period following the acquisition date. If the acquisition is completed, the Company will account for this acquisition as a business combination. The Company expects to use existing cash on hand to fund the acquisition.

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

You should read the following discussion and analysis of our financial condition and results of operations together with our unaudited condensed consolidated financial statements and accompanying notes included in this Quarterly Report on Form 10-Q and the financial statements and accompanying notes and other financial information in the Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's Annual Report on Form 10-K for the year ended December 31, 2019, filed with the Securities and Exchange Commission ("SEC") on March 13, 2020. This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Exchange Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements are often identified by the use of words such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "plan," "project," "will," "would" or the negative or plural of these words or similar expressions or variations. Such forward-looking statements are subject to a number of risks, uncertainties, assumptions and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified herein, those discussed in the subsection titled "Impact of COVID-19 and Social Unrest on our Business" below, as well as the section titled "Risk Factors" set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and in our other SEC filings. You should not rely upon forward-looking statements as predictions of future events. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We provide precision-policing and security solutions for law enforcement and security personnel to help prevent and reduce gun violence and make cities, campuses and facilities safer. Our flagship public safety solution, ShotSpotter Flex, is the leading outdoor gunshot detection, location and alerting system. Our patrol management software, ShotSpotter Connect (formerly ShotSpotter Missions), creates crime forecasts designed to enable more precise and effective use of patrol resources to deter crime. In 2019, we created a new technology innovation unit, ShotSpotter Labs, to expand our efforts supporting innovative uses of our technology to help protect wildlife and the environment. Our security solutions, ShotSpotter SecureCampus and ShotSpotter SiteSecure, are designed to help law enforcement and security personnel serving universities, corporate campuses and key infrastructure or transportation centers mitigate risk and enhance security by notifying authorities of a potential outdoor gunfire incident, saving critical minutes for first responders to arrive. Our gunshot detection solutions are trusted by law enforcement agencies in over 110 cities as of September 30, 2020.

Our gunshot detection solutions consist of highly-specialized, cloud-based software integrated with proprietary, internet-enabled sensors designed to detect outdoor gunfire. The speed and accuracy of our gunfire alerts enable law enforcement and security personnel to reduce their response times to shooting events, which can increase the chances of apprehending the shooter, providing timely aid to victims, and identifying witnesses before they scatter, as well as aid in evidentiary collection and serve as an overall deterrent. When a potential gunfire incident is detected by our sensors, our software precisely locates where the incident occurred and applies machine classification combined with human review by acoustic experts in our Incident Review Center ("IRC"), who are on duty 24 hours a day, seven days a week, every day of the year, to analyze and validate the incident. Our acoustic experts can supplement alerts with additional tactical information, such as the potential presence of multiple shooters or the use of high-capacity weapons. An alert containing a location on a map and additional tactical information about the incident is sent directly to subscribing law enforcement or security personnel through any internet-connected computer and to iPhone or Android mobile devices. Gunshot incident alerts are typically sent within 45 seconds of the receipt of the gunfire incident.

We generate annual subscription revenues from the deployment of ShotSpotter Flex on a per-square-mile basis. Our security solutions, ShotSpotter SecureCampus and ShotSpotter SiteSecure, are typically sold on a subscription basis, each with a customized deployment plan. Our ShotSpotter Connect solution is also sold on a subscription basis. As of September 30, 2020, we had ShotSpotter Flex, ShotSpotter SecureCampus and ShotSpotter SiteSecure coverage areas under contract for approximately 770 square miles, of which 758 square miles had gone live. Coverage areas under contract included 113 cities and 13 campuses/sites worldwide across the United States, South Africa and the Bahamas, including three of the ten largest cities in the United States. As a result of the COVID-19 pandemic, work-from-home and travel ban policies designed to protect the health of employees, and related government-mandated restrictions, our ability to deploy customer solutions since mid-March 2020 has been adversely impacted. While this disruption is currently expected to be temporary, there is considerable uncertainty around the magnitude or duration.

While we intend to continue to devote resources to increase sales of our ShotSpotter SecureCampus, ShotSpotter SiteSecure, ShotSpotter Labs and ShotSpotter Connect solutions, we expect that revenues from our ShotSpotter Flex solution will continue to comprise a substantial majority of our revenues for the foreseeable future. ShotSpotter Labs projects are generally conducted in coordination with a sponsoring charitable organization. These projects may or may not be revenue-producing. When they are revenue-producing, they will generally be sold on a cost-plus basis. As such, ShotSpotter Labs projects will normally produce gross margins significantly lower than our ShotSpotter Flex solutions. Additionally, in early 2020, we added new pricing programs for Tier 4 and 5 law enforcement agencies (those with fewer than 100 sworn officers) that allow them to contract for our gunshot detection solutions to cover a footprint of less than three square miles, using standardized coverage parameters, at a discounted annual subscription rate.

We enter into subscription agreements on a term basis that typically range from one to five years in duration, with the majority having a contract term of one year. Substantially all of our sales are to governmental agencies and universities, which often undertake a prolonged contract evaluation process that affects the size or the timing of our sales contracts and may likewise increase our customer acquisition costs.

We rely on a limited number of suppliers and contract manufacturers to produce components of our solutions. We have no long-term contracts with these manufacturers and purchase from them on a purchase-order basis. Our outsourced manufacturers generally procure the components directly from third-party suppliers. Although we use a limited number of suppliers and contract manufacturers, we believe that we could find alternate suppliers or manufacturers if circumstances required us to do so, in part because a significant portion of the components required by our solutions is available off the shelf.

We generated revenues of \$11.4 million and \$10.0 million for the three months ended September 30, 2020 and 2019, respectively, a year-over-year increase of 14%. Revenues from ShotSpotter Flex during the three months ended September 30, 2020 and 2019, represented approximately 97% and 96% of total revenues, respectively. Our two current largest customers, the City of Chicago and the City of New York, accounted for 18% and 13%, respectively, of our total revenues for the three months ended September 30, 2020, and 20% and 14%, respectively, of our total revenues for the three months ended September 30, 2019.

We generated revenues of \$33.1 million and \$29.8 million for the nine months ended September 30, 2020 and 2019, respectively, a year-over-year increase of 11%. Revenues from ShotSpotter Flex during the nine months ended September 30, 2020 and 2019, represented approximately 96% of total revenues for both periods. Our two current largest customers, the City of Chicago and the City of New York, accounted for 18% and 13%, respectively, of our total revenues for the nine months ended September 30, 2020, and 20% and 14%, respectively, of our total revenues for the nine months ended September 30, 2019.

For the three months ended September 30, 2020 and 2019, revenues generated within the United States accounted for \$11.2 million and \$9.8 million, respectively, or 98% of total revenues for the both periods, and \$0.2 million for both three months ended September 30, 2020 and 2019, and was derived from our customers located outside the United States.

For the nine months ended September 30, 2020 and 2019, revenues generated within the United States accounted for \$32.6 million and \$28.9 million, respectively, or 98% and 97%, respectively, of total revenues for the both periods, and \$0.5 million and \$0.9 million for the nine months ended September 30, 2020 and 2019, respectively, and was derived from our customers located outside the United States.

We had net income of \$0.6 million and \$0.4 million for the three months ended September 30, 2020 and 2019, respectively and a net income of \$1.4 million and \$0.5 million for the nine months ended September 30, 2020 and 2019, respectively. Our accumulated deficit was \$94.1 million and \$95.6 million at September 30, 2020 and December 31, 2019, respectively.

We have focused on rapidly growing our business and believe that its future growth is dependent on many factors, including our ability to increase our customer base, expand the coverage of our solutions among our existing customers, expand our international presence and increase sales of our security solutions. Our future growth will primarily depend on the market acceptance for outdoor gunshot detection solutions. The challenges we are facing in this regard as a result of the COVID-19 pandemic are summarized in the section below entitled “Impact of COVID-19 and Social Unrest on our Business.” Other challenges we face in this regard include our target customers not having access to adequate funding sources, the fact that contracting with government entities can be complex, expensive, and time-consuming and the fact that our typical sales cycle is often very long, difficult to estimate accurately and can be costly. We expect international sales cycles to be even longer than our domestic sales cycles. To combat these challenges, we invest in research and development, increase awareness of our solutions, invest in new sales and marketing campaigns, often in different languages for international sales, and hire additional sales representatives to drive sales in order to continue to maintain our position as a market leader. In addition, we believe that entering into strategic partnerships with other service providers to cities and municipalities offers another potential avenue for expansion, particularly for our ShotSpotter Flex solution.

We will also focus on expanding our business by introducing new products and services to existing customers such as ShotSpotter Connect and gaining new customers for ShotSpotter Labs. We believe that developing and acquiring products for law enforcement in adjacent categories is a path for additional growth given our large and growing installed base of police departments who trust ShotSpotter’s products, support and way of doing business. The ability to cross-sell new products provides an opportunity to grow revenues per customer and lifetime value. Challenges we face in this area include ensuring our new products are reliable, integrated well with other ShotSpotter solutions and priced and serviced appropriately. In some cases, we will need to bring in new skills sets to properly develop, market, sell or service these new products depending on the categories they represent.

In October 2018, we acquired the HunchLab technology and related assets that underline our ShotSpotter Connect solution. ShotSpotter Connect applies risk modeling and artificial intelligence to help forecast when and where crimes are likely to emerge and recommends directed patrols that can deter these events. HunchLab technology provides a high-value and complementary solution we can immediately offer to our existing law enforcement customers. We believe our investment will democratize the sharing of important intelligence with patrol officers who currently have limited direct access to crime analysts.

With respect to international sales, we believe that we have the potential to expand our coverage within existing areas, and to pursue opportunities in Latin America and other regions of the world. By adding additional sales resources in strategic locations, we believe we will be better positioned to reach these markets. However, we recognize that we have limited international operational experience and currently operate in a limited number of regions outside of the United States. Operating successfully in international markets will require significant resources and management attention and will subject us to additional regulatory, economic and political risks. We may face additional challenges that may delay contract execution related to negotiating with governments in transition, the use of third-party integrations and consultants. Moreover, we anticipate that different political and regulatory considerations that vary across different jurisdictions could extend or make more difficult to predict the length of what is already a lengthy sales cycle.

On November 4, 2020, the Company entered into a definitive agreement to acquire 100% of the membership interests in LEEDS, LLC (“LEEDS”), a New Jersey-based technology company. The purchase consideration includes \$15.0 million in cash, \$2.0 million in issued stock and a contingent earnout payable in cash for up to \$5.0 million based on LEEDS’ revenues generated over a two-year period following the acquisition date. If the acquisition is completed, the Company will account for this acquisition as a business combination. The Company expects to use existing cash on hand to fund the acquisition.

Net New “Go-Live” Square Miles

Net new “go-live” square miles represent the square miles covered by deployments of our gunshot detection solutions that were formally approved by customers during the quarter, both from initial and expanded customer deployments, net of square miles that ceased to be “live” during the quarter due to customer cancellations. New square miles include deployed square miles that may have been sold, or booked, in prior quarters. We focus on net new “go-live” square miles as a key business metric to measure our operational performance and inform strategic decisions. The net new “go-live” square miles during the nine months ended September 30, 2020 included the completion of our

deployment in Puerto Rico and Nelson Mandela Bay. It is also net of seven miles lost due to our loss of two customers and a coverage area reduction of three miles for one of our customers.

This metric, presented below for the three and nine months ended September 30, 2020 and 2019, is calculated on a quarterly basis using internal data, and may be calculated in a manner different than similar metrics used by other companies. While the ultimate economic impact of the COVID-19 pandemic and social unrest is highly uncertain, we expect that our business will be adversely impacted for at least the balance of 2020. For a discussion of the risks to our ability to deploy new “go-live” square miles associated with the COVID-19 pandemic and social unrest, see “Impact of COVID-19 and Social Unrest on our Business” below, as well as in the risk factors described in Part II, Item 1A, Risk Factors, included in this Quarterly Report on Form 10-Q.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Net new "go-live" square miles added	(3)	11	28	48

Impact of COVID-19 and Social Unrest on our Business

The COVID-19 pandemic has resulted in a substantial curtailment of business activities worldwide and is causing weakened economic conditions, both in the United States and many countries abroad. As part of intensifying efforts to contain the spread of COVID-19, many companies and state, local and foreign governments have imposed restrictions, including shelter-in-place orders and travel bans. While some of these companies and jurisdictions have started to relax such restrictions, in some cases, the restrictions were put back in place after having been lifted. These factors have negatively impacted our operations and results of operations for the first three quarters of 2020. We expect that the evolving COVID-19 pandemic, associated travel restrictions and social distancing requirements will continue to have an adverse impact on our results of operations. While the ultimate economic impact of the COVID-19 pandemic is highly uncertain, we expect that our business and results of operations, including our revenues, earnings and cash flows from operations, will be adversely impacted for at least the balance of 2020 and early 2021, including as a result of:

- Delays in our ability to deploy new “go-live” miles attributable to company policies or customer policies designed to protect employee health and comply with government restrictions;
- Greater funding challenges for our customer base, which may adversely affect customer contract renewals, expansion of existing customer deployments or new customer sales;
- Possible disruption to our supply chain caused by distribution and other logistical issues, which may further delay our ability to deploy new go-live miles; and
- Potential decrease in productivity of our employees or these of our customers or suppliers due to travel bans or restrictions, work-from-home or shelter-in-place policies and orders.

We may be adversely affected by increasing social unrest, protests against racial inequality, protests against police brutality and movements such as “Defund the Police”. These events may directly or indirectly affect police agency budgets and funding available to current and potential customers. Participants in these events may also attempt to create the perception that our solutions are contributing to the perceived problems, which may adversely affect us, our business and results of operations, including our revenues, earnings and cash flows from operations.

It is currently not possible to predict the magnitude or duration of the COVID-19 pandemic’s impact on our business or the future impact of the recent, ongoing and possible future unrest. The extent to which these events impact our business will depend on numerous evolving factors that we may not be able to control or accurately predict, including without limitation:

- the duration and scope of the challenges created by pandemic or by ongoing social unrest;
- governmental, business and individuals’ actions that have been and continue to be taken in response to these events;

- the impact of the pandemic and social unrest on economic activity and actions taken in response;
- the effect on our customers and demand for our products and services;
- our ability to continue to sell our products and services, including as a result of travel restrictions and people working from home, or restrictions on access to our potential customers;
- the ability of our customers to pay for our products and services;
- any closures of our facilities and the facilities of our customers and suppliers; and
- the degree to which our employees or those of our customers or suppliers become ill with COVID-19.

Components of Results of Operations

Revenues

We derive substantially all of our revenues from subscription services. We recognize subscription fees ratably, on a straight-line basis, over the term of the subscription, which for new customers is typically initially one to three years in length. Customer contracts include one-time set-up fees for the set-up of our sensors in the customer's coverage areas, training and third-party integration licenses. If the set-up fees are deemed to be a material right, they are recognized ratably over three to five years. Training and third-party integration license fees are recognized upon delivery.

For ShotSpotter Flex, we generally invoice customers for 50% of the total contract value when the contract is fully executed and for the remaining 50% when the subscription service is operational and ready to go live – that is, when the customer has acknowledged the completion of all the deliverables in the signed customer acceptance form. All fees billed in advance of services being delivered are recorded as deferred revenue. The timing of when new miles go live can be uncertain and, as a result, can have a significant impact on the levels of revenues and deferred revenue from quarter to quarter. For our ShotSpotter Flex solution, our pricing model is based on a per-square-mile basis. For ShotSpotter SecureCampus and ShotSpotter SiteSecure, our pricing model is on a customized-site basis. For our ShotSpotter Connect solution, pricing is currently customized, generally tied to the number of sworn police officers in a particular city. We may also offer discounts or other incentives in conjunction with ShotSpotter Connect sales in an effort to introduce the product and accelerate sales. As a result of our process for invoicing contracts and renewals upon execution, our cash flow from operations and accounts receivable can fluctuate due to timing of contract execution and timing of deployment.

We generally invoice subscription service renewals for 100% of the total contract value when the renewal contract is executed. Renewal fees are recognized ratably over the term of the renewal, which is typically one year. While most of our customers elect to renew their agreements, in some cases, they may not be able to obtain the proper approvals or funding to complete the renewal prior to expiration. For these customers, we stop recognizing subscription revenues at the end of the current contract term, even though we may continue to provide services for a period of time until the renewal process is completed. Once the renewal is complete, we then recognize subscription revenues for the period between the expiration of the term of the agreement and the completion of the renewal process in the month in which the renewal is executed. If a customer declines to renew its subscription prior to the end of three years, then the remaining setup fees are immediately recognized.

It is likely that international deployments may have different payment and billing terms due to their local laws, restrictions or other customary terms and conditions.

ShotSpotter Labs projects may or may not be revenue-producing. When they are revenue-producing, they will generally be sold on a cost-plus basis.

We anticipate that, due to the ongoing COVID-19 pandemic, our customers may be facing budget shortfalls due to the increased expenditures our customers have had to endure to address the pandemic, as well as the anticipated significant tax revenue declines resulting from the economic impact that the pandemic has rapidly generated in the first nine months of 2020, the duration of which is unknown.

Costs

Costs include the cost of revenues. Cost of revenues primarily includes depreciation expense associated with capitalized customer acoustic sensor networks, communication expenses, costs related to hosting our service applications, costs related to operating our IRC, providing remote and on-site customer support and maintenance and forensic services, providing customer training and onboarding services, certain personnel and related costs of operations, stock-based compensation and allocated overheads, which includes information technology, facility and equipment depreciation costs.

We will have to upgrade our sensors that use third-generation (“3G”) cellular communications to the fourth-generation Long-Term Evolution wireless technology, which will increase our cost of revenues. Originally, we had expected to start incurring these upgrade costs in 2021 through 2022. We have begun plans to replace sensors in certain geographic areas starting in the second half of 2020 in order to optimize personnel utilization. Accelerated bandwidth changes by our carriers may require us to continue to accelerate the upgrade of our 3G sensors prior to 2022, which would accelerate the costs associated with the upgrade, which are estimated to be between \$4.0 million and \$6.0 million in total. We may re-use and re-deploy the old 3G sensors that have a remaining serviceable life where it makes sense to do so.

In the near term, we expect our cost of revenues to increase in absolute dollars as our installed base increases, although certain of our costs of revenues are fixed and do not need to increase commensurate with increases in revenues. In addition, depreciation expense associated with deployed equipment is recognized over the first five years from the go-live date. We also expect cost of revenues to increase in absolute dollars as we continue to invest in our customer success capabilities to drive growth and value for our customers. As we expect to build out these capabilities in 2020, even while our ability to deploy new go-live miles is significantly impacted as a result of the COVID-19 pandemic, depending on the timing of new bookings, cost of revenues is expected to increase as a percentage of revenues.

Operating Expenses

Operating expenses consist of sales and marketing, research and development, and general and administrative expenses. Salaries, bonuses, stock-based compensation expense and other personnel costs are the most significant components of each of these expense categories. We include stock-based compensation expense incurred in connection with the grant of stock options and restricted stock units to the applicable operating expense category based on the equity award recipient’s functional area.

Sales and Marketing

Sales and marketing expenses primarily consist of personnel-related costs attributable to our sales and marketing personnel, commissions earned by our sales personnel, marketing expenses for trade shows, conferences and conventions, consulting fees, travel and facility-related costs and allocated overhead.

During the duration of the COVID-19 pandemic and associated shelter-in-place orders, work-from-home policies and travel bans, our sales and marketing expense has decreased and is expected to remain relatively flat as the pandemic continues. Thereafter, in the near term, we expect our sales and marketing expenses to increase in absolute dollars primarily due to planned growth in our sales and marketing organization. This growth may include adding sales and/or marketing personnel and expanding our marketing activities to continue to generate additional leads. Sales and marketing expense may fluctuate from quarter to quarter based on the timing of commission expense, marketing campaigns and tradeshow.

Research and Development

Research and development expenses primarily consist of personnel-related costs attributable to our research and development personnel, consulting fees and allocated overhead. We have devoted our product development efforts primarily to develop new lower-cost sensor hardware, develop new features, improve functionality of our solutions and adapt to new technologies or changes to existing technologies.

We are investing in engineering resources to support further development of ShotSpotter Connect. The focus of this effort will be in the areas of data science modeling, user experience, core application functionality and backend infrastructure improvements, including integration of ShotSpotter gunshot data to enhance forecasting of gun violence.

We are also investing research and development resources in conjunction with our ShotSpotter Labs projects and initiatives. The initial focus of these efforts is to develop innovative sensor applications as well as to test and expand the functionality of our outdoor sensors in challenging environmental conditions.

In the near term, we expect our research and development expenses to increase in absolute dollars as we increase our research and development headcount to further strengthen our software and invest in the development of our service.

We will continue to invest in research and development to leverage our large and growing database of acoustic events, which includes those from both gunfire and non-gunfire. We also intend to leverage third-party AI and our own evolving cognitive and analytical applications to improve the efficiency of our solutions. Certain of these applications and outputs may expand the platform of services that we will be able to offer our customers.

General and Administrative

General and administrative expenses primarily consist of personnel-related costs attributable to our executive, finance, and administrative personnel, legal, accounting and other professional services fees, other corporate expenses and allocated overhead.

In the near term, we expect our general and administrative expenses to increase in absolute dollars as we grow our business.

Other Income (Expense), Net

Other income (expense), net, consisted primarily of interest income and local and franchise tax expenses.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable.

We continually monitor all positive and negative evidence regarding the realization of our deferred tax assets and may record assets when it becomes more likely than not, than they will be realized.

Results of Operations

Comparison of Three Months Ended September 30, 2020 and 2019

The following table sets forth our selected condensed consolidated statements of operations data for the three months ended September 30, 2020 and 2019 (in thousands):

	Three Months Ended September 30,				Change	
	2020	As a % of Revenues	2019	As a % of Revenues	\$	%
Revenues	\$ 11,350	100 %	\$ 9,984	100 %	\$ 1,366	14 %
Costs						
Cost of revenues	4,745	42 %	4,019	40 %	726	18 %
Impairment of property and equipment	161	1 %	—	—	161	—
Total costs	4,906	43 %	4,019	40 %	887	22 %
Gross profit	6,444	57 %	5,965	60 %	479	8 %
Operating expenses:						
Sales and marketing	2,400	21 %	2,426	24 %	(26)	(1) %
Research and development	1,375	12 %	1,358	14 %	17	1 %
General and administrative	2,040	18 %	1,803	18 %	237	13 %
Total operating expenses	5,815	51 %	5,587	56 %	228	4 %
Operating income	629	6 %	378	4 %	251	66 %
Other income (expense), net	(55)	—	61	1 %	(116)	(190) %
Provision (benefit) for income taxes	8	—	(7)	—	15	(214) %
Net income	\$ 566	5 %	\$ 446	4 %	\$ 120	27 %

Revenues

The increase of \$1.4 million was primarily attributable to new customers and expansions of existing customer coverage areas, partially offset by a normal rate of customer attrition as well as the effect of COVID-19 related delays in deploying contracted miles and contract renewals with certain customer. We went live with 62 net new square miles since September 30, 2019.

Costs

The increase of \$0.9 million was due primarily to a \$0.6 million increase in overall personnel-related costs and a reallocation of certain resources as we formalized our customer success organization as well as a \$0.2 million increase in repairs and maintenance costs. There was also a \$0.2 million write-off related to sensor assets due to the loss of a customer. These increases are partially offset by a \$0.1 million decrease in costs related to ShotSpotter Labs projects, for which revenues and costs vary from quarter to quarter depending on the phase of the projects.

Operating Expenses

Sales and Marketing Expense

Sales and marketing expense remained relatively unchanged, because while we have added more personnel and expanded our marketing activities, we have also reallocated certain resources as part of the formalization of our customer success organization beginning in the first quarter of 2020, thus impacting cost of revenues. Sales and marketing activity was also lower in the third quarter of 2020 because of the curtailment of business activities and travel restrictions due to the COVID-19 pandemic.

Research and Development Expense

The expenses remained relatively unchanged due to the increased personnel-related costs offset by a reduction in outside consulting fees.

General and Administrative Expense

The increase of \$0.2 million was due primarily to an increase in personnel-related costs and insurance costs.

Other Income, Net

The decrease of \$0.1 million was due primarily to a decrease in interest income as interest rates have significantly decreased over the third quarter.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable. For the three months ended September 30, 2020 and 2019, due to having net operating loss carryforwards, our recorded income taxes consisted of foreign taxes only.

We continually monitor all positive and negative evidence regarding the realization of our deferred tax assets and may record assets when it becomes more likely than not, than they will be realized.

Comparison of Nine Months Ended September 30, 2020 and 2019

The following table sets forth our selected condensed consolidated statements of operations data for the nine months ended September 30, 2020 and 2019 (in thousands):

	Nine Months Ended September 30,				Change	
	2020	As a % of Revenues	2019	As a % of Revenues	\$	%
Revenues	\$ 33,085	100 %	\$ 29,837	100 %	\$ 3,248	11 %
Costs						
Cost of revenues	13,440	41 %	12,300	41 %	1,140	9 %
Impairment of property and equipment	161	—	—	—	161	—
Total costs	13,601	41 %	12,300	41 %	1,301	11 %
Gross profit	19,484	59 %	17,537	59 %	1,947	11 %
Operating expenses:						
Sales and marketing	7,237	22 %	7,494	25 %	(257)	(3) %
Research and development	4,104	12 %	4,026	13 %	78	2 %
General and administrative	6,627	20 %	5,669	19 %	958	17 %
Total operating expenses	17,968	54 %	17,189	58 %	779	5 %
Operating income	1,516	5 %	348	—	1,168	336 %
Other income (expense), net	(72)	—	156	—	(228)	(146) %
Provision (benefit) for income taxes	(1)	—	33	—	(34)	(103) %
Net income	\$ 1,445	4 %	\$ 471	\$ —	\$ 974	207 %

Revenues

The increase of \$3.2 million was primarily attributable to new customers and expansions of existing customer coverage areas, partially offset by a normal rate of customer attrition as well as COVID-19 related delays renewals of certain customers. We went live with 62 net new square miles since September 30, 2019.

Costs

The increase of \$1.3 million was due primarily to an increase of \$1.1 million related to personnel-related costs as well as a reallocation of certain resources as we formalized our customer success organization. In addition, there was a \$0.2 million increase in repairs and maintenance, a \$0.2 million write-off related to sensor assets due to the loss of a customer, a \$0.2 million increase in depreciation due to 62 net new square miles having gone live since September 30, 2019. These increases were partially offset by a \$0.3 million decrease in ShotSpotter Labs projects and a \$0.2 million decrease from the more efficient use of third-party labor.

Operating Expenses

Sales and Marketing Expense

Sales and marketing expense decreased by \$0.3 million because while we have added more personnel and expanded our marketing activities, we have also reallocated certain resources as part of the formalization of our customer success organization beginning in the first quarter of 2020, thus impacting cost of revenues. Sales and marketing activity also slowed in the second and third quarters of 2020 because of the curtailment of business activities and travel restrictions due to the COVID-19 pandemic.

Research and Development Expense

The expenses remained flat due to increased personnel-related costs offset by a reduction in outside consulting fees.

General and Administrative Expense

The increase of \$1.0 million was due primarily to \$0.4 million increase in personnel-related costs, \$0.3 million increase in cost of business insurance, \$0.1 million increase in legal expenses, \$0.1 million increase in equipment and software and \$0.1 million in consulting fees.

Other Income, Net

The decrease of \$0.2 million was due primarily to a decrease in interest income as interest rates have significantly decreased in response to the COVID-19 pandemic.

Income Taxes

Our income taxes are based on the amount of our taxable income and enacted federal, state and foreign tax rates, adjusted for allowable credits, deductions and the valuations allowance against deferred tax assets, as applicable. For the nine months ended September 30, 2020 and 2019, due to having net operating loss carryforwards, our recorded income taxes consisted of foreign taxes only.

We continually monitor all positive and negative evidence regarding the realization of our deferred tax assets and may record assets when it becomes more likely than not, than they will be realized.

Liquidity and Capital Resources

Sources of Funds

Our operations have been financed primarily through net proceeds from the sale of equity, debt financing arrangements and cash from operating activities. Our principal source of liquidity is cash and cash equivalents totaling \$28.7 million as of September 30, 2020. In August 2020, we entered into an amendment to our credit facility to increase the size of our available loan facility from \$10.0 million to \$20.0 million. As of September 30, 2020, no amounts were outstanding as of September 30, 2020.

In March 2019, we issued and sold 250,000 shares of our common stock in an underwritten public offering, for which we received net proceeds of \$10.6 million after deducting offering expenses.

We believe our existing cash and cash equivalent balances, our available credit facility and cash flow from operations will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months. Our future capital requirements may vary materially from those currently planned and will depend on many factors, including our rate of revenue growth, the timing and extent of spending on sales and marketing, the expansion of sales and marketing activities, the timing of new product introductions, market acceptance of our products and overall economic conditions. We may also seek additional capital to fund our operations, including through the sale of equity or debt financings. To the extent that we raise additional capital through the future sale of equity, the ownership interest of our stockholders will be diluted, and the terms of these securities may include liquidation or other preferences that adversely affect the rights of our existing common stockholders. The incurrence of debt financing would result in debt service obligations and the instruments governing such debt could provide for operating and financing covenants that would restrict our operations.

Use of Funds

Our historical uses of cash have primarily consisted of cash used for operating activities, such as expansion of our sales and marketing operations, research and development activities and other working capital needs, and cash used in investing activities, such as property and equipment expenditures to install infrastructure in customer cities in order to deliver our solutions. We also invest in company and technology acquisitions, where appropriate.

Stock Repurchase Program

In May 2019, we announced that our board of directors had approved a stock repurchase program for up to \$15 million of our common stock. The shares may be repurchased from time to time in open market transactions, in privately negotiated transactions or by other methods in accordance with federal securities laws. The actual timing, number and value of shares repurchased under the program will be determined by management in its discretion and will depend on a number of factors, including the market price of our common stock, general market and economic conditions and applicable legal requirements. The stock repurchase program does not obligate us to purchase any particular amount of common stock and may be suspended or discontinued at any time.

During the three months ended September 30, 2020, the Company did not repurchase any shares of its common stock. During the nine months ended September 30, 2020, the Company repurchased 74,520 shares of its common stock at an average price of \$21.65 per share for \$1.6 million. At September 30, 2020, \$6.7 million remained of this \$15 million stock repurchase program. During the year ended December 31, 2019, we repurchased 257,824 shares of our common stock at an average price of \$26 per share for \$6.7 million. The repurchases were made in open market transactions using cash on hand, and all of the shares repurchased were retired.

Cash Flows

Comparison of the Nine Months Ended September 30, 2020 and 2019

The following table presents a summary of our cash flows for the nine months ended September 30, 2020 and 2019:

	<u>September 30,</u>	
	<u>2020</u>	<u>2019</u>
	<u>(in thousands)</u>	
Net cash provided by (used in):		
Operating activities	\$ 8,809	\$ 11,151
Investing activities	(3,178)	(3,731)
Financing activities	(1,391)	8,492
Net change in cash and cash equivalents	<u>\$ 4,240</u>	<u>\$ 15,912</u>

Operating Activities

For standard customer deployments, we typically achieve cash flow breakeven, on a direct variable cost-basis, in less than a year from the date of execution of the contract. Our net income and cash flows provided by operating activities are significantly influenced by our ability to recognize deferred revenue by deploying new “go-live” miles, our

ability to bill and collect in a timely manner, and our planned increases in headcount and operating expenses to support our growth.

Net cash provided by operating activities decreased \$2.3 million from the nine months ended September 30, 2019 to the nine months ended September 30, 2020 primarily due to a \$1.8 million decrease in cash collected from customers, driven by the timing of executing contracts and renewals, which impacted the timing of billings and collections and \$0.5 million increase in payments including insurance and software subscriptions.

Investing Activities

Our investing activities consist primarily of capital expenditures to install our solutions in customer coverage areas, purchases of property and equipment, and investment in intangible assets.

Investing activities used \$3.2 million and \$3.7 million in the nine months ended September 30, 2020 and 2019, respectively, primarily for property and equipment installed for our solutions in customer coverage areas.

Financing Activities

Cash generated by financing activities includes proceeds from our follow-on offering in 2019, net proceeds from the exercise of stock options and warrants, proceeds from the employee stock purchase plan, offset by payment for repurchases of our common stock, payment of indebtedness, and debt issuance and financing costs.

Financing activities used \$1.4 million during the nine months ended September 30, 2020, mainly due to \$1.6 million paid for the share repurchases and \$0.3 million for the payment of contingent consideration liability to Azavea, Inc. in connection with the purchase of ShotSpotter Connect partially offset by the \$0.4 million proceeds from the ESPP purchase during the nine months ended September 30, 2020.

Financing activities provided \$8.5 million in cash during the nine months ended September 30, 2019 from \$11.2 million in proceeds from the issuance of common stock upon our secondary offering, \$0.6 million from ESPP purchase and \$0.5 million in proceeds from the exercise of options and warrants, partially offset by \$3.5 million in payments for repurchases of our common stock and \$0.4 million in payments related to secondary offering costs.

Off-Balance Sheet Arrangements

At September 30, 2020, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities that were established for the purpose of facilitating off-balance sheet arrangements. We do not engage in off-balance sheet financing arrangements. In addition, we do not engage in trading activities involving non-exchange traded contracts.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles. The preparation of our consolidated financial statements requires us to make estimates, assumptions and judgments that affect the reported amounts of revenues, assets, liabilities, costs and expenses. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates.

For the significant or material changes in our critical accounting policies during the nine months ended September 30, 2020, see Note 2, *Summary of Significant Accounting Policies*, to the notes of our condensed consolidated financial statements included in this Quarterly Report on Form 10-Q.

Recently Issued Accounting Pronouncements

See Note 2, *Summary of Significant Accounting Policies*, to the notes to our condensed consolidated financial statements included in this Quarterly Report on Form 10-Q for a summary of recently issued accounting pronouncements.

Item 3. Qualitative and Quantitative 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 the result of fluctuations in interest rates and foreign exchange rates as well as, to a lesser extent, inflation.

There were no material changes in our market risk during the nine months ended September 30, 2020, compared to the market risk disclosed in the Qualitative and Quantitative Disclosures about Market Risk section of our 2019 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management has evaluated, under the supervision and with the participation of our Chief Executive Officer and Interim Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13-a-15(e) and 15d-15(e)) as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Interim Chief Financial Officer have concluded that as of September 30, 2020, our disclosure controls and procedures were effective to provide reasonable assurance that the information we are required to file or submit under the Exchange Act 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 our management, including our Chief Executive Officer and Interim Chief Financial Officer, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the quarter ended September 30, 2020 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including our principal executive officer and principal financial officer, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

Item 1A. RISK FACTORS

Summary of Risk Factors

Our business is subject to numerous risks and uncertainties, discussed in more detail in the following section. These risks include, among others, the following key risks:

- The COVID-19 pandemic has resulted in a material adverse effect on our business, the future magnitude or duration of which we cannot predict with accuracy.
- Ongoing social unrest may result in a material adverse effect on our business, the future magnitude or duration of which we cannot predict with accuracy.
- Our success depends on maintaining and increasing our sales, which depends on factors we cannot control, including the availability of funding to our customers.
- Contracting with government entities can be complex, expensive and time-consuming.
- If we are unable to maintain and expand coverage of our existing public safety customer accounts and further penetrate the public safety market, our revenues may not grow.
- If we are unable to sell our solutions into new markets, our revenues may not grow.
- Our sales cycle can be lengthy, time-consuming and costly, and our inability to successfully complete sales could harm our business.
- Changes in the availability of federal funding to support local law enforcement efforts could impact our business.
- If our business does not grow as we expect, or if we fail to manage our growth effectively, our operating results and business prospects would suffer.
- The failure of our solutions to meet our customers' expectations could harm our reputation, which may have a material adverse effect on our business, operating results and financial condition.
- Interruptions or performance problems associated with our technology and infrastructure may adversely affect our business and results of operations.
- Real or perceived false positive gunshot alerts or failure or perceived failure to generate alerts for actual gunfire could adversely affect our customers and their operations, damage our brand and reputation and adversely affect our growth prospects and results of operations.
- We may require additional capital to fund our business and support our growth, and our inability to generate and obtain such capital on acceptable terms, or at all, could harm our business, operating results, financial condition and prospects.
- Our strategy includes pursuing acquisitions, including our current planned acquisition of Leeds, LLC, and our inability to successfully integrate newly-acquired technologies, assets or businesses may harm our financial results. Future acquisitions of technologies, assets or businesses, which are paid for partially or entirely through the issuance of stock or stock rights, could dilute the ownership of our existing stockholders.
- The nature of our business exposes us to inherent liability risks.
- The nature of our business may result in undesirable press coverage or other negative publicity.
- Failure to protect our intellectual property rights could adversely affect our business.
- Our stock price may be volatile or may decline regardless of our operating performance, resulting in substantial losses for investors.

Risks Related to Our Business and Industry

The COVID-19 pandemic has resulted in a material adverse effect on our business, the future magnitude or duration of which we cannot predict with accuracy.

The COVID-19 pandemic has resulted in a substantial curtailment of business activities worldwide and is causing weakened economic conditions, both in the United States and many countries abroad. As part of intensifying efforts to contain the spread of COVID-19, many companies and state, local and foreign governments have imposed restrictions, including shelter-in-place orders and travel bans. While some of these companies and jurisdictions have started to relax such restrictions, in some cases, the restrictions were put back in place shortly after having been

lifted. These factors have negatively impacted the Company's operations and results of operations for the first three quarters of 2020. The Company expects that the evolving COVID-19 pandemic, associated travel restrictions and social distancing requirements will continue to have an adverse impact on its results of operations. While the ultimate economic impact of the COVID-19 pandemic is highly uncertain, the Company expects that its business and results of operations, including its revenues, earnings and cash flows from operations, will be adversely impacted for at least the balance of 2020 and early 2021, including as a result of:

- Delays in its ability to deploy new "go-live" miles attributable to company policies or customer policies designed to protect employee health and comply with government restrictions;
- Greater funding challenges for its customer base, which may adversely affect customer contract renewals, expansion of existing customer deployments or new customer sales;
- Possible disruption to the Company's supply chain caused by distribution and other logistical issues, which may further delay its ability to deploy new go-live miles; and
- Potential decrease in productivity of its employees or that of its customers or suppliers due to travel bans or restrictions, work-from-home or shelter-in-place policies and orders.

It is currently not possible to predict the magnitude or duration of the COVID-19 pandemic's impact on our business. The extent to which the COVID-19 pandemic impacts our business will depend on numerous evolving factors that we may not be able to control or accurately predict, including without limitation:

- the duration and scope of the pandemic;
- governmental, business and individuals' actions that have been and continue to be taken in response to the pandemic;
- the impact of the pandemic on economic activity and actions taken in response;
- the effect on our customers and demand for our products and services;
- our ability to continue to sell our products and services, including as a result of travel restrictions and people working from home, or restrictions on access to our potential customers;
- the ability of our customers to pay for its products and services;
- any closures of our facilities and the facilities of our customers and suppliers; and
- the degree to which our employees or those of our customers or suppliers become ill with COVID-19.

Ongoing social unrest may result in a material adverse effect on our business, the future magnitude or duration of which we cannot predict with accuracy.

The Company may be adversely affected by ongoing social unrest, protests against racial inequality, protests against police brutality and movements such as "Defund the Police" or increases in such unrest that may occur in the future. These events may directly or indirectly affect police agency budgets and funding available to current and potential customers. Participants in these events may also attempt to create the perception that our solutions are contributing to the "problem", which may adversely affect the Company, its business and results of operations, including its revenues, earnings and cash flows from operations.

Our success depends on maintaining and increasing our sales, which depends on factors we cannot control, including the availability of funding to our customers.

To date, substantially all of our revenues have been derived from contracts with local governments and their agencies, in particular the police departments of major cities in the United States. To a lesser extent, we also generate revenues from federal agencies, foreign governments and higher education institutions. We believe that the success and growth of our business will continue to depend on our ability to add new police departments and other government agencies, domestically and internationally, as customers of our public safety solution and new universities, corporate campuses and key infrastructure and transportation centers as customers of our security solutions. Many of our target customers have restricted budgets, such that we are forced to compete with programs or solutions that offer an

alternative use of the same funds. A number of factors could cause current and/or potential customers to: delay or refrain from purchasing our solutions, prevent expansion of, or reduce coverage areas and/ or terminate use of our solutions, including:

- decreases or changes in available funding, including tax revenues, budgetary allocations, government grants and other government funding programs;
- potential delays or changes in appropriations or other funding authorization processes;
- changes in fiscal or contracting policies;
- macro-and/or local economic changes that may affect customer funding;
- changes in elected or appointed officials; and
- changes in laws or public sentiment regarding privacy or surveillance.

The COVID-19 pandemic and any associated impact on economic conditions could also cause or exacerbate any of the foregoing. The occurrence of any of the foregoing would impede or delay our ability to maintain or increase the amount of revenues derived from these customers, which could have a material adverse effect on our business, operating results and financial condition.

Contracting with government entities can be complex, expensive and time-consuming.

The procurement process for government entities is in many ways more challenging than contracting in the private sector. We must comply with laws and regulations relating to the formation, administration, performance and pricing of contracts with government entities, including U.S. federal, state and local governmental bodies. These laws and regulations may impose added costs on our business or prolong or complicate our sales efforts, and failure to comply with these laws and regulations or other applicable requirements could lead to claims for damages from our customers, penalties, termination of contracts and other adverse consequences. Any such damages, penalties, disruptions or limitations in our ability to do business with government entities could have a material adverse effect on our business, operating results and financial condition.

Government entities often require highly specialized contract terms that may differ from our standard arrangements. For example, if the federal government provides grants to certain state and local governments for our solutions, and such governments do not continue to receive these grants, then these customers have the ability to terminate their contracts with us without penalty. Government entities often impose compliance requirements that are complicated, require preferential pricing or “most favored nation” terms and conditions, or are otherwise time-consuming and expensive to satisfy. Compliance with these special standards or satisfaction of such requirements could complicate our efforts to obtain business or increase the cost of doing so. Even if we do meet these special standards or requirements, the increased costs associated with providing our solutions to government customers could harm our margins. Additionally, even once we have secured a government contract, the renewal process can be lengthy and as time-consuming as the initial sale, and we may be providing our service for months past the contract expiration date without certainty if the renewal agreement will be signed or not. During the COVID-19 pandemic and any associated impact on economic conditions, these risks are more pronounced than usual, as government entities struggle with reduced levels of resources related to implications of the pandemic.

Changes in the underlying regulatory conditions, political landscape or required procurement procedures that affect these types of customers could be introduced prior to the completion of our sales cycle, making it more difficult or costly to finalize a contract with a new customer or expand or renew an existing customer relationship. For example, customers may require a competitive bidding process with extended response deadlines, review or appeal periods, or customer attention may be diverted to other government matters, postponing the consideration of the purchase of our products. Such delays could harm our ability to provide our solutions efficiently and to grow or maintain our customer base.

If we are unable to maintain and expand coverage of our existing public safety customer accounts and further penetrate the public safety market, our revenues may not grow.

Our ability to increase revenues will depend in large part on our existing public safety solution customers renewing their annual subscriptions and expanding their mileage coverage or purchasing and implementing our ShotSpotter Connect solutions. Most of our ShotSpotter Flex customers begin using our solution in a limited coverage area. Our experience has been, and we expect will continue to be, that after the initial implementation of our solutions, our new customers typically renew their annual subscriptions, and many also choose to expand their coverage area. If our existing customers do not renew their subscriptions, our revenues may decrease. However, some customers may choose to not renew or reduce their coverage. If existing customers do not choose to renew or expand their coverage areas, our revenues will not grow as we anticipate, or may even decline. During the COVID-19 pandemic and any associated impact on economic conditions, this risk is more pronounced than usual, as our customers' priorities may change or they may have greater uncertainty regarding the availability of funding for our solutions as a result.

Our ability to further penetrate the market for our public safety solutions depends on several factors, including: maintaining a high level of customer satisfaction and a strong reputation among law enforcement; increasing the awareness of our ShotSpotter Flex and ShotSpotter Connect solutions and their benefits; the effectiveness of our marketing programs; the availability of funding to our customers, particularly in challenging economic conditions we anticipate from the COVID-19 pandemic; and the costs of our solutions. Some potential public safety customers may be reluctant or unwilling to use our solution for a number of reasons, including concerns about additional costs, unwillingness to expose or lack of concern regarding the extent of gun violence in their community, uncertainty regarding the reliability and security of cloud-based offerings or lack of awareness of the benefits of our public safety solutions. If we are unsuccessful in expanding the coverage of ShotSpotter Flex by existing public safety customers or adding new ShotSpotter Flex and ShotSpotter Connect public safety customers, our revenues and growth prospects would suffer.

If we are unable to sell our solutions into new markets, our revenues may not grow.

Part of our growth strategy depends on our ability to increase sales of our security solutions and add new customers for our public safety solution in markets outside of the United States. Our security solutions include ShotSpotter Connect, ShotSpotter Labs, ShotSpotter SecureCampus and ShotSpotter SiteSecure. We are focused on expanding the sales of these solutions into new markets, but customers in these new markets may not be receptive or sales may be delayed beyond our expectations, causing our revenue growth and growth prospects to suffer. During the COVID-19 pandemic and any associated impact on economic conditions, this risk is more pronounced than usual.

Our ability to successfully face these challenges depends on several factors, including increasing the awareness of our solutions and their benefits; the effectiveness of our marketing programs; the costs of our solutions; our ability to attract, retain and effectively train sales and marketing personnel; and our ability to develop relationships with communication carriers and other partners. If we are unsuccessful in developing and marketing our solutions into new markets, new markets for our solutions might not develop or might develop more slowly than we expect, either of which would harm our revenues and growth prospects.

Our sales cycle can be lengthy, time-consuming and costly, and our inability to successfully complete sales could harm our business.

Our sales process involves educating prospective customers and existing customers about the use, technical capabilities and benefits of our solutions. Prospective customers, especially government agencies, often undertake a prolonged evaluation process that may last up to nine months or more and that typically involves comparing the benefits of our solutions to alternative uses of funds. We may spend substantial time, effort and money on our sales and marketing efforts without any assurance that our efforts will produce any sales.

Additionally, events affecting our customers' budgets or missions may occur during the sales cycle that could negatively impact the size or timing of a purchase after we have invested substantial time, effort and resources into a potential sale, contributing to more unpredictability in the growth of our business. If we are unable to succeed in closing sales with new and existing customers, our business, operating results and financial condition will be harmed. During the COVID-19 pandemic and any associated impact on economic conditions, this risk is more pronounced than usual, as our customers' priorities may change or they may have greater uncertainty regarding the availability of funding for our solutions as a result.

Changes in the availability of federal funding to support local law enforcement efforts could impact our business.

Many of our customers rely to some extent on funds from the U.S. federal government in order to purchase and pay for our solutions. Any reduction in federal funding for local law enforcement efforts could result in our customers having less access to funds required to continue, renew, expand or pay for our solutions. Increasing social unrest, protests against racial inequality, protests against police brutality and movements such as “Defund the Police” have increased throughout 2020. These events may directly or indirectly affect municipal and police agency budgets, including federal funding available to current and potential customers. If federal funding is reduced or eliminated and our customers cannot find alternative sources of funding to purchase our solutions, our business will be harmed.

Federal stimulus funding increased in the second quarter as a result of the COVID-19 pandemic; however, we do not know whether additional stimulus funding will be made available, and many state and local governments anticipate budget shortfalls without additional funding. Further, the allocation of and prioritization of stimulus funds is uncertain and may change. There is no guarantee that additional funding will be made available to fund our solutions.

If our business does not grow as we expect, or if we fail to manage our growth effectively, our operating results and business prospects would suffer.

Our ability to successfully grow our business depends on a number of factors including our ability to:

- accelerate our acquisition of new customers;
- further sell expansions of coverage areas to our existing customers;
- expand our international footprint;
- expand into new vertical markets, such as precision policing, and security solutions;
- increase awareness of the benefits that our solutions offer;
- maintain our competitive and technology leadership position; and
- manage our business successfully through the COVID-19 pandemic and any resulting impact on economic conditions, including conditions impacting the availability of funding for our public safety solution.

As usage of our solutions grows, we will need to continue to make investments to develop and implement new or updated solutions, technologies, security features and cloud-based infrastructure operations. In addition, we will need to appropriately scale our internal business systems and our services organization, including the suppliers of our detection equipment and customer support services, to serve our growing customer base. Any failure of, or delay in, these efforts could impair the performance of our solutions and reduce customer satisfaction.

Further, our growth could increase quickly and place a strain on our managerial, operational, financial and other resources, and our future operating results depend to a large extent on our ability to successfully manage our anticipated expansion and growth. To manage our growth successfully, we will need to continue to invest in sales and marketing, research and development, and general and administrative functions and other areas. We are likely to recognize the costs associated with these investments earlier than receiving some of the anticipated benefits, and the return on these investments may be lower, or may develop more slowly, than we expect, which could adversely affect our operating results.

If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities or develop new solutions or upgrades to our existing solutions, satisfy customer requirements, maintain the quality and security of our solutions or execute on our business plan, any of which could have a material adverse effect on our business, operating results and financial condition.

The failure of our solutions to meet our customers' expectations could harm our reputation, which may have a material adverse effect on our business, operating results and financial condition.

Promoting and demonstrating the utility of our solutions as useful, reliable and important tools for law enforcement and security personnel is critical to the success of our business. Our ability to secure customer renewals, expand existing customer coverage areas, and enter into new customer contracts is dependent on our reputation and our ability to deliver our solutions effectively. We believe that our reputation among police departments using ShotSpotter Flex is particularly important to our success. Our ability to meet customer expectations will depend on a wide range of factors, including:

- our ability to continue to offer high-quality, innovative and accurate gunshot detection and gunshot deterrence services, and precision policing software and solutions;
- our ability to maintain continuous monitoring during high outdoor-noise activity periods such as New Year's Day, the Fourth of July and Cinco de Mayo, and Carnival for international deployments;
- our ability to maintain high customer satisfaction, including meeting our SLA ("Service Level Agreements") standards;
- the perceived value and quality of our solutions;
- differences in opinion regarding the metrics that measure the success of our solutions;
- our ability to successfully communicate the unique value proposition of our solutions;
- our ability to provide high-quality customer support;
- any misuse or perceived misuse of our solutions;
- interruptions, delays or attacks on our platform;
- litigation- or regulation-related developments; and
- damage to or degradation of our sensors or sensor network by third parties.

Furthermore, negative publicity, whether or not justified, relating to events or activities attributable to us, our solutions, our employees, our partners or others associated with any of these parties, may tarnish our reputation. Damage to our reputation may reduce demand for our solutions and would likely have a material adverse effect on our business, operating results and financial condition. Moreover, any attempts to rebuild our reputation may be costly and time-consuming, and such efforts may not ultimately be successful.

Interruptions or performance problems associated with our technology and infrastructure may adversely affect our business and results of operations.

We have in the past experienced, and may in the future experience, performance issues due to a variety of factors, including infrastructure changes, human or software errors, intentional or accidental damage to our technology (including sensors), website or third-party hosting disruptions or capacity constraints due to a number of potential causes including technical failures, natural disasters or security attacks. If our security is compromised, our platform is unavailable or our users are unable to receive our alerts or otherwise communicate with our IRC reviewers, within a reasonable amount of time or at all, our business could be negatively affected. In some instances, we may not be able to identify the cause or causes of these performance problems within an acceptable period of time.

In addition, our IRC department personnel operate either remotely or out of our offices. Any interruption or delay in service from our IRC, such as from a communications or power outage, could limit our ability deliver our solutions. In addition, it may become increasingly difficult to maintain and improve the performance of our solutions, especially during peak usage times as the capacity of our IRC operations reaches its limits. If there is an interruption or delay in service from our IRC operations and a gunshot is detected but not reviewed in the allotted time, our software will flag the incident for off-line review. This may result in delayed notifications to our customers and as a result, we could experience a decline in customer satisfaction with our solutions and our reputation and growth prospects could be harmed.

We expect to continue to make significant investments to maintain and improve the performance of our solutions. To the extent that we do not effectively address capacity constraints, upgrade our systems as needed and continually develop our technology to accommodate actual and anticipated changes in technology, our business, operating results and financial condition may be adversely affected.

We rely on wireless carriers to provide access to wireless networks through which our acoustic sensors communicate with our cloud-based backend and with which we provide our notification services to customers, and any interruption of such access would impair our business.

We rely on wireless carriers, mainly AT&T and Verizon, to provide access to wireless networks for machine-to-machine data transmissions, which are an integral part of our services. Our wireless carriers may suspend wireless service to expand, maintain or improve their networks. These wireless carriers perform routine maintenance and periodic software and firmware updates that may damage our sensors or make them inoperable. Any suspension or other interruption of services would adversely affect our ability to provide our services to our customers and may adversely affect our reputation. In addition, the terms of our agreements with these wireless carriers provide that either party can cancel or terminate the agreement for convenience. If one of our wireless carriers were to terminate its agreement with us, we would need to source a different wireless carrier and/or modify our equipment during the notice period in order to minimize disruption in the performance of our solutions. Price increases or termination by our wireless carriers or changes to existing contract terms could have a material adverse effect on our business, operating results and financial condition.

Natural disasters, infectious disease outbreaks, power outages or other events impacting us or our customers could harm our operating results and financial condition.

We recognize revenue on a subscription basis as our solutions are provided to our customers over time. If our services are disrupted due to natural disasters, infectious disease outbreaks, power outages or other events that we cannot control, we may not be able to continue providing our solutions as expected. For example, during the COVID-19 pandemic, our employees, including our IRC reviewers, are being required to work remotely, which may negatively impact productivity of our employees and effectiveness of our solutions.

When we stop providing coverage, we also stop recognizing revenues as a result of the affected subscription agreement. If we are forced to discontinue our services due to natural disasters, power outages and other events outside of our control, our revenues may decline, which would negatively impact our results of operations and financial condition. In addition, we may face liability for damages caused by our sensors in the event of heavy weather, hurricanes or other natural disasters. We may also incur additional costs to repair or replace installed sensor networks damaged by heavy weather, hurricanes or other natural disasters.

Any of our facilities or operations may be harmed or rendered inoperable by natural or man-made disasters, including earthquakes, tornadoes, hurricanes, wildfires, floods, nuclear disasters, acts of terrorism or other criminal activities, infectious disease outbreaks, such as COVID-19, and power outages, which may render it difficult or impossible for us to operate our business for some period of time or decrease productivity. For example, our primary IRC and a data center that hosts some of our customer services are located in the San Francisco Bay Area, a region known for seismic activity. Our facilities would likely be costly to repair or replace, and any such efforts would likely require substantial time. In addition, like many companies, we have recently implemented a work from home policy as a result of the COVID-19 pandemic. This policy may negatively impact productivity of our employees. Any disruptions in our operations could negatively impact our business and operating results and harm our reputation. In addition, we may not carry business insurance or may not carry sufficient business insurance to compensate for losses that may occur. Any such losses or damages could have a material adverse effect on our business, operating results and financial condition. In addition, the facilities of significant vendors, including the manufacturer of our proprietary acoustic sensor, may be harmed or rendered inoperable by such natural or man-made disasters, which may cause disruptions, difficulties or material adverse effects on our business.

Real or perceived false positive gunshot alerts or failure or perceived failure to generate alerts for actual gunfire could adversely affect our customers and their operations, damage our brand and reputation and adversely affect our growth prospects and results of operations.

A false positive alert, in which a non-gunfire incident is reported as gunfire, could result in an unnecessary rapid deployment of police officers and first responders, which may raise unnecessary fear among the occupants of a community or facility, and may be deemed a waste of police and first responder resources. A failure to alert law enforcement or security personnel of actual gunfire (false negative) could result in a less rapid or no response by police officers and first responders, increasing the probability of injury or loss of life. Both false positive alerts and the failure to generate alerts of actual gunfire (false negative) may result in customer dissatisfaction, potential loss of confidence in our solutions, and potential liabilities to customers or other third parties, any of which could harm our reputation and adversely impact our business and operating results. Additionally, the perception of a false positive alert or of a failure to generate an alert, even where our customers understand that our solutions were utilized correctly, could lead to negative publicity or harm the public perception of our solutions, which could harm our reputation and adversely impact our business and operating results.

Economic uncertainties or downturns, or political changes, could limit the availability of funds available to our customers and potential customers, which could materially adversely affect our business.

Economic uncertainties or downturns could adversely affect our business and operating results. Negative conditions in the general economy both in the United States and abroad, including conditions resulting from changes in gross domestic product growth, financial and credit market fluctuations, political deadlock, natural catastrophes, warfare, terrorist attacks and infectious disease outbreaks, such as COVID-19 pandemic, could cause a decrease in funds available to our customers and potential customers and negatively affect the rate of growth of our business.

These economic conditions may make it extremely difficult for our customers and us to forecast and plan future budgetary decisions or business activities accurately, and they could cause our customers to reevaluate their decisions to purchase our solutions, which could delay and lengthen our sales cycles or result in cancellations of planned purchases. Furthermore, during challenging economic times or as a result of political changes, our customers may tighten their budgets and face constraints in gaining timely access to sufficient funding or other credit, which could result in an impairment of their ability to make timely payments to us. In turn, we may be required to increase our allowance for doubtful accounts, which would adversely affect our financial results.

We cannot predict the timing, strength or duration of any economic slowdown, instability or recovery, generally or within any particular industry, or the impact of political changes. If the economic conditions of the general economy or industries in which we operate worsen from present levels, or if recent political changes result in less funding being available to purchase our solutions, our business, operating results, financial condition and cash flows could be adversely affected.

We have not been profitable historically and may not achieve or maintain profitability in the future.

We only reached our first full year of net income in 2019; prior to that, we posted a net loss in each year since inception. As of September 30, 2020, we had an accumulated deficit of \$94.1 million. We are not certain whether we will be able to maintain enough revenues from sales of our solutions to sustain or increase our growth or maintain profitability in the future. We also expect our costs to increase in future periods, which could negatively affect our future operating results if our revenues do not increase. In particular, we expect to continue to expend substantial financial and other resources on:

- sales and marketing, including a significant expansion of our sales organization, both domestically and internationally;
- research and development related to our solutions, including investments in our engineering and technical teams;
- acquisition of complementary technologies or businesses, such as our acquisition of HunchLab technology in October 2018, and our planned acquisition of Leeds, LLC in November 2020;

- continued international expansion of our business; and
- general and administrative expenses.

These investments may not result in increased revenues or growth in our business. If we are unable to increase our revenues at a rate sufficient to offset the expected increase in our costs, our business, operating results and financial position may be harmed, and we may not be able to maintain profitability over the long term. In particular, the COVID-19 pandemic and its impact on economic conditions will make it more difficult for us to increase revenues sufficient to maintain profitability. Additionally, we may encounter unforeseen operating expenses, difficulties, complications, delays and other unknown factors that may result in losses in future periods. If our revenue growth does not meet our expectations in future periods, our financial performance may be harmed, and we may not maintain profitability in the future.

We may require additional capital to fund our business and support our growth, and our inability to generate and obtain such capital on acceptable terms, or at all, could harm our business, operating results, financial condition and prospects.

We intend to continue to make substantial investments to fund our business and support our growth. In addition, we may require additional funds to respond to business challenges, including the need to develop new features or enhance our solutions, improve our operating infrastructure or acquire or develop complementary businesses and technologies. As a result, in addition to the revenues we generate from our business and our existing cash balances, we may need to engage in additional equity or debt financings to provide the funds required for these and other business endeavors. If we raise additional funds through future issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing that we may secure in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. We may not be able to obtain such additional financing on terms favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support our business growth and to respond to business challenges could be significantly impaired, and our business may be adversely affected. In addition, our inability to generate or obtain the financial resources needed may require us to delay, scale back, or eliminate some or all of our operations, which may have a material adverse effect on our business, operating results, financial condition and prospects.

The incurrence of debt may impact our financial position and subject us to additional financial and operating restrictions.

On September 27, 2018, we entered into a senior secured revolving credit facility with Umpqua Bank (the “Umpqua Credit Agreement”), which we increased to \$20.0 million in August 2020 and which we intend to use for general working capital purposes. As of September 30, 2020, we had no outstanding amounts due on nor any usage of the Umpqua Credit Agreement.

Under the Umpqua Credit Agreement, we are subject to various negative covenants that limit, subject to certain exclusions, our ability to incur indebtedness, make loans, invest in or secure the obligations of other parties, pay or declare dividends, make distributions with respect to our securities, redeem outstanding shares of our stock, create subsidiaries, materially change the nature of its business, enter into related party transactions, engage in mergers and business combinations, the acquisition or transfer of our assets outside of the ordinary course of business, grant liens or enter into collateral relationships involving company assets or reincorporate, reorganize or dissolve the company. These covenants could adversely affect our financial health and business and future operations by, among other things:

- making it more difficult to satisfy our obligations, including under the terms of the Umpqua Credit Agreement;
- limiting our ability to refinance our debt on terms acceptable to us or at all;
- limiting our flexibility to plan for and adjust to changing business and market conditions and increasing our vulnerability;

- limiting our ability to use our available cash flow to fund future acquisitions, working capital, business activities, and other general corporate requirements; and
- limiting our ability to obtain additional financing for working capital to fund growth or for general corporate purposes, even when necessary to maintain adequate liquidity.

We are also required to maintain certain financial covenants tied to our leverage, interest charges and profitability. Our ability to meet such covenants (those negative covenants discussed in the preceding paragraph) or other restrictions can be affected by events beyond our control, and our failure to comply with the financial and other covenants would be an event of default under the Umpqua Credit Agreement. If an event of default under the Umpqua Credit Agreement, has occurred and is continuing, the outstanding borrowings thereunder could become immediately due and payable, and we would then be required to cash collateralize any letters of credit then outstanding, and the lender could refuse to permit additional borrowings under the facility. We cannot assure you that we would have sufficient assets to repay those borrowings and, if we are unable to repay those amounts, the lender could proceed against the collateral granted to them to secure such indebtedness. We have pledged substantially all of our assets as collateral, and an event of default would likely have a material adverse effect on our business.

New competitors may enter the market for our public safety solution.

If cities and other government entities increase their efforts to reduce gun violence or our solutions gain visibility in the market, companies could decide to enter into the public safety solution market and thereby increase the competition we face. In addition to other gunshot detection products, we also compete with other technologies and solutions targeting our public safety customers' resources for law enforcement and crime prevention. Our competitors could benefit from the disclosure of our data or information concerning our techniques and processes due to legal or other obligations (for example, as a result of public-records requests or subpoenas to provide information or to testify in court). Because there are several possible uses for these limited budgetary resources, if we are not able to compete successfully for these limited resources, our business may not grow as we expect, which could adversely impact our revenues and operating results.

The competitive landscape for our security solutions is evolving.

The market for security solutions for university campuses, corporate campuses and transportation and key infrastructure centers includes a number of available options, such as video surveillance and increased human security presence. Because there are several possible uses of funds for security needs, we may face increased challenges in demonstrating or distinguishing the benefits of ShotSpotter SecureCampus and ShotSpotter SiteSecure. In particular, while we have seen growing interest in our security solutions, interest in the indoor gunshot detection offering was limited, and as a result, in June 2018, we made the strategic decision to cease indoor coverage as part of our service offering. While our ShotSpotter Connect may increase sales of our outdoor detection services, we may face challenges in demonstrating or distinguishing the benefits of ShotSpotter Connect' for development of crime forecasts and increased effectiveness of patrol resources.

Failure to effectively develop and expand our sales and marketing capabilities could harm our ability to increase our customer base and achieve broader market acceptance of our solutions.

To increase total customers and customer coverage areas and to achieve broader market acceptance of our solutions, we will need to expand our sales and marketing organization and increase our business development resources, including the vertical and geographic distribution of our sales force and our teams of account executives focused on new accounts and responsible for renewal and growth of existing accounts.

Our business requires that our sales personnel have particular expertise and experience in working with law enforcement agencies, other government organizations and higher education institutions. We may not achieve revenue growth from expanding our sales force if we are unable to hire, develop and retain talented sales personnel with appropriate experience, if our new sales personnel are unable to achieve desired productivity levels in a reasonable period of time or if our sales and marketing programs are not effective.

During the COVID-19 pandemic, this risk is more pronounced than usual, as our sales and marketing organization has been unable to travel and meetings with our current and potential customers have been more difficult to conduct.

Our strategy includes pursuing acquisitions, and our inability to successfully integrate newly-acquired technologies, assets or businesses may harm our financial results. Future acquisitions of technologies, assets or businesses, which are paid for partially or entirely through the issuance of stock or stock rights, could dilute the ownership of our existing stockholders.

We have announced our intention to acquire Leeds, LLC in order to enhance our precision policing platform. We will evaluate and consider potential strategic transactions, including acquisitions of, or investments in, businesses, technologies, services, products and other assets in the future. We also may enter into relationships with other businesses to expand our platform and applications, which could involve preferred or exclusive licenses, additional channels of distribution, discount pricing or investments in other companies.

We believe that part of our continued growth will be driven by acquisitions of other companies or their technologies, assets, businesses and teams. Acquisitions in the future that we complete will give rise to risks, including:

- incurring higher than anticipated capital expenditures and operating expenses;
- failing to assimilate the operations and personnel or failing to retain the key personnel of the acquired company or business;
- failing to integrate the acquired technologies, or incurring significant expense to integrate acquired technologies, into our platform and applications;
- disrupting our ongoing business;
- diverting our management's attention and other company resources;
- failing to maintain uniform standards, controls and policies;
- incurring significant accounting charges;
- impairing relationships with our customers and employees;
- finding that the acquired technology, asset or business does not further our business strategy, that we overpaid for the technology, asset or business or that we may be required to write off acquired assets or investments partially or entirely;
- failing to realize the expected synergies of the transaction;
- being exposed to unforeseen liabilities and contingencies that were not identified prior to acquiring the company; and
- being unable to generate sufficient revenues and profits from acquisitions to offset the associated acquisition costs.

Fully integrating an acquired technology, asset or business into our operations may take a significant amount of time. We may not be successful in overcoming these risks or any other problems encountered with the acquisition of Leeds or any future acquisitions. To the extent that we do not successfully avoid or overcome the risks or problems related to any such acquisitions, our results of operations and financial condition could be harmed. Acquisitions also could impact our financial position and capital requirements or could cause fluctuations in our quarterly and annual results of operations. Acquisitions could include significant goodwill and intangible assets, which may result in future impairment charges that would reduce our stated earnings. We may incur significant costs in our efforts to engage in strategic transactions and these expenditures may not result in successful acquisitions.

We expect that the consideration we might pay for any future acquisitions of technologies, assets, businesses or teams could include stock, rights to purchase stock, cash or some combination of the foregoing. If we issue stock or rights to purchase stock in connection with future acquisitions, net income per share and then-existing holders of our common stock may experience dilution.

The nature of our business exposes us to inherent liability risks.

Our gunshot detection solutions are designed to communicate real-time alerts of gunfire incidents to police officers and first responders. Due to the nature of such applications, we are potentially exposed to greater risks of liability for employee acts or omissions or system failures than may be inherent in other businesses. Although substantially all of our customer agreements contain provisions limiting our liability to our customers, we cannot be certain that these limitations will be enforced or that the costs of any litigation related to actual or alleged omissions or failures would not have a material adverse effect on us even if we prevail. Further, certain of our insurance policies and the laws of some states may limit or prohibit insurance coverage for punitive or certain other types of damages or liability arising from gross negligence, or other issues, such as damages caused due to installation of our sensors on buildings owned by third parties, and we cannot assure you that we are adequately insured against the risks that we face.

The nature of our business may result in undesirable press coverage or other negative publicity.

Our solutions are used to assist law enforcement and first responders in the event that gunfire is detected. Even when our solutions work as intended, the incidents detected by our solutions could lead to injury, loss of life and other negative outcomes, and such events are likely to receive negative publicity. If we fail to detect an incident, or if we detect an incident, such as a terrorist attack or active-shooter event, but the response time of law enforcement or first responders is not sufficiently quick to prevent injury, loss of life, property damage or other adverse outcomes, we may receive negative media attention. At times, our data or information concerning our techniques and processes may become a matter of public record due to legal or other obligations (for example, as a result of public-records requests or subpoenas to provide information or to testify in court), and we may receive negative media attention as a result.

In addition, our solutions require that our customers monitor alerts and respond timely to notifications of gunshots. If our customers do not fully utilize our systems, we may be subject to criticism and unflattering media coverage regarding the effectiveness of our solutions and the cost of our solutions to our customers. Such negative publicity could have an adverse impact on new sales or renewals or expansions of coverage areas by existing customers, which would adversely impact our financial results and future prospects.

Real or perceived errors, failures or bugs in our software could adversely affect our operating results and growth prospects.

Because our software is complex, undetected errors, failures or bugs may occur. Our software is often installed and used with different operating systems, system management software, and equipment and networking configurations, which may cause errors or failures of our software or other aspects of the computing environment into which it is deployed. In addition, deployment of our software into computing environments may expose undetected errors, compatibility issues, failures or bugs in our software. Despite our testing, errors, failures or bugs may not be found in our software until it is released to our customers. Moreover, our customers could incorrectly implement or inadvertently misuse our software, which could result in customer dissatisfaction and adversely impact the perceived utility of our products as well as our brand. Any of these real or perceived errors, compatibility issues, failures or bugs in our software could result in negative publicity, reputational harm, loss of or delay in market acceptance of our software, loss of competitive position or claims by customers for losses sustained by them. In any such event, we may be required, or may choose, for customer relations or other reasons, to expend additional resources in order to correct the problem. Alleviating any of these problems could require significant expenditures of our capital and other resources and could cause interruptions or delays in the use of our solutions, which could cause us to lose existing or potential customers and could adversely affect our operating results and growth prospects.

Interruptions or delays in service from our third-party providers could impair our ability to make our solutions available to our customers, resulting in customer dissatisfaction, damage to our reputation, loss of customers, limited growth and reduction in revenues.

We currently use third-party data center hosting facilities to host certain components of our solutions. Our operations depend, in part, on our third-party providers' abilities to protect these facilities against damage or interruption from natural disasters, power or communications failures, cyber incidents, criminal acts and similar events. In the event that any of our third-party facility arrangements is terminated, or if there is a lapse of service or damage to a facility, we could experience service interruptions in our solutions as well as delays and additional expenses in arranging new facilities and services. The COVID-19 pandemic and its associated shelter-in-place orders, travel bans and work-from-

home policies may increase the likelihood of service interruptions or cyber incidents at these data center hosting facilities. Any changes in third-party service levels at our data centers or any errors, defects, disruptions, cyber incidents or other performance problems with our solutions could harm our reputation.

Any damage to, or failure of, the systems of the communications providers with whom our data center provider contracts could result in interruptions to our solutions. The occurrence of spikes in usage volume, natural disasters, cyber incidents, acts of terrorism, vandalism or sabotage, closure of a facility without adequate notice or other unanticipated problems could result in lengthy interruptions in the availability of our services. Problems faced by these network providers, or with the systems by which they allocate capacity among their customers, including us, could adversely affect the experience of our customers. The COVID-19 pandemic and its associated shelter-in-place orders, travel bans and work-from-home policies may increase the likelihood of these problems with such network providers and their capacity allocation systems. Interruptions in our services might cause us to issue refunds to customers and subject us to potential liability.

Further, our insurance policies may not adequately compensate us for any losses that we may incur in the event of damage or interruption, and therefore the occurrence of any of the foregoing could subject us to liability, cause us to issue credits to customers or cause customers not to renew their subscriptions for our applications, any of which could materially adversely affect our business.

If our security measures or those of our customers or third-party providers are compromised, or if unauthorized access to the data of our customers is otherwise obtained, our solutions may be perceived as not being secure, our customers may be harmed and may curtail or cease their use of our solutions, our reputation may be damaged and we may incur significant liabilities.

Our operations involve the storage and transmission of gunfire incident data, including date, time, address and GPS coordinates, occurring in our customer's coverage area. Security incidents, whether as a result of third-party action, employee or customer error, technology impairment or failure, malfeasance or criminal activity, could result in unauthorized access to, or loss or unauthorized disclosure of, this gunfire incident data, which could result in litigation expenses or damages, indemnity and other contractual obligations and other possible liabilities, including but not limited to government fines and penalties and mitigation expenses, as well as negative publicity, which could damage our reputation, impair our sales and harm our customers and our business. Cyber incidents and malicious internet-based activity continue to increase generally, and providers of cloud-based services have been targeted. If third parties with whom we work, such as vendors or developers, violate applicable laws or our security policies, such violations may also put our gunfire incident data at risk and could in turn have an adverse effect on our business. In addition, such a violation could expose the locations of our sensors, including those sensors for which we obtained third-party consents that include confidentiality obligations. The COVID-19 pandemic may increase the likelihood of such cyber incidents. We may be unable to anticipate or prevent techniques used to obtain unauthorized access or to sabotage systems because such techniques change frequently and often are not detected until after an incident has occurred. As we increase our customer base and our brand becomes more widely known and recognized, third parties may increasingly seek to compromise our security controls or gain unauthorized access to customer data or other sensitive information. Further, because of the nature of the services that we provide to our customers, we may be a unique target for attacks.

Many governments have enacted laws requiring companies to notify individuals of data security incidents or unauthorized transfers involving certain types of personal data. In addition, some of our customers contractually require notification of any data security incident. Accordingly, security incidents experienced by our competitors, by our customers or by us may lead to public disclosures, which may lead to widespread negative publicity. Any security compromise in our industry, whether actual or perceived, could harm our reputation, erode customer confidence in the effectiveness of our security measures, negatively impact our ability to attract new customers, cause existing customers to elect not to renew their subscriptions or subject us to third-party lawsuits, regulatory fines or other action or liability, which could materially and adversely affect our business and operating results. Further, the costs of compliance with notification laws and contractual obligations may be significant and any requirement that we provide such notifications as a result of an actual or alleged compromise could have a material and adverse effect on our business.

While we maintain general liability insurance coverage and coverage for errors or omissions, we cannot assure you that such coverage would be adequate or would otherwise protect us from liabilities or damages with respect to claims alleging compromise or loss of data, or that such coverage will continue to be available on acceptable terms or at all.

We rely on the cooperation of customers and third parties to permit us to install our ShotSpotter sensors on their facilities, and failure to obtain these rights could increase our costs or limit the effectiveness of our ShotSpotter Flex solution.

Our ShotSpotter Flex solution requires us to deploy ShotSpotter sensors in our customer coverage areas, which typically entails the installation of approximately 20 to 25 sensors per square mile. The ShotSpotter sensors are mounted on city facilities and third-party buildings, and occasionally on city or utility-owned light poles, and installing the sensors requires the consent of the property owners, which can be time-consuming to obtain and can delay deployment. Generally, we do not pay a site license fee in order to install our sensors, and our contractual agreements with these facility owners provide them the right to revoke permission to use their facility with notice of generally 60 days.

To the extent that required consents delay our ability to deploy our solutions or facility owners do not grant permission to use their facilities, revoke previously granted permissions, or require us to pay a site license fee in order to install our sensors, our business may be harmed. If we were required to pay a site license fee in order to install sensors, our deployment expenses would increase, which would impact our gross margins. If we cannot obtain a sufficient number of sensor mounting locations that are appropriately dispersed in a coverage area, the effectiveness of our ShotSpotter Flex solution would be limited, we may need to reduce the coverage area of the solution. During the COVID-19 pandemic, our installation team has been unable to travel at times. Additionally, both our installation team and our third-party providers are facing greater challenges in obtaining permissions to install and in installing our sensors. To the extent our deployments are delayed for these reasons, we may not be able to meet our service level requirements, any of which could result in customer dissatisfaction or have a material adverse impact on our reputation, our business and our financial results.

If we fail to offer high-quality customer support, our business and reputation may suffer.

We offer customer support 24 hours a day, seven days a week, as well as training on best practices, forensic expertise and expert witness services. Providing these services requires that our personnel have specific experience, knowledge and expertise, making it more difficult for us to hire qualified personnel and to scale up our support operations. The importance of high-quality customer support will increase as we expand our business and pursue new customers. We may be unable to respond quickly enough to accommodate short-term increases in customer demand for support services or scale our services if our business grows. Increased customer demand for these services, without corresponding revenues, could increase our costs and harm our operating results. If we do not help our customers use applications within our solutions and provide effective ongoing support, our ability to sell additional applications to, or to retain, existing customers may suffer and our reputation with existing or potential customers may be harmed.

Our reliance on wireless carriers will require updates to our technology, and making such updates could result in disruptions in our service or increase our costs of operations.

Approximately 60% of our installed ShotSpotter sensors use fourth-generation Long-Term Evolution (“LTE”) wireless technology and 33% use third-generation (“3G”) cellular communications. Our US wireless carriers have advised us that they will discontinue their 3G services in the future and our ShotSpotter sensors will not be able to transmit on these networks. As a result, we will have to upgrade the sensors that use 3G cellular communications at no additional cost to our customers prior to the discontinuation of 3G services. As our wireless carriers phase out their 3G services or make changes to their spectrum allocation, we may experience reduced service performance, which may require us to replace our 3G sensors sooner than planned. Originally, we had expected to start incurring these upgrade costs in 2021 through 2022. We have begun plans to replace sensors in certain geographic areas starting in the second half of 2020 in order to optimize personnel utilization. Accelerated bandwidth changes by our carriers may require us to continue to accelerate the upgrade of our 3G sensors prior to 2022, which would accelerate the costs associated with the upgrade. These sensor replacements will require significant capital expenditures, which are estimated to be between \$4.0 million and \$6.0 million in total and may reduce our gross margins and also divert management’s attention and other important resources away from our customer service and sales efforts for new customers.

In the future, we may not be able to successfully implement new technologies or adapt existing technologies to changing market demands. If we are unable to adapt timely to changing technologies, market conditions or customer preferences, our business, operating results and financial condition could be materially and adversely affected.

Concerns regarding privacy and government-sponsored surveillance may deter customers from purchasing our solutions.

Governmental agencies and private citizens have become increasingly sensitive to real or perceived government or third-party surveillance and may wrongly believe that our outdoor sensors allow customers to listen to private conversations and monitor private citizen activity. Our sensors are not designed for “live listening” and are triggered only at loud impulsive sounds that may likely be gunfire. However, perceived privacy concerns may result in negative media coverage and efforts by private citizens to persuade municipalities, educational institutions or other potential customers not to purchase our solutions for their communities, campuses or facilities. In addition, laws may exist or be enacted to address such concerns that could impact our ability to deploy our solutions. For example, the City of Toronto, Canada decided against using ShotSpotter solutions because the Ministry of the Attorney General of Ontario indicated that it may compromise Section 8 of Canada’s Charter of Rights and Freedoms, which relates to unreasonable search and seizure. If customers choose not to purchase our solutions due to privacy or surveillance concerns, then the market for our solutions may develop more slowly than we expect, or it may not achieve the growth potential we expect, any of which would adversely affect our business and financial results.

We rely on a limited number of suppliers and contract manufacturers, and our proprietary ShotSpotter sensors are manufactured by a single contract manufacturer.

We rely on a limited number of suppliers and contract manufacturers. In particular, we use a single manufacturer, with which we have no long-term contract and from which we purchase on a purchase-order basis, to produce our proprietary ShotSpotter sensors. Our reliance on a sole contract manufacturer increases our risks since we do not currently have any alternative or replacement manufacturers, and we do not maintain a high volume of inventory. In the event of an interruption from a contract manufacturer, we may not be able to develop alternate or secondary sources without incurring material additional costs and substantial delays. Furthermore, these risks could materially and adversely affect our business if our contract manufacturer is impacted by a natural disaster or other interruption at a particular location because each of our contract manufacturers produces our products from a single location. Although our contract manufacturer has alternative manufacturing locations, transferring manufacturing to another location may result in significant delays in the availability of our sensors. Also, many standardized components used broadly in our sensors are manufactured in significant quantities in concentrated geographic regions, particularly in Greater China. As a result, protracted regional crises, or the COVID-19 pandemic, could lead to eventual shortages of necessary components. It could be difficult, costly and time consuming to obtain alternative sources for these components, or to change product designs to make use of alternative components. In addition, difficulties in transitioning from an existing supplier to a new supplier could create delays in component availability that would have a significant impact on our ability to fulfill orders for our products.

Many of the key components used to manufacture our proprietary ShotSpotter sensors also come from limited or sole sources of supply. Our contract manufacturer generally purchases these components on our behalf, and we do not have any long-term arrangements with our suppliers. We are therefore subject to the risk of shortages and long lead times in the supply of these components and the risk that suppliers discontinue or modify components used in our products. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantities and delivery schedules. Developing alternate sources of supply for these components may be time-consuming, difficult, and costly, and we or our suppliers may not be able to source these components on terms that are acceptable to us, or at all, which may undermine our ability to fill our orders in a timely manner.

If we experience significantly increased demand, or if we need to replace an existing supplier or contract manufacturer, we may be unable to supplement or replace such supply or contract manufacturing on terms that are acceptable to us, which may undermine our ability to deliver our products to customers in a timely manner. For example, for our ShotSpotter sensors, it may take a significant amount of time to identify a contract manufacturer that has the capability and resources to build the sensors to our specifications. Identifying suitable suppliers and contract manufacturers is an extensive process that requires us to become satisfied with their quality control, technical capabilities, responsiveness and service, financial stability, regulatory compliance, and labor and other ethical practices. Accordingly, the loss of any key supplier or contract manufacturer could adversely impact our business, operating results and financial condition.

Our solutions use third-party software and services that may be difficult to replace or cause errors or failures of our solutions that could lead to a loss of customers or harm to our reputation and our operating results.

We license third-party software and depend on services from various third parties for use in our solutions. In the future, such software or services may not be available to us on commercially reasonable terms, or at all. Any loss of the right to use any of the software or services could result in decreased functionality of our solutions until equivalent technology is either developed by us or, if available from another provider, is identified, obtained and integrated, which could harm our business. In addition, any errors or defects in or failures of the third-party software or services could result in errors or defects in our solutions or cause our solutions to fail, which could harm our business and be costly to correct. Many of these providers attempt to impose limitations on their liability for such errors, defects or failures, and if enforceable, we may have additional liability to our customers or third-party providers that could harm our reputation and increase our operating costs.

We will need to maintain our relationships with third-party software and service providers, and obtain from such providers software and services that do not contain any errors or defects. Any failure to do so could adversely impact our ability to deliver effective products to our customers and could harm our operating results.

If we do not or cannot maintain the compatibility of our platform with applications that our customers use, our business could suffer.

Some of our customers choose to integrate our solutions with certain other systems used by our customers, such as real-time crime center platforms or computer-aided dispatch systems. The functionality and popularity of our solutions depend, in part, on our ability to integrate our solutions these systems. Providers of these systems may change the features of their technologies, restrict our access to their applications or alter the terms governing use of their applications in an adverse manner. Such changes could functionally limit or terminate our ability to use these technologies in conjunction with our solutions, which could negatively impact our customer service and harm our business. If we fail to integrate our solutions with applications that our customers use, we may not be able to offer the functionality that our customers need, and our customers may not renew their agreements, which would negatively impact our ability to generate revenues and adversely impact our business.

As a result of our use of outdoor acoustic sensors, we are subject to governmental regulation and other legal obligations, particularly related to privacy, data protection and information security, and our actual or perceived failure to comply with such obligations could harm our business. Compliance with such laws could impair our efforts to maintain and expand our customer base, and thereby decrease our revenues.

Our outdoor sensors are acoustic devices that are designed to recognize impulsive sounds that are likely to be gunfire. ShotSpotter sensors do not use high gain, directional or other specialized microphones.

The sensors do not have the ability to live stream audio. Typically, sounds, noises or voices captured on the secure sensors are cached temporarily but are written over and permanently deleted within 30 hours. When a sensor is triggered by an impulsive sound, it creates a potential gunshot "incident" that contains a recording, which includes no more than one second before the incident and one second after the incident. This incident audio snippet is preserved indefinitely for potential evidentiary use.

There is the potential to include human voices that occur at the same time as the gunshot in these incident audio snippets. We retain incident audio snippets indefinitely as evidence. We also use information collected to support, expand and improve our software algorithms as well as our gunfire detection and notification methods. Sensors are often installed in densely populated urban areas. They are not designed or tuned to capture human voices, but it is possible they could pick up a human voice. Human voices are not impulsive and do not typically trigger the sensors, and unless accompanied by an impulsive sound no audio snippet would be transmitted out of the sensor and preserved as an incident audio snippet. The human voice would be temporarily cached on the sensor for 30 hours and would then be written over and permanently deleted. Information collected from loud impulsive sounds ("incidents") is used to provide information to our customers regarding those incidents, but shared information is limited, by both our technology and our privacy policies, to the audio snippet containing the incident.

Our handling and storage of data is subject to a variety of laws and regulations, including regulation by various government agencies and various state, local and foreign agencies. The U.S. federal and various state and foreign governments have adopted or proposed legislation that regulates the monitoring and collection of personal information

of individuals and that mandates security requirements with respect to certain personally identifiable information. In the United States, the Federal Trade Commission and numerous state attorneys general are imposing standards for the online collection, distribution, use and storage of data by applying federal and state consumer protection laws. The lack of a clear and universal standard for protecting such information means, however, that these obligations may be interpreted and applied in a manner that is inconsistent from one jurisdiction to another and may conflict with other requirements or our practices. Any failure or perceived failure by us to comply with privacy or security laws, policies, legal obligations or industry standards or any security incident that results in the unauthorized release or transfer of sensitive corporate information, personally identifiable information or other customer data may result in governmental enforcement actions, litigation, fines and penalties and/or adverse publicity, and could cause our customers to lose trust in us, which could have an adverse effect on our reputation and business.

California enacted the California Consumer Privacy Act (the “CCPA”), which became operative on January 1, 2020. The CCPA requires covered companies to, among other things, provide new disclosures to California consumers, and affords such consumers new abilities to opt-out of certain sales of personal information. On June 1, 2020, the California Attorney General submitted the final implementing regulations for review to the Office of Administrative Law and the enforcement of the CCPA by the California Attorney General began on July 1, 2020. The impact of the CCPA on our business or operations, may require us to modify our data processing practices and policies and to incur substantial costs and expenses in an effort to comply.

Some proposed laws or regulations concerning privacy, data protection and information security are in their early stages, and we cannot yet determine how these laws and regulations may be interpreted nor can we determine the impact these proposed laws and regulations, may have on our business. Such proposed laws and regulations may require companies to implement privacy and security policies, permit users to access, correct and delete personal information stored or maintained by such companies, inform individuals of security breaches that affect their personal information, and, in some cases, obtain individuals’ consent to use personal information for certain purposes. In addition, a foreign government could require that any personal information collected in a country not be disseminated outside of that country, and we may not be currently equipped to comply with such a requirement. Our failure to comply with federal, state and international data privacy laws and regulators could harm our ability to successfully operate our business and pursue our business goals.

Our quarterly results of operations may fluctuate significantly due to a wide range of factors, which makes our future results difficult to predict.

Our revenues and results of operations could vary significantly from quarter to quarter as a result of various factors, many of which are outside of our control, including:

- the expansion or contraction of our customer base;
- the renewal or nonrenewal of subscription agreements with, and expansion of coverage areas by, existing customers;
- the size, timing, terms and deployment schedules of our sales to both existing and new customers;
- the introduction of products or services that may compete with us for the limited funds available to our customers, and changes in the cost of such products or services;
- changes in our customers’ and potential customers’ budgets;
- our ability to control costs, including our operating expenses;
- our ability to hire, train and maintain our direct sales force;
- the timing of satisfying revenues recognition criteria in connection with initial deployment and renewals;
- fluctuations in our effective tax rate;
- the impact of the COVID-19 pandemic on business operations and economic conditions; and
- general economic and political conditions, both domestically and internationally.

Any one of these or other factors discussed elsewhere in this report may result in fluctuations in our revenues and operating results, meaning that quarter-to-quarter comparisons of our revenues, results of operations and cash flows may not necessarily be indicative of our future performance.

Because of the fluctuations described above, our ability to forecast revenues is limited and we may not be able to accurately predict our future revenues or results of operations. In addition, we base our current and future expense levels on our operating plans and sales forecasts, and our operating expenses are expected to increase in the short term. Accordingly, we may not be able to reduce our costs sufficiently to compensate for an unexpected shortfall in revenues, and even a small shortfall in revenues could disproportionately and adversely affect our financial results for that quarter. The variability and unpredictability of these and other factors could result in our failing to meet or exceed financial expectations for a given period.

Because we generally recognize our subscription revenues ratably over the term of our contract with a customer, fluctuations in sales will not be fully reflected in our operating results until future periods.

Our revenues are primarily generated from subscriptions to our solutions. With the exception of a small number of legacy customers, our customers do not have the right to take possession of our equipment or software platform. Revenues from subscriptions to our software platform is recognized ratably over the subscription period beginning on the date that the subscription is made available to the customer, which we refer to as the “go-live” date. Our agreements with our customers typically range from one to five years. As a result, much of the revenues that we report in each quarter are attributable to agreements entered into during previous quarters. Consequently, a decline in sales, customer renewals or market acceptance of our solutions in any one quarter would not necessarily be fully reflected in the revenues in that quarter and would negatively affect our revenues and profitability in future quarters. This ratable revenues recognition also makes it difficult for us to rapidly increase our revenues through additional sales in any period, as revenues from new customers generally are recognized over the applicable agreement term. Our subscription-based approach may result in uneven recognition of revenues.

We recognize subscription revenues over the term of a subscription agreement. Once we enter into a contract with a customer, there is a delay until we begin recognizing revenues while we survey the coverage areas, obtain any required consents for installation, and install our sensors, which together can take up to several months or more. We begin recognizing revenues from a sale only when all of these steps are complete and the solution is live.

While most of our customers elect to renew their subscription agreements following the expiration of a term, in some cases, they may not be able to obtain the proper approvals or funding to complete the renewal prior to such expiration. For these customers, we stop recognizing subscription revenues at the end of the current term, even though we may continue to provide services for a period of time while the renewal process is completed. Once the renewal is complete, we then recognize subscription revenues for the period between the expiration of the term of the agreement and the completion of the renewal process.

The variation in the timeline for deploying our solutions and completing renewals may result in fluctuations in our revenues, which could cause our results to differ from projections. Additionally, while we generally invoice for 50% of the contract cost upon a customer’s go-live date, our cash flows may be volatile and will not match our revenues recognition.

We are in the process of expanding our international operations, which exposes us to significant risks.

We currently operate in limited number of locations outside the United States. A key component to our business strategy is to expand our international operations to increase our revenues from customers outside of the United States as part of our growth strategy. Operating in international markets requires significant resources and management attention and will subject us to regulatory, economic and political risks in addition to those we already face in the United States. In addition, we will need to invest time and resources in understanding the regulatory framework and political environments of our potential customers overseas in order to focus our sales efforts. Because such regulatory and political considerations are likely to vary across jurisdictions, this effort will require additional time and attention from our sales team and could lead to a sales cycle that is longer than our typical process for sales in the United States. We also may need to hire additional employees and otherwise invest in our international operations in order to reach new customers. Because of our limited experience with international operations as well as developing and managing sales in international markets, our international expansion efforts may be delayed or may not be successful.

In addition, we face and will continue to face risks in doing business internationally that could adversely affect our business, including:

- the potential impact of currency exchange fluctuations;
- the need to comply with local data residency requirements;
- the availability and reliability of local data centers and internet bandwidth providers;
- the difficulty of staffing and managing international operations and the increased operations, travel, shipping and compliance costs associated with having customers in numerous international locations;
- potentially greater difficulty collecting accounts receivable and longer payment cycles;
- the availability and cost of coverage by wireless carriers in international markets;
- higher or more variable costs associated with wireless carriers and other service providers;
- the need to offer customer support in various languages;
- challenges in understanding and complying with local laws, regulations and customs in foreign jurisdictions, including laws regarding privacy and government surveillance;
- export controls and economic sanctions administered by the Department of Commerce Bureau of Industry and Security and the Treasury Department's Office of Foreign Assets Control;
- compliance with various anti-bribery and anti-corruption laws such as the Foreign Corrupt Practices Act and United Kingdom Bribery Act of 2010;
- tariffs and other non-tariff barriers, such as quotas and local content rules;
- more limited protection for our intellectual property in some countries;
- adverse or uncertain tax consequences as a result of international operations;
- currency control regulations, which might restrict or prohibit our conversion of other currencies into U.S. dollars;
- restrictions on the transfer of funds;
- deterioration of political relations between the United States and other countries; and
- political or social unrest or economic instability in a specific country or region in which we operate, which could have an adverse impact on our operations in that location.

Also, we expect that due to costs related to our international expansion efforts and the increased cost of doing business internationally, we will incur higher costs to secure sales to international customers than the comparable costs for domestic customers. As a result, our financial results may fluctuate as we expand our operations and customer base worldwide.

Our failure to manage any of these risks successfully could harm our international operations, and adversely affect our business, operating results and financial condition.

We are dependent on the continued services and performance of our senior management and other key personnel, the loss of any of whom could adversely affect our business.

Our future success depends in large part on the continued contributions of our senior management and other key personnel. In particular, the leadership of key management personnel is critical to the successful management of our company, the development of our products, and our strategic direction. We also depend on the contributions of key technical personnel.

We do not maintain “key person” insurance for any member of our senior management team or any of our other key employees. Our senior management and key personnel are all employed on an at-will basis, which means that they could terminate their employment with us at any time, for any reason and without notice. The loss of any of our key management personnel could significantly delay or prevent the achievement of our development and strategic objectives and adversely affect our business.

If we are unable to attract, integrate and retain additional qualified personnel, including top technical talent, our business could be adversely affected.

Our future success depends in part on our ability to identify, attract, integrate and retain highly skilled technical, managerial, sales and other personnel. We face intense competition for qualified individuals from numerous other companies, including other software and technology companies, many of whom have greater financial and other resources than we do. Some of these characteristics may be more appealing to high-quality candidates than those we have to offer. In addition, new hires often require significant training and, in many cases, take significant time before they achieve full productivity. We may incur significant costs to attract and retain qualified personnel, including significant expenditures related to salaries and benefits and compensation expenses related to equity awards, and we may lose new employees to our competitors or other companies before we realize the benefit of our investment in recruiting and training them. Moreover, new employees, especially those who work from home, may not be or become as productive as we expect, as we may face challenges in adequately or appropriately integrating them into our workforce and culture. If we are unable to attract, integrate and retain suitably qualified individuals who are capable of meeting our growing technical, operational and managerial requirements, on a timely basis or at all, our business will be adversely affected.

Volatility or lack of positive performance in our stock price may also affect our ability to attract and retain our key employees. Many of our senior management personnel and other key employees have become, or will soon become, vested in a substantial amount of stock or stock options. Employees may be more likely to leave us if the shares they own or the shares underlying their vested options have significantly appreciated in value relative to the original purchase prices of the shares or the exercise prices of the options, or, conversely, if the exercise prices of the options that they hold are significantly above the market price of our common stock. If we are unable to appropriately incentivize and retain our employees through equity compensation, or if we need to increase our compensation expenses in order to appropriately incentivize and retain our employees, our business, operating results and financial condition would be adversely affected.

We may be subject to additional obligations to collect and remit certain taxes, and we may be subject to tax liability for past activities, which could harm our business.

State, local and foreign jurisdictions have differing rules and regulations governing sales, use, value added and other taxes, and these rules and regulations are subject to varying interpretations that may change over time, particularly with respect to software-as-a-service products like our solutions. Further, these jurisdictions’ rules regarding tax nexus are complex and vary significantly. If one or more jurisdictions were to assert that we have failed to collect taxes for sales of our solutions, we could face the possibility of tax assessments and audits. A successful assertion that we should be collecting additional sales, use, value added or other taxes in those jurisdictions where we have not historically done so and do not accrue for such taxes could result in substantial tax liabilities and related penalties for past sales or otherwise harm our business and operating results.

Our ability to use our net operating losses to offset future taxable income may be subject to certain limitations.

As of December 31, 2019, we had federal net operating loss carryforwards (“NOLs”) of approximately \$85.6 million, of which \$80.6 million will expire between 2026 through 2038, if not utilized. As of December 31, 2019, we also had state NOLs of approximately \$55.0 million, which will expire, if not utilized, in 2020 through 2039. These federal and state NOLs may be available to reduce future income subject to income taxes. In general, under Section 382 of the Internal Revenue Code of 1986, as amended (“the Code”), a corporation that undergoes an “ownership change” is subject to limitations on its ability to utilize its NOLs to offset future taxable income. Past or future changes in our stock ownership, some of which are outside of our control, may have resulted or could result in an ownership change. State NOLs generated in one state cannot be used to offset income generated in another state.

We may be subject to litigation for a variety of claims or to other legal requests, which could adversely affect our results of operations, harm our reputation or otherwise negatively impact our business.

We may be subject to litigation for a variety of claims arising from our normal business activities. These may include claims, suits, and proceedings involving labor and employment, wage and hour, commercial and other matters. The outcome of any litigation, regardless of its merits, is inherently uncertain. Any claims and lawsuits, and the disposition of such claims and lawsuits, could be time-consuming and expensive to resolve, divert management attention and resources, and lead to attempts on the part of other parties to pursue similar claims. Any adverse determination related to litigation could adversely affect our results of operations, harm our reputation or otherwise negatively impact our business. In addition, depending on the nature and timing of any such dispute, a resolution of a legal matter could materially affect our future operating results, our cash flows or both.

An unfavorable outcome on any litigation matters could require us to pay substantial damages, or, in connection with any intellectual property infringement claims, could require us to pay ongoing royalty payments or could prevent us from selling certain of our products. As a result, a settlement of, or an unfavorable outcome on, any of the matters referenced above or other litigation matters could have a material adverse effect on our business, operating results, financial condition and cash flows.

We, or our customers, may be subject to requests for our data or information concerning our techniques and processes, pursuant to state or federal law (for example, public-records requests or subpoenas to provide information or to testify in court). This data and information, some of which we may deem to be confidential or trade secrets, could therefore become a matter of public record and also become accessible by competitors, which could negatively impact our business.

Changes in financial accounting standards may cause adverse and unexpected revenues fluctuations and impact our reported results of operations.

The accounting rules and regulations that we must comply with are complex and subject to interpretation by the Financial Accounting Standards Board, the Securities and Exchange Commission and various bodies formed to promulgate and interpret appropriate accounting principles. In addition, many companies' accounting disclosures are being subjected to heightened scrutiny by regulators and the public. Further, the accounting rules and regulations are continually changing in ways that could impact our financial statements.

Changes to accounting principles or our accounting policies on our financial statements going forward are difficult to predict, could have a significant effect on our reported financial results, and could affect the reporting of transactions completed before the announcement of the change. In addition, were we to change our critical accounting estimates, including the timing of recognition of subscription and professional services revenues and other revenues sources, our results of operations could be significantly impacted.

Risks Related to Our Intellectual Property

Failure to protect our intellectual property rights could adversely affect our business.

Our success depends, in part, on our ability to protect proprietary methods and technologies that we develop or license under patent and other intellectual property laws of the United States, as well as our brands, so that we can prevent others from them. We rely on a combination of contractual and intellectual property rights, including non-disclosure agreements, patents, trade secrets, copyrights and trademarks, to establish and protect our intellectual property rights in our names, services, innovations, methodologies and related technologies. If we fail to protect our intellectual property rights adequately, our competitors might gain access to our technology and our business might be adversely affected.

As of September 30, 2020, we had 33 U.S. patents directed to our technologies, as well as one granted patent in Israel and one granted patent in Mexico. The issued patents expire on various dates from 2022 to 2034. We also license one patent from a third party, which expires in 2023. We have patent applications pending for examination in the United States, Europe, Mexico and Brazil, but we cannot guarantee that these patent applications will be granted. We also license one other U.S. patent from one third party. The patents that we own or those that we license from others (including those that may be issued in the future) may not provide us with any competitive advantages or may be challenged by third parties.

The process of obtaining patent protection is expensive and time-consuming, and we may not be able to prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. Even if issued, there can be no assurance that these patents will adequately protect our intellectual property, as the legal standards relating to the validity, enforceability and scope of protection of patent and other intellectual property rights are uncertain.

Any patents that are issued may subsequently be invalidated or otherwise limited, allowing other companies to develop offerings that compete with ours, which could adversely affect our competitive business position, business prospects and financial condition. In addition, issuance of a patent does not guarantee that we have a right to practice the patented invention. Patent applications in the United States are typically not published until 18 months after their earliest priority date or, in some cases, not at all, and publications of discoveries in industry-related literature lag behind actual discoveries. We cannot be certain that third parties do not have blocking patents that could be used to prevent us from marketing or practicing our software or technology.

Effective patent, trademark, copyright and trade secret protection may not be available to us in every country in which our software is available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the United States (in particular, some foreign jurisdictions do not permit patent protection for software), and mechanisms for enforcement of intellectual property rights may be inadequate. Additional uncertainty may result from changes to intellectual property legislation enacted in the United States, including the recent America Invents Act, or to the laws of other countries and from interpretations of the intellectual property laws of the United States and other countries by applicable courts and agencies. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

We rely in part on trade secrets, proprietary know-how and other confidential information to maintain our competitive position. Although we endeavor to enter into non-disclosure agreements with our employees, licensees and others who may have access to this information, we cannot assure you that these agreements or other steps we have taken will prevent unauthorized use, disclosure or reverse engineering of our technology. Moreover, third parties may independently develop technologies or products that compete with ours, and we may be unable to prevent this competition. Third parties also may seek access to our trade secrets, proprietary know-how and other confidential information through legal measures (for example, public-records requests or subpoenas to provide information or to testify in court) and it could be expensive to defend against those requests. Disclosure of our trade secrets, proprietary know-how and other confidential information could negatively impact our business.

We might be required to spend significant resources to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Litigation also puts our patents at risk of being invalidated or interpreted narrowly and our patent applications at risk of not issuing. Additionally, we may provoke third parties to assert counterclaims against us. We may not prevail in any lawsuits that we initiate, and the damages or other remedies awarded, if any, may not be commercially viable. Any litigation, whether or not resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel, which may adversely affect our business, operating results, financial condition and cash flows.

We may be subject to intellectual property rights claims by third parties, which are extremely costly to defend, could require us to pay significant damages and could limit our ability to use certain technologies.

Companies in the software and technology industries, including some of our current and potential competitors, own large numbers of patents, copyrights, trademarks and trade secrets and frequently enter into litigation based on allegations of infringement or other violations of intellectual property rights. In addition, many of these companies have the capability to dedicate substantially greater resources to enforce their intellectual property rights and to defend claims that may be brought against them. The litigation may involve patent holding companies or other adverse patent owners that have no relevant product revenues and against which our patents may therefore provide little or no deterrence. We may have previously received, and may in the future receive, notices that claim we have misappropriated, misused, or infringed other parties' intellectual property rights, and, to the extent we gain greater market visibility, we face a higher risk of being the subject of intellectual property infringement claims.

There may be third-party intellectual property rights, including issued or pending patents that cover significant aspects of our technologies or business methods. Any intellectual property claims, with or without merit, could be very time-consuming, could be expensive to settle or litigate and could divert our management's attention and other resources. These claims could also subject us to significant liability for damages, potentially including treble damages if we are found to have willfully infringed patents or copyrights. These claims could also result in our having to stop using technology found to be in violation of a third party's rights. We might be required to seek a license for the intellectual property, which may not be available on a timely basis, on reasonable terms or at all. We also may be required to modify our products, services, internal systems or technologies. Even if a license were available, we could be required to pay significant royalties, which would increase our operating expenses. As a result, we may be required to develop alternative non-infringing technology, which could require significant effort and expense. If we cannot license or develop technology for any infringing aspect of our business, we would be forced to limit or stop sales of our software and may be unable to compete effectively. Any of these results would adversely affect our business, operating results, financial condition and cash flows.

Our use of open source software could subject us to possible litigation.

A portion of our technologies incorporates open source software, and we expect to continue to incorporate open source software into our platform in the future. Few of the licenses applicable to open source software have been interpreted by courts, and their application to the open source software integrated into our proprietary technology platform may be uncertain. If we fail to comply with these licenses, then pursuant to the terms of these licenses, we may be subject to certain requirements, including requirements that we make available the source code for our software that incorporates the open source software. We cannot assure you that we have not incorporated open source software in our software in a manner that is inconsistent with the terms of the applicable licenses or our current policies and procedures. If an author or other third party that distributes such open source software were to allege that we had not complied with the conditions of one or more of these licenses, we could incur significant legal expenses defending against such allegations. Litigation could be costly for us to defend, have a negative effect on our operating results and financial condition or require us to devote additional research and development resources to change our technology platform.

Risks Related to the Ownership of Our Common Stock

Our stock price may be volatile or may decline regardless of our operating performance, resulting in substantial losses for investors.

The market price of our common stock has fluctuated and may continue to fluctuate significantly in response to numerous factors, many of which are beyond our control, including the factors listed below and other factors described in this "Risk Factors" section:

- actual or anticipated fluctuations in our operating results;
- the financial projections we may provide to the public, any changes in these projections or our failure to meet these projections;
- failure of securities analysts to initiate or maintain coverage of our company, changes in financial estimates by any securities analysts who follow our company, or our failure to meet these estimates or the expectations of investors;
- ratings changes by any securities analysts who follow our company;
- changes in the availability of federal funding to support local law enforcement efforts, or local budgets;
- announcements by us of significant technical innovations, acquisitions, strategic partnerships, joint ventures or capital commitments;
- changes in operating performance and stock market valuations of other software companies generally;
- price and volume fluctuations in the overall stock market, including as a result of trends in the economy as a whole;
- changes in our board of directors or management;

- sales of large blocks of our common stock, including sales by our executive officers, directors and significant stockholders;
- lawsuits threatened or filed against us;
- short sales, hedging and other derivative transactions involving our capital stock;
- the impact of the COVID-19 pandemic;
- general economic conditions in the United States and abroad;
- other events or factors, including those resulting from pandemics, protests against racial inequality, protests against police brutality and movements such as “Defund the Police”, war, incidents of terrorism or responses to these events; and
- media misperception of our sales and customer relationships, including press announcements or media mentions of future sales that may be misleading or inaccurate.

In addition, stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many software companies. Stock prices of many software companies have fluctuated in a manner unrelated or disproportionate to the operating performance of those companies. Broad market and industry fluctuations, as well as general economic, political, regulatory and market conditions, may negatively impact the market price of our common stock. In the past, stockholders have instituted securities action litigation following periods of market volatility. If we were to become involved in securities litigation, it could subject us to substantial costs, divert resources and the attention of management from our business and adversely affect our business, operating results, financial condition and cash flows.

Substantial future sales of shares of our common stock could cause the market price of our common stock to decline.

Certain holders of our shares of common stock have the right, subject to various conditions and limitations, to include their shares of our common stock in registration statements relating to our securities, including approximately 3.3 million shares that were registered in connection with the Registration Statement on Form S-3 that became effective on July 27, 2018, of which approximately 136,000 were sold in an underwritten registered follow-on offering in March 2019. If the offer and sale of these shares are registered, they will be freely tradable without restriction under the Securities Act. In addition, non-affiliates have the ability to sell shares of our common stock in the open market or through block trades without subject to volume restrictions under Rule 144 of the Securities Act. In addition, in the future we may issue common stock or other securities if we need to raise additional capital. The number of new shares of our common stock issued in connection with raising additional capital could constitute a material portion of the then outstanding shares of our common stock. In the event a large number of shares of common stock are sold in the public market, such share sales could reduce the trading price of our common stock.

Stock repurchases could increase the volatility of the trading price of our common stock and diminish our cash reserves, and we cannot guarantee that our stock repurchase program will enhance long-term stockholder value.

In May 2019, our board of directors adopted a stock repurchase program for up to \$15 million of our common stock. Although our board of directors has authorized the stock repurchase program, it does not obligate us to repurchase any specific dollar amount or number of shares, there is no expiration date for the stock repurchase program, and the stock repurchase program may be modified, suspended or terminated at any time and for any reason. The timing and actual number of shares repurchased under the stock repurchase program will depend on a variety of factors, including the acquisition price of the shares, our liquidity position, general market and economic conditions, legal and regulatory requirements and other considerations. Our ability to repurchase shares may also be limited by restrictive covenants in our existing credit agreement or in future borrowing arrangements we may enter into from time to time.

Repurchases of our shares could increase the volatility of the trading price of our stock, which could have a negative impact on the trading price of our stock. Similarly, the future announcement of the termination or suspension of the stock repurchase program, or our decision not to utilize the full authorized repurchase amount under the stock repurchase program, could result in a decrease in the trading price of our stock. In addition, the stock repurchase program could have the impact of diminishing our cash reserves, which may impact our ability to finance our growth, complete acquisitions and execute our strategic plan. There can be no assurance that any share repurchases we do elect

to make will enhance stockholder value because the market price of our common stock may decline below the levels at which we repurchased our shares. Although our stock repurchase program is intended to enhance long-term stockholder value, we cannot guarantee that it will do so and short-term stock price fluctuations could reduce the effectiveness of the stock repurchase program.

If securities or industry analysts do not publish research or reports about our business, or publish negative reports about our business, our share price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about us or our business, our market and our competitors. We do not have any control over these analysts. If one or more of the analysts who cover us downgrade our shares of common stock or change their opinion of our shares of common stock, our share price would likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause our share price or trading volume to decline.

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

We are an “emerging growth company,” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”), and we take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We will remain an “emerging growth company” for up to five years, although we will cease to be an “emerging growth company” upon the earliest of (i) the last day of fiscal year 2022, (ii) the last day of the first fiscal year in which our annual gross revenues are \$1.07 billion or more, (iii) the date on which we have, during the previous rolling three-year period, issued more than \$1 billion in non-convertible debt securities or (iv) the date on which we are deemed to be a “large accelerated filer” as defined in the Exchange Act. We cannot predict if investors will find our common stock less attractive or our company less comparable to certain other public companies because we will rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

We incur substantial costs as a result of being a public company.

As a public company, we are incurring significant levels of legal, accounting, insurance and other expenses that we did not incur as a private company. We are subject to the reporting requirements of the Exchange Act, the Sarbanes-Oxley Act, the Dodd-Frank Act, the listing requirements of the Nasdaq Capital Market, and other applicable securities rules and regulations. Compliance with these rules and regulations increases our legal and financial compliance costs, makes some activities more difficult, time-consuming or costly and increases demand on our systems and resources as compared to when we operated as a private company. The Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and operating results. The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal control over financial reporting. In order to maintain and, if required, improve our disclosure controls and procedures and internal control over financial reporting to meet this standard, significant resources and management oversight may be required. As a result, management’s attention may be diverted from other business concerns, which could adversely affect our business and operating results. Although we have already hired additional corporate employees to comply with these requirements, we may need to hire more corporate employees in the future or engage outside consultants, which would increase our costs and expenses.

In addition, changing laws, regulations and standards relating to corporate governance and public disclosure are creating uncertainty for public companies, increasing legal and financial compliance costs and making some activities more time-consuming. These laws, regulations and standards are subject to varying interpretations, in many cases due to their lack of specificity, and, as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. We intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased general and administrative

expenses and a diversion of management's time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to their application and practice, regulatory authorities may initiate legal proceedings against us and our business may be adversely affected.

As a result of disclosure of information in this report and in the filings that we are required to make as a public company, our business, operating results and financial condition have become more visible, which has resulted in, and may in the future result in threatened or actual litigation, including by competitors and other third parties. If any such claims are successful, our business, operating results and financial condition could be adversely affected, and even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the resources of our management and adversely affect our business, operating results and financial condition.

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

We have never declared or paid any cash dividends on our common stock and do not intend to pay any cash dividends in the foreseeable future. We anticipate that we will retain all of our future earnings for use in the development of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of our board of directors. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of our company more difficult, limit attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our certificate of incorporation and bylaws may have the effect of delaying or preventing a change of control or changes in our management. Our certificate of incorporation and bylaws include provisions that:

- establish a classified board of directors so that not all members of our board of directors are elected at one time;
- permit the board of directors to establish the number of directors and fill any vacancies and newly-created directorships;
- provide that directors may only be removed for cause;
- require super-majority voting to amend some provisions in our certificate of incorporation and bylaws;
- authorize the issuance of "blank check" preferred stock that our board of directors could use to implement a stockholder rights plan;
- eliminate the ability of our stockholders to call special meetings of stockholders;
- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and
- establish advance notice requirements for nominations for election to our board of directors or for proposing matters that can be acted upon by stockholders at annual stockholder meetings.

In addition, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which generally prohibits stockholders owning 15% or more of our outstanding voting stock from merging or otherwise combining with us for a period of three years following the date on which the stockholder became a 15% stockholder without the consent of our board of directors. These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management, and otherwise discourage management takeover attempts.

Our certificate of incorporation contains exclusive forum provisions that could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us.

Pursuant to our certificate of incorporation, unless we consent in writing to the selection of an alternative forum, the Court of Chancery of the State of Delaware is the sole and exclusive forum for (1) any derivative action or proceeding brought on our behalf, (2) any action asserting a claim of breach of a fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders, (3) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, our certificate of incorporation or our bylaws or (4) any action asserting a claim governed by the internal affairs doctrine. Our certificate of incorporation further provides that any person or entity purchasing or otherwise acquiring any interest in shares of our common stock is deemed to have notice of and consented to the foregoing provision.

Our certificate of incorporation further provides that the federal district courts of the United States of America will be the exclusive forum for resolving any complaint asserting a cause of action arising under the Securities Act. These forum selection clauses in our certificate of incorporation may limit our stockholders' ability to obtain a favorable judicial forum for disputes with us.

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

(a) Unregistered Sales of Equity Securities

None.

(c) Issuer Purchases of Equity Securities

None.

Item 6. Exhibits

A list of exhibits is set forth below.

Exhibit Index

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File No.	Exhibit	Filing Date	
3.1	Amended and Restated Certificate of Incorporation	8-K	001-38107	3.1	June 13, 2017	
3.2	Amended and Restated Bylaws	8-K	001-38107	3.2	June 13, 2017	
10.1	Second Amendment to Credit Agreement by and between ShotSpotter, Inc. and Umpqua Bank, dated August 14, 2020	8-K	001-38107	10.1	August 14, 2020	
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.					X
32.1*	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.					X
101.INS	Inline XBRL Instance Document (the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document).					X
101.SCH	Inline XBRL Taxonomy Extension Schema Document					X
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document					X
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document					X
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document					X
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document					X
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)					X

* Furnished herewith and not deemed to be “filed” for purposes of Section 18 of the Exchange Act, and shall not be deemed to be incorporated by reference into any filing under the Securities Act, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

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.

SHOTSPOTTER, INC.

Date: November 9, 2020

By: /s/ Ralph A. Clark
Ralph A. Clark
President and Chief Executive Officer

Date: November 9, 2020

By: /s/ Mary Hentges
Mary Hentges
Interim Chief Financial Officer

CERTIFICATION OF PERIODIC REPORT UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Ralph A. Clark, certify that:

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

November 9, 2020

/s/ Ralph A. Clark

Ralph A. Clark

President and Chief Executive Officer

(Principal Executive Officer)

CERTIFICATION OF PERIODIC REPORT UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Mary Hentges, certify that:

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

November 9, 2020

/s/ Mary Hentges

Mary Hentges

Interim Chief Financial Officer

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

Pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, (the "Exchange Act") and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350), I, Ralph A. Clark, President and Chief Executive Officer of ShotSpotter, Inc. (the "Company"), and Mary Hentges, Interim Chief Financial Officer of the Company, each hereby certifies, to the best of his knowledge:

- (1) The Company's Quarterly Report on Form 10-Q for the period ended September 30, 2020, to which this Certification is attached as Exhibit 32.1 (the "Periodic Report"), fully complies with the requirements of Section 13(a) or Section 15(d) of the Exchange Act; and
- (2) The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2020

/s/ Ralph A. Clark

Ralph A. Clark
President and Chief Executive Officer

/s/ Mary Hentges

Mary Hentges
Interim Chief Financial Officer