

Verint Systems Inc. and Subsidiaries

Supplemental Information About Non-GAAP Financial Measures

The following tables include a reconciliation of certain financial measures consisting of non-GAAP revenue, non-GAAP gross profit and gross margin, non-GAAP operating income and operating margin, non-GAAP other income (expense), net, non-GAAP provision (benefit) for income taxes and non-GAAP effective income tax rate, non-GAAP net income attributable to Verint Systems Inc., non-GAAP net income per common share attributable to Verint Systems Inc., adjusted EBITDA, net debt, and constant currency measures prepared in accordance with Generally Accepted Accounting Principles (“GAAP”) to the most directly comparable financial measures not prepared in accordance with GAAP (“non-GAAP”).

We believe these non-GAAP financial measures, used in conjunction with the corresponding GAAP measures, provide investors with useful supplemental information about the financial performance of our business by:

- facilitating the comparison of our financial results and business trends between periods, including by excluding certain items that either can vary significantly in amount and frequency, are based upon subjective assumptions, or in certain cases are unplanned for or difficult to forecast,
- facilitating the comparison of our financial results and business trends with other technology companies who publish similar non-GAAP measures, and
- allowing investors to see and understand key supplementary metrics used by our management to run our business, including for budgeting and forecasting, resource allocation, and compensation matters.

We also make these non-GAAP financial measures available because a number of our investors have informed us that they find this supplemental information useful.

Non-GAAP financial measures should not be considered in isolation as substitutes for, or superior to, comparable GAAP financial measures. The non-GAAP financial measures we present have limitations in that they do not reflect all of the amounts associated with our results of operations as determined in accordance with GAAP, and these non-GAAP financial measures should only be used to evaluate our results of operations in conjunction with the corresponding GAAP financial measures. These non-GAAP financial measures do not represent discretionary cash available to us to invest in the growth of our business, and we may in the future incur expenses similar to or in addition to the adjustments made in these non-GAAP financial measures. Other companies may calculate similar non-GAAP financial measures differently than we do, limiting their usefulness as comparative measures.

Our non-GAAP financial measures are calculated by making the following adjustments to our GAAP financial measures:

Revenue adjustments related to acquisitions. We exclude from our non-GAAP revenue the impact of fair value adjustments required under GAAP relating to acquired customer support contracts, which would have otherwise been recognized on a stand-alone basis. We believe that it is useful for investors to understand the total amount of revenue that we and the acquired company would have recognized on a stand-alone basis under GAAP, absent the accounting adjustment associated with the business acquisition. Our non-GAAP revenue also reflects certain adjustments from aligning an acquired company’s revenue recognition policies to our policies. We believe that our non-GAAP revenue measure helps management and investors understand our revenue trends and serves as a useful measure of ongoing business performance.

Amortization of acquired technology and other acquired intangible assets. When we acquire an entity, we are required under GAAP to record the fair values of the intangible assets of the acquired entity and amortize those assets over their useful lives. We exclude the amortization of acquired intangible assets, including acquired technology, from our non-GAAP financial measures because they are inconsistent in amount and frequency and are significantly impacted by the timing and size of acquisitions. We also exclude these amounts to provide easier comparability of pre- and post-acquisition operating results.

Stock-based compensation expenses. We exclude stock-based compensation expenses related to restricted stock awards, stock bonus programs, bonus share programs, and other stock-based awards from our non-GAAP financial measures. We evaluate our performance both with and without these measures because stock-based compensation is typically a non-cash expense and can vary significantly over time based on the timing, size and nature of awards granted, and is influenced in part by certain factors which are generally beyond our control, such as the volatility of the price of our common stock. In addition, measurement of stock-based compensation is subject to varying valuation methodologies and subjective assumptions, and therefore we believe that excluding stock-based compensation from our non-GAAP financial measures allows for meaningful comparisons of our current operating results to our historical operating results and to other companies in our industry.

Unrealized gains and losses on certain derivatives, net. We exclude from our non-GAAP financial measures unrealized gains and losses on certain foreign currency derivatives which are not designated as hedges under accounting guidance. We exclude unrealized gains and losses on foreign currency derivatives that serve as economic hedges against variability in the cash flows of recognized assets or liabilities, or of forecasted transactions. These contracts, if designated as hedges under accounting guidance, would be considered “cash flow” hedges. These unrealized gains and losses are excluded from our non-GAAP financial measures because they are non-cash transactions which are highly variable from period to period. Upon settlement of these foreign currency derivatives, any realized gain or loss is included in our non-GAAP financial measures.

Amortization of convertible note discount. Our non-GAAP financial measures exclude the amortization of the imputed discount on our convertible notes. Under GAAP, certain convertible debt instruments that may be settled in cash upon conversion are required to be bifurcated into separate liability (debt) and equity (conversion option) components in a manner that reflects the issuer’s assumed non-convertible debt borrowing rate. For GAAP purposes, we are required to recognize imputed interest expense on the difference between our assumed non-convertible debt borrowing rate and the coupon rate on our \$400.0 million of 1.50% convertible notes. This difference is excluded from our non-GAAP financial measures because we believe that this expense is based upon subjective assumptions and does not reflect the cash cost of our convertible debt.

Acquisition Expenses, net. In connection with acquisition activity (including with respect to acquisitions that are not consummated), we incur expenses, including legal, accounting, and other professional fees, integration costs, changes in the fair value of contingent consideration obligations, and other costs. Integration costs may consist of information technology expenses as systems are integrated across the combined entity, consulting expenses, marketing expenses, and professional fees, as well as non-cash charges to write-off or impair the value of redundant assets. We exclude these expenses from our non-GAAP financial measures because they are unpredictable, can vary based on the size and complexity of each transaction, and are unrelated to our continuing operations or to the continuing operations of the acquired businesses.

Restructuring Expenses. We exclude restructuring expenses from our non-GAAP financial measures, which include employee termination costs, facility exit costs, certain professional fees, asset impairment charges, and other costs directly associated with resource realignments incurred in reaction to changing strategies or business conditions. All of these costs can vary significantly in amount and frequency based on the nature of the actions as well as the changing needs of our business and we believe that excluding them provides easier comparability of pre- and post-restructuring operating results.

Impairment Charges and Other Adjustments. We exclude from our non-GAAP financial measures asset impairment charges other than those associated with restructuring or acquisition activity, rent expense for redundant facilities, and gains or losses on sales of property, all of which are unusual in nature and can vary significantly in amount and frequency.

Non-GAAP income tax adjustments. We exclude our GAAP provision (benefit) for income taxes from our non-GAAP measures of net income attributable to Verint Systems Inc., and instead include a non-GAAP provision for income taxes, determined by applying a non-GAAP effective income tax rate to our income before provision for income taxes, as adjusted for the non-GAAP items described above. The non-GAAP effective income tax rate is generally based upon the income taxes we expect to pay in the reporting year. We adjust our non-GAAP effective income tax rate to exclude current-year tax payments or refunds associated with prior-year income tax returns and related amendments which were significantly delayed as a result of our previous extended filing delay. Our GAAP effective income tax rate can vary significantly from year to year as a result of tax law changes, settlements with tax authorities, changes in the geographic mix of earnings including acquisition activity, changes in the projected realizability of deferred tax assets, and other unusual or period-specific events, all of which can vary in size and frequency. We believe that our non-GAAP effective income tax rate removes much of this variability and facilitates meaningful comparisons of operating results across periods. Our non-GAAP effective income tax rate for the year ending January 31, 2017 is currently approximately 9%. We evaluate our non-GAAP effective income tax rate on an ongoing basis and it can change from time to time. Our non-GAAP income tax rate can differ materially from our GAAP effective income tax rate.

Adjusted EBITDA

Adjusted EBITDA is a non-GAAP measure defined as net income (loss) before interest expense, interest income, income taxes, depreciation expense, amortization expense, revenue adjustments related to acquisitions, restructuring expenses, acquisition expenses, and other expenses excluded from our non-GAAP financial measures as described above. We believe that adjusted EBITDA is also commonly used by investors to evaluate operating performance between competitors because it helps reduce variability caused by differences in capital structures, income taxes, stock-based compensation accounting policies, and depreciation and amortization policies. Adjusted EBITDA is also used by credit rating agencies, lenders, and other parties to evaluate our creditworthiness.

Net Debt

Net Debt is a non-GAAP measure defined as the sum of long-term and short-term debt on our consolidated balance sheet, excluding unamortized discounts and issuance costs, less the sum of cash and cash equivalents, restricted cash and bank time deposits, and short-term investments. We use this non-GAAP financial measure to help evaluate our capital structure, financial leverage, and our ability to reduce debt and to fund investing and financing activities, and believe that it provides useful information to investors.

Supplemental Information About Constant Currency

Because we operate on a global basis and transact business in many currencies, fluctuations in foreign currency exchange rates can affect our consolidated U.S. dollar operating results. To facilitate the assessment of our performance excluding the effect of foreign currency exchange rate fluctuations, we calculate our GAAP and non-GAAP revenue, cost of revenue, and operating expenses on both an as-reported basis and a constant currency basis, allowing for comparison of results between periods as if foreign currency exchange rates had remained constant. We perform our constant currency calculations by translating current-period foreign currency results into U.S. dollars using prior-period average foreign currency exchange rates or hedge rates, as applicable, rather than current period exchange rates. We believe that constant currency measures, which exclude the impact of changes in foreign currency exchange rates, facilitate the assessment of underlying business trends.

Unless otherwise indicated, our financial outlook for revenue, operating margin, and diluted earnings per share, which is provided on a non-GAAP basis, reflects foreign currency exchange rates approximately consistent with rates in effect when the outlook is provided.

We also incur foreign exchange gains and losses resulting from the revaluation and settlement of monetary assets and liabilities that are denominated in currencies other than the entity's functional currency. We periodically report our historical non-GAAP diluted net income per share both inclusive and exclusive of these net foreign exchange gains or losses. Our financial outlook for diluted earnings per share includes net foreign exchange gains or losses incurred to date, if any, but does not include potential future gains or losses.

(in thousands, except per share data)

	Three Months Ended		
	April 30, 2016	July 31, 2016	October 31, 2016
<u>Table of Reconciliation from GAAP Revenue to Non-GAAP Revenue</u>			
GAAP revenue	\$ 245,424	\$ 261,921	\$ 258,902
Revenue adjustments related to acquisitions	3,554	2,229	1,127
Non-GAAP revenue	<u>\$ 248,978</u>	<u>\$ 264,150</u>	<u>\$ 260,029</u>

Table of Reconciliation from GAAP Gross Profit to Non-GAAP Gross Profit

GAAP gross profit	\$ 144,730	\$ 159,460	\$ 155,696
GAAP gross margin	59.0%	60.9%	60.1%
Revenue adjustments related to acquisitions	3,554	2,229	1,127
Amortization of acquired technology	9,180	9,134	9,700
Stock-based compensation expenses	1,504	2,262	1,807
Acquisition expenses, net	(191)	193	—
Restructuring expenses	920	122	787
Other adjustments	—	—	—
Non-GAAP gross profit	<u>\$ 159,697</u>	<u>\$ 173,400</u>	<u>\$ 169,117</u>
Non-GAAP gross margin	<u>64.1%</u>	<u>65.6%</u>	<u>65.0%</u>

Table of Reconciliation from GAAP Operating (Loss) Income to Non-GAAP Operating Income

GAAP operating (loss) income	\$ (11,291)	\$ 3,749	\$ 5,525
As a percentage of GAAP revenue	(4.6%)	1.4%	2.1%
Revenue adjustments related to acquisitions	3,554	2,229	1,127
Amortization of acquired technology	9,180	9,134	9,700
Amortization of other acquired intangible assets	11,266	11,466	10,244
Stock-based compensation expenses	15,340	16,388	13,954
Acquisition expenses, net	1,677	2,906	3,480
Restructuring expenses	4,914	2,351	4,955
Other adjustments	155	188	58
Non-GAAP operating income	<u>\$ 34,795</u>	<u>\$ 48,411</u>	<u>\$ 49,043</u>
As a percentage of non-GAAP revenue	<u>14.0%</u>	<u>18.3%</u>	<u>18.9%</u>

Table of Reconciliation from GAAP Other Expense, Net to Non-GAAP Other Expense, Net

GAAP other expense, net	\$ (4,572)	\$ (13,769)	\$ (9,600)
Unrealized losses on derivatives, net	258	134	87
Amortization of convertible note discount	2,614	2,650	2,684
Acquisition expenses, net	101	(15)	(30)
Restructuring expenses	245	118	(144)
Impairment charge	—	2,400	—
Other adjustments	—	—	—
Non-GAAP other expense, net	<u>\$ (1,354)</u>	<u>\$ (8,482)</u>	<u>\$ (7,003)</u>

Table of Reconciliation from GAAP Provision for Income Taxes to Non-GAAP Provision for Income Taxes

GAAP provision for income taxes	\$ 330	\$ 1,058	\$ 3,359
GAAP effective income tax rate	(2.1%)	(10.6%)	(82.4%)
Non-GAAP tax adjustments	2,644	2,586	665
Non-GAAP provision for income taxes	<u>\$ 2,974</u>	<u>\$ 3,644</u>	<u>\$ 4,024</u>
Non-GAAP effective income tax rate	<u>8.9%</u>	<u>9.1%</u>	<u>9.6%</u>

(in thousands, except per share data)

	Three Months Ended		
	April 30, 2016	July 31, 2016	October 31, 2016
<u>Table of Reconciliation from GAAP Net Loss Attributable to Verint Systems Inc. to Non-GAAP Net Income Attributable to Verint Systems Inc.</u>			
GAAP net loss attributable to Verint Systems Inc.	\$ (17,456)	\$ (11,705)	\$ (8,237)
Revenue adjustments related to acquisitions	3,554	2,229	1,127
Amortization of acquired technology	9,180	9,134	9,700
Amortization of other acquired intangible assets	11,266	11,466	10,244
Stock-based compensation expenses	15,340	16,388	13,954
Unrealized losses on derivatives, net	258	134	87
Amortization of convertible note discount	2,614	2,650	2,684
Acquisition expenses, net	1,778	2,891	3,450
Restructuring expenses	5,159	2,469	4,811
Impairment charge	—	2,400	—
Other adjustments	155	188	58
Non-GAAP tax adjustments	(2,644)	(2,586)	(665)
Total GAAP net loss adjustments	46,660	47,363	45,450
Non-GAAP net income attributable to Verint Systems Inc.	\$ 29,204	\$ 35,658	\$ 37,213

Table Comparing GAAP Diluted Net Loss Per Common Share Attributable to Verint Systems Inc. to Non-GAAP Diluted Net Income Per Common Share Attributable to Verint Systems Inc.

GAAP diluted net loss per common share attributable to Verint Systems Inc.	\$ (0.28)	\$ (0.19)	\$ (0.13)
Non-GAAP diluted net income per common share attributable to Verint Systems Inc.	\$ 0.46	\$ 0.57	\$ 0.59

GAAP diluted weighted-average shares used in computing net loss per common share attributable to Verint Systems Inc.	62,258	62,668	62,895
Additional weighted-average anti-dilutive shares applicable to non-GAAP net income per common share attributable to Verint Systems Inc.	676	260	355
Non-GAAP diluted weighted-average shares used in computing net income per common share attributable to Verint Systems Inc.	62,934	62,928	63,250

Table of Reconciliation from GAAP Net Loss Attributable to Verint Systems Inc. to Adjusted EBITDA

GAAP net loss attributable to Verint Systems Inc.	\$ (17,456)	\$ (11,705)	\$ (8,237)
Net income attributable to noncontrolling interest	1,263	627	803
Provision for income taxes	330	1,058	3,359
Other expense, net	4,572	13,769	9,600
Depreciation and amortization ⁽¹⁾	27,547	27,894	27,566
Revenue adjustments related to acquisitions	3,554	2,229	1,127
Stock-based compensation expenses	15,340	16,388	13,954
Acquisition expenses, net	1,677	2,906	3,480
Restructuring expenses	4,913	2,348	4,289
Other adjustments	155	188	58
Adjusted EBITDA	\$ 41,895	\$ 55,702	\$ 55,999

Table of Reconciliation from Gross Debt to Net Debt

	April 30, 2016	July 31, 2016	October 31, 2016
Current maturities of long-term debt	\$ 4,171	\$ 5,186	\$ 4,709
Long-term debt	737,878	739,914	742,067
Unamortized debt discounts and issuance costs	70,108	67,021	63,816
Gross debt	812,157	812,121	810,592
Less:			
Cash and cash equivalents	323,905	340,116	295,829
Restricted cash and bank time deposits	11,089	8,957	14,628
Short-term investments	48,087	27,337	10,318
Net debt	\$ 429,076	\$ 435,711	\$ 489,817

(1) Adjusted for financing fee amortization.