Workday, Inc.
Form 10-Q
December 03, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended October 31, 2018
OR
¨ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number: 001-35680

Workday, Inc.
(Exact name of registrant as specified in its charter)

Delaware	20-2480422
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

6110 Stoneridge Mall Road
Pleasanton, California 94588
(Address of principal executive offices)
Telephone Number (925) 951-9000
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x 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	x	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨
		Emerging growth company	¨

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 x

As of November 30, 2018, there were approximately 220 million shares of the registrant's common stock outstanding, net of treasury stock.

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Workday, Inc.

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
Workday, Inc.
Condensed Consolidated Balance Sheets
(in thousands)
(unaudited)

	October 31, 2018	January 31, 2018
Assets		
Current assets:		
Cash and cash equivalents	$540,430	$1,134,355
Marketable securities	1,041,709	2,133,495
Trade and other receivables, net	486,044	528,208
Deferred costs	70,608	63,060
Prepaid expenses and other current assets	132,488	97,860
Total current assets	2,271,279	3,956,978
Property and equipment, net	735,443	546,609
Deferred costs, noncurrent	151,150	140,509
Acquisition-related intangible assets, net	332,583	34,234
Goodwill	1,377,615	159,376
Other assets	132,229	109,718
Total assets	$5,000,299	$4,947,424
Liabilities and stockholders’ equity		
Current liabilities:		
Accounts payable	$28,779	$20,998
Accrued expenses and other current liabilities	131,170	121,879
Accrued compensation	205,602	148,247
Unearned revenue	1,460,650	1,426,241
Current portion of convertible senior notes, net	229,684	341,509
Total current liabilities	2,055,885	2,058,874
Convertible senior notes, net	961,139	1,149,845
Unearned revenue, noncurrent	109,694	110,906
Other liabilities	40,432	47,434
Total liabilities	3,167,150	3,367,059
Stockholders’ equity:		
Common stock	220	211
Additional paid-in capital	4,049,785	3,354,423
Treasury stock	(178,801)	—
Accumulated other comprehensive income (loss)	3,768	(46,413)
Accumulated deficit	(2,041,823)	(1,727,856)
Total stockholders’ equity	1,833,149	1,580,365
Total liabilities and stockholders’ equity	$5,000,299	$4,947,424

See Notes to Condensed Consolidated Financial Statements

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Workday, Inc.
Condensed Consolidated Statements of Operations
(in thousands, except per share data)
(unaudited)

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Revenues:				
Subscription services	$624,416	$463,568	$1,712,224	$1,297,831
Professional services	118,773	91,821	321,328	262,739
Total revenues	743,189	555,389	2,033,552	1,560,570
Costs and expenses [1]:				
Costs of subscription services	103,310	71,898	271,078	197,627
Costs of professional services	119,691	91,657	330,124	260,834
Product development	318,003	239,588	874,427	657,130
Sales and marketing	246,156	176,121	641,391	503,782
General and administrative	138,784	56,184	259,533	163,085
Total costs and expenses	925,944	635,448	2,376,553	1,782,458
Operating loss	(182,755)	(80,059)	(343,001)	(221,888)
Other income (expense), net	26,617	(3,742)	24,382	(4,467)
Loss before provision for (benefit from) income taxes	(156,138)	(83,801)	(318,619)	(226,355)
Provision for (benefit from) income taxes	(2,807)	1,745	(4,722)	5,767
Net loss	$(153,331)	$(85,546)	$(313,897)	$(232,122)
Net loss per share, basic and diluted	$(0.70)	$(0.41)	$(1.46)	$(1.12)
Weighted-average shares used to compute net loss per share, basic and diluted	217,694	209,188	215,588	206,715

[1] Costs and expenses include share-based compensation expenses as follows:

Costs of subscription services	$10,205	$6,899	$26,603	$19,170
Costs of professional services	15,702	9,956	39,012	27,278
Product development	86,304	59,116	230,169	167,068
Sales and marketing	38,720	25,517	93,699	74,618
General and administrative	57,993	20,991	99,163	63,656

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Workday, Inc.
Condensed Consolidated Statements of Comprehensive Loss
(in thousands)
(unaudited)

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Net loss	$(153,331)	$(85,546)	$(313,897)	$(232,122)
Other comprehensive income (loss), net of tax:				
Net change in foreign currency translation adjustment	(551)	(504)	(1,812)	462
Net change in unrealized gains (losses) on available-for-sale debt securities, net of tax provision of $10, $0, $294, and $0, respectively	375	(302)	1,281	(931)
Net change in market value of effective foreign currency forward exchange contracts, net of tax provision of $2,339, $0, $7,244, and $0, respectively	16,375	6,693	50,712	(17,912)
Other comprehensive income (loss), net of tax	16,199	5,887	50,181	(18,381)
Comprehensive loss	$(137,132)	$(79,659)	$(263,716)	$(250,503)

See Notes to Condensed Consolidated Financial Statements

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Workday, Inc.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Cash flows from operating activities				
Net loss	$(153,331)	$(85,546)	$(313,897)	$(232,122)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:				
Depreciation and amortization	57,602	34,727	138,492	100,025
Share-based compensation expenses	187,971	122,479	467,693	351,790
Amortization of deferred costs	18,165	14,519	51,586	42,165
Amortization of debt discount and issuance costs	12,342	12,257	47,971	25,992
Other	(30,990)	(1,133)	(45,173)	5,052
Changes in operating assets and liabilities, net of business combinations:				
Trade and other receivables, net	(9,379)	19,070	54,565	59,463
Deferred costs	(33,226)	(19,245)	(69,775)	(50,063)
Prepaid expenses and other assets	(5,985)	(11,355)	(2,943)	(23,373)
Accounts payable	(12,148)	(7,383)	1,793	2,830
Accrued expenses and other liabilities	63,896	59,171	60,341	49,788
Unearned revenue	19,379	6,470	(34,508)	7,632
Net cash provided by (used in) operating activities	114,296	144,031	356,145	339,179
Cash flows from investing activities				
Purchases of marketable securities	(89,294)	(930,783)	(1,523,636)	(1,829,231)
Maturities of marketable securities	369,771	372,389	1,711,652	1,185,730
Sales of marketable securities	3,388	32,886	945,685	222,823
Owned real estate projects	(37,302)	(27,616)	(126,072)	(80,151)
Capital expenditures, excluding owned real estate projects	(55,427)	(36,356)	(157,635)	(105,477)
Business combinations, net of cash acquired	(1,447,600)	—	(1,474,337)	—
Purchase of other intangible assets	—	—	(1,000)	—
Purchases of non-marketable equity and other investments	(29,375)	(5,272)	(32,775)	(10,722)
Sales and maturities of non-marketable equity and other investments	17,771	294	17,771	1,026
Other	(11)	(1,000)	(11)	(1,000)
Net cash provided by (used in) investing activities	(1,268,079)	(595,458)	(640,358)	(617,002)
Cash flows from financing activities				
Proceeds from borrowings on convertible senior notes, net of issuance costs	—	1,132,101	—	1,132,101
Proceeds from issuance of warrants	—	80,805	—	80,805
Purchase of convertible senior notes hedges	—	(175,530)	—	(175,530)
Payments on convertible senior notes	(3)	—	(350,008)	—
Proceeds from issuance of common stock from employee equity plans	2,767	1,974	44,064	36,501
Other	(60)	(36)	(176)	(112)
Net cash provided by (used in) financing activities	2,704	1,039,314	(306,120)	1,073,765
Effect of exchange rate changes	(213)	(322)	(795)	261

Net increase (decrease) in cash, cash equivalents, and restricted cash	(1,151,292)	587,565	(591,128)	796,203
Cash, cash equivalents, and restricted cash at the beginning of period	1,695,818	750,532	1,135,654	541,894
Cash, cash equivalents, and restricted cash at the end of period	$544,526	$1,338,097	$544,526	$1,338,097

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	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Supplemental cash flow data				
Cash paid for interest, net of amounts capitalized	$1	$ 18	$34	$ 64
Cash paid for income taxes	633	651	3,839	3,259
Non-cash investing and financing activities:				
Vesting of early exercised stock options	$—	$ 106	$—	$ 670
Purchases of property and equipment, accrued but not paid	60,800	47,055	60,800	47,055
Non-cash additions to property and equipment	2,316	449	2,679	1,276

	October 31,	
	2018	2017
Reconciliation of cash, cash equivalents, and restricted cash as shown in the statements of cash flows		
Cash and cash equivalents	$540,430	$1,336,984
Restricted cash included in Prepaid expenses and other current assets	3,966	—
Restricted cash included in Other assets	130	1,113
Total cash, cash equivalents, and restricted cash	$544,526	$1,338,097

See Notes to Condensed Consolidated Financial Statements

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Workday, Inc.

Notes to Condensed Consolidated Financial Statements

Note 1. Overview and Basis of Presentation

Company and Background

Workday provides financial management, human capital management, and analytics applications designed for the world's largest companies, educational institutions, and government agencies. We offer innovative and adaptable technology focused on the consumer internet experience and cloud delivery model. Our applications are designed for global enterprises to manage complex and dynamic operating environments. We provide our customers highly adaptable, accessible, and reliable applications to manage critical business functions that enable them to optimize their financial and human capital resources. We were originally incorporated in March 2005 in Nevada and in June 2012, we reincorporated in Delaware. As used in this report, the terms "Workday," "registrant," "we," "us," and "our" mean Workday, Inc. and its subsidiaries unless the context indicates otherwise.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP") and applicable rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim financial reporting. The condensed consolidated financial statements include the results of Workday, Inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. In the opinion of our management, the information contained herein reflects all adjustments necessary for a fair presentation of Workday's results of operations, financial position, and cash flows. All such adjustments are of a normal, recurring nature. The results of operations for the quarter ended October 31, 2018 shown in this report are not necessarily indicative of the results to be expected for the full year ending January 31, 2019. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements in our Annual Report on Form 10-K for the year ended January 31, 2018, filed with the SEC on March 14, 2018.

Certain prior period amounts reported in our condensed consolidated financial statements have been reclassified to conform to current period presentation.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires us to make certain estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the condensed consolidated financial statements as well as the reported amounts of revenues and expenses during the reporting period. These estimates include, but are not limited to, the determination of the period of benefit for deferred commissions, certain assumptions used in the valuation of equity awards, and the fair value of assets acquired and liabilities assumed through business combinations. Actual results could differ from those estimates and such differences could be material to our condensed consolidated financial position and results of operations.

Segment Information

We operate in one operating segment, cloud applications. Operating segments are defined as components of an enterprise where separate financial information is evaluated regularly by the chief operating decision maker, who is our chief executive officer, in deciding how to allocate resources and assessing performance. Our chief operating decision maker allocates resources and assesses performance based upon discrete financial information at the consolidated level.

Note 2. Accounting Standards

Recently Adopted Accounting Pronouncements

In January 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (Subtopic 825-10), which amends various aspects of the recognition, measurement, presentation, and disclosure of financial instruments. As of February 1, 2018, we adopted the applicable provisions of ASU No. 2016-01 as follows:

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- Marketable equity investments (readily determinable fair values): For our equity investments previously classified as available-for-sale equity investments, we are required to account for changes in fair value of these investments in the condensed consolidated statements of operations. We have applied the modified retrospective transition method upon adoption, resulting in no impact to our condensed consolidated financial statements as of February 1, 2018.
- Non-marketable equity investments (no readily determinable fair values): For our equity investments previously classified as cost method investments that do not qualify for the net asset value practical expedient, we measure them at fair value or the measurement alternative. The measurement alternative is defined as cost, less impairment, adjusted for observable price changes from orderly transactions for identical or similar investments of the same issuer. Adjustments resulting from impairment, fair value, or observable price changes are accounted for in the condensed consolidated statements of operations. We adopted the guidance prospectively effective February 1, 2018, and there was no impact to our condensed consolidated financial statements.

Going forward, the impact of this new standard could result in volatility in the condensed consolidated statements of operations.

In October 2016, the FASB issued ASU No. 2016-16, Intra-Entity Transfers of Assets Other Than Inventory (Topic 740), which requires entities to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Prior to the issuance of this ASU, existing guidance prohibited the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset had been sold to an outside party. We adopted this new standard effective February 1, 2018 using the modified retrospective transition method, resulting in a $0.4 million cumulative-effect adjustment to Accumulated deficit as of February 1, 2018.

Recently Issued Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which requires the recognition of lease assets and lease liabilities on the balance sheet by lessees for those leases currently classified as operating leases under Accounting Standards Codification Topic 840 Leases. The guidance is effective for our fiscal year beginning February 1, 2019. We plan to adopt this new standard in the first quarter of our fiscal 2020 using a modified retrospective method, and we will not restate comparative periods. We continue to evaluate the effect of adopting this guidance on our condensed consolidated financial statements and related disclosures. Upon adoption, we will recognize right-of-use assets and operating lease liabilities on our condensed consolidated balance sheets, which will increase our total assets and total liabilities. We are evaluating the accounting, transition, and disclosure requirements of this standard and cannot currently estimate the financial statement impact of adoption.

In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815), to better align an entity’s risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The guidance is effective for our fiscal year beginning February 1, 2019 and must be applied using a modified retrospective approach. We plan to adopt this new standard in the first quarter of our fiscal 2020. We are evaluating the accounting, transition, and disclosure requirements of this standard and cannot currently estimate the financial statement impact of adoption.

In February 2018, the FASB issued ASU No. 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which provides entities the option to reclassify tax effects stranded in accumulated other comprehensive income as a result of the 2017 Tax Cuts and Jobs Act (the “Tax Act”) to retained earnings. The guidance is effective for our fiscal year beginning February 1, 2019 and must be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Act is recognized. We plan to adopt the new standard in the first quarter of our fiscal 2020 and do not expect it to have a material impact on our condensed consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-07, Compensation - Stock Compensation (Topic 718): Improvements to Non-employee Share-Based Payment Accounting, which expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from non-employees, with certain exceptions. The guidance is effective for our fiscal year beginning February 1, 2019. We plan to adopt this new standard in the first quarter of our fiscal 2020 and do not expect it to have a material impact on our condensed consolidated financial statements.

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Note 3. Investments

Debt Securities

As of October 31, 2018, debt securities consisted of the following (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Aggregate Fair Value
U.S. agency obligations	$188,241	$ 1	$ (375)	$187,867
U.S. treasury securities	376,887	—	(437)	376,450
Corporate bonds	402,034	6	(1,027)	401,013
Commercial paper	283,260	—	—	283,260
	$1,250,422	$ 7	$ (1,839)	$1,248,590
Included in cash and cash equivalents	$239,214	$ —	$ —	$239,214
Included in marketable securities	$1,011,208	$ 7	$ (1,839)	$1,009,376

As of January 31, 2018, debt securities consisted of the following (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Aggregate Fair Value
U.S. agency obligations	$683,551	$ —	$ (1,127)	$682,424
U.S. treasury securities	797,977	—	(1,142)	796,835
Corporate bonds	470,259	16	(1,154)	469,121
Commercial paper	602,727	—	—	602,727
	$2,554,514	$ 16	$ (3,423)	$2,551,107
Included in cash and cash equivalents	$417,613	$ —	$ (1)	$417,612
Included in marketable securities	$2,136,901	$ 16	$ (3,422)	$2,133,495

We do not believe the unrealized losses represent other-than-temporary impairments based on our evaluation of available evidence, which includes our intent to hold these investments to maturity as of October 31, 2018. The unrealized losses on debt securities that have been in a net loss position for 12 months or more were not material as of October 31, 2018. We classify our debt securities as available-for-sale at the time of purchase and reevaluate such classification as of each balance sheet date. We consider all debt securities as available for use in current operations, including those with maturity dates beyond one year, and therefore classify these securities as current assets in the accompanying condensed consolidated balance sheets. Debt securities included in Marketable securities on the condensed consolidated balance sheets consist of securities with original maturities at the time of purchase greater than three months, and the remainder of the securities is included in Cash and cash equivalents. We sold $3 million and $33 million of our debt securities during the three months ended October 31, 2018 and 2017, respectively, and $946 million and $223 million of our debt securities during the nine months ended October 31, 2018 and 2017, respectively. The realized gains and losses from the sales were immaterial.

Equity Investments

Money market funds and marketable equity investments are investments with readily determinable fair values. Non-marketable equity investments consist of investments in privately held companies without readily determinable fair values.

Equity investments consisted of the following (in thousands):

	Condensed Consolidated Balance Sheets Location	October 31, 2018	January 31, 2018
Money market funds	Cash and cash equivalents	$ 194,272	$551,804
Marketable equity investments	Marketable securities	32,333	—

Non-marketable equity investments	Other assets	27,661	28,005
		$ 254,266	$579,809

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There were no adjustments made to the carrying value of the non-marketable equity investments as measured under the measurement alternative during the three and nine months ended October 31, 2018. Realized and unrealized gains and losses associated with our equity investments consisted of the following (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Net realized gains (losses) recognized on equity investments sold	$8,193	$194	$8,193	$720
Net unrealized gains (losses) recognized on equity investments held	20,333	(100)	20,333	(100)
Total net gains (losses) recognized in other income (expense), net	$28,526	$94	$28,526	$620

Note 4. Fair Value Measurements

We measure our cash equivalents, marketable securities, and foreign currency derivative contracts at fair value at each reporting period using a fair value hierarchy that requires that we maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's classification within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Three levels of inputs may be used to measure fair value:

Level 1 — Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 — Other inputs that are directly or indirectly observable in the marketplace.

Level 3 — Unobservable inputs that are supported by little or no market activity.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents information about our assets and liabilities that are measured at fair value on a recurring basis and their assigned levels within the valuation hierarchy as of October 31, 2018 (in thousands):

Description	Level 1	Level 2	Level 3	Total
U.S. agency obligations	$—	$187,867	$ —	$187,867
U.S. treasury securities	376,450	—	—	376,450
Corporate bonds	—	401,013	—	401,013
Commercial paper	—	283,260	—	283,260
Money market funds	194,272	—	—	194,272
Marketable equity investments	32,333	—	—	32,333
Foreign currency derivative assets	—	36,416	—	36,416
Total assets	$603,055	$908,556	$ —	$1,511,611
Foreign currency derivative liabilities	$—	$540	$ —	$540
Total liabilities	$—	$540	$ —	$540

The following table presents information about our assets and liabilities that are measured at fair value on a recurring basis and their assigned levels within the valuation hierarchy as of January 31, 2018 (in thousands):

Description	Level 1	Level 2	Level 3	Total
U.S. agency obligations	$—	$682,424	$ —	$682,424
U.S. treasury securities	796,835	—	—	796,835
Corporate bonds	—	469,121	—	469,121
Commercial paper	—	602,727	—	602,727
Money market funds	551,804	—	—	551,804
Foreign currency derivative assets	—	98	—	98
Total assets	$1,348,639	$1,754,370	$ —	$3,103,009
Foreign currency derivative liabilities	$—	$32,912	$ —	$32,912
Total liabilities	$—	$32,912	$ —	$32,912

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Fair Value Measurements of Other Financial Instruments

The following table presents the carrying amounts and estimated fair values of our financial instruments that are not recorded at fair value on the condensed consolidated balance sheets (in thousands):

	October 31, 2018		January 31, 2018	
	Net Carrying Amount	Estimated Fair Value	Net Carrying Amount	Estimated Fair Value
0.75% Convertible senior notes	$ —	$ —	$ 341,509	$ 504,994
1.50% Convertible senior notes	229,684	418,310	221,378	385,550
0.25% Convertible senior notes	961,139	1,274,798	928,467	1,200,577

In June 2013, we completed an offering of $350 million of 0.75% convertible senior notes due July 15, 2018 (“2018 Notes”), which were subsequently converted by note holders during the second quarter of fiscal 2019. In June 2013, concurrent with the 2018 Notes offering, we issued $250 million of 1.50% convertible senior notes due July 15, 2020 (“2020 Notes”). In September 2017, we completed an offering of $1.15 billion of 0.25% convertible senior notes due October 1, 2022 (“2022 Notes” and together with the 2018 Notes and 2020 Notes, the “Notes”). The estimated fair values of the Notes, which we have classified as Level 2 financial instruments, were determined based on the quoted bid prices of the Notes in an over-the-counter market on the last trading day of each reporting period. The if-converted value of the 2020 Notes exceeded the principal amount by $157 million. The if-converted value of the 2022 Notes was less than the principal amount by $110 million. The if-converted values were determined based on the closing price of our common stock of $133.02 on October 31, 2018. For further information, see Note 11.

Note 5. Deferred Costs

Deferred costs, which primarily consist of deferred sales commissions, were $222 million and $204 million as of October 31, 2018 and January 31, 2018, respectively. Amortization expense for the deferred costs was $18 million and $14 million for the three months ended October 31, 2018 and 2017, respectively, and $52 million and $42 million for the nine months ended October 31, 2018 and 2017, respectively. There was no impairment loss in relation to the costs capitalized for the periods presented.

Note 6. Property and Equipment, Net

Property and equipment, net consisted of the following (in thousands):

	October 31, 2018	January 31, 2018
Land	$ 18,593	$ 8,451
Buildings	389,320	255,093
Computers, equipment, and software	510,677	425,025
Furniture and fixtures	36,557	34,809
Leasehold improvements	154,108	132,209
Property and equipment, gross [1]	1,109,255	855,587
Less accumulated depreciation and amortization	(373,812)	(308,978)
Property and equipment, net	$ 735,443	$ 546,609

(1) Property and equipment, gross included construction-in-progress for owned real estate projects of $297 million and $177 million that had not yet been placed in service as of October 31, 2018 and January 31, 2018, respectively.

Depreciation expense totaled $38 million and $30 million for the three months ended October 31, 2018 and 2017, respectively, and $107 million and $85 million for the nine months ended October 31, 2018 and 2017, respectively. Interest costs capitalized to property and equipment totaled $3 million for each of the three month periods ended October 31, 2018 and 2017, and $7 million and $6 million for the nine months ended October 31, 2018 and 2017, respectively.

Note 7. Business Combination

On August 1, 2018, we acquired all outstanding stock of Adaptive Insights, Inc. (“Adaptive Insights”) for $1.5 billion. The acquisition of Adaptive Insights, a cloud-based provider of business planning software strengthens our product portfolio and will enable our customers to better plan, execute, and analyze in one system.

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The purchase consideration transferred consisted of the following (in thousands):

	Purchase Consideration
Cash paid to common and preferred stockholders, warrant holders, and vested option holders	$ 1,408,422
Debt repaid by Workday on behalf of Adaptive Insights	53,696
Transaction costs paid by Workday on behalf of Adaptive Insights	23,375
Fair value of assumed Adaptive Insights awards attributable to pre-combination services (1)	5,424
Total purchase consideration	$ 1,490,917

(1) The assumed awards were primarily options, which were fair valued based upon the Black-Scholes option-pricing model.

The purchase consideration was preliminarily allocated to the tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of the acquisition date, with the excess recorded to goodwill as shown below. The fair values of assets acquired and liabilities assumed, including current income taxes payable and deferred taxes, may change as additional information is received during the measurement period. The measurement period will end no later than one year from the acquisition date.

Assets acquired:	(in thousands)
Cash and cash equivalents	$37,892
Trade and other receivables, net	23,042
Prepaid expenses and other current assets and other assets	4,619
Property and equipment, net	2,246
Acquisition-related intangible assets, net	316,000
Total assets acquired	$383,799
Liabilities assumed:	
Accounts payable	$3,115
Accrued expenses and other current liabilities	9,092
Accrued compensation	13,545
Unearned revenue (1)	67,754
Other liabilities	1,919
Total liabilities assumed	95,425
Net assets acquired, excluding goodwill	288,374
Total purchase consideration	1,490,917
Estimated goodwill (2)	$1,202,543

(1) The cost build-up method was used to determine the fair value of unearned revenue.

(2) The goodwill recognized was primarily attributable to the value of the acquired workforce, the opportunity to expand our customer base, and the ability to add breadth and depth to our product portfolio by accelerating our financial planning roadmap. The goodwill is not deductible for U.S. federal income tax purposes.

The fair value of the separately identifiable finite-lived intangible assets acquired and estimated useful lives are as follows (in thousands, except years):

	Estimated Fair Values	Estimated Useful Lives
Trade name	$12,000	1.5
Developed technology	105,000	5.0
Customer relationships	188,000	9.0 - 10.0
Backlog	11,000	2.0
Total acquisition-related intangible assets	$316,000	

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The fair values of the trade name and developed technology were determined utilizing the relief-from-royalty method, and the multi-period excess earnings method was utilized to fair value customer relationships and backlog. The valuation model inputs required the application of considerable judgment by management. The acquired finite-lived intangible assets have a total weighted-average amortization period of 7.6 years.

We have included the financial results of Adaptive Insights in our condensed consolidated financial statements from the date of acquisition. One-time acquisition related transaction costs of $23 million and $25 million were expensed as incurred during the three and nine months ended October 31, 2018, respectively, and were recorded within general and administrative expense in our condensed consolidated statements of operations.

Unaudited Pro Forma Financial Information

The unaudited pro forma financial information shown below summarizes the combined results of operations for Workday and Adaptive Insights as if the closing of the acquisition had occurred on February 1, 2017, the first day of our fiscal year 2018. The unaudited pro forma financial information includes adjustments that are directly attributable to the business combination and are factually supportable. The adjustments primarily reflect the amortization of acquired intangible assets, share-based compensation expense for replacement awards, as well as the pro forma tax impact for such adjustments. The pro forma financial information reflects $67 million of nonrecurring expenses related to acquisition costs and certain compensation expenses.

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
	(in thousands, except per share data)			
Total revenues	$743,189	$578,551	$2,097,429	$1,620,094
Net loss	(92,417)	(121,309)	(320,908)	(409,032)
Net loss per share, basic and diluted	$(0.42)	$(0.58)	$(1.49)	$(1.98)

The unaudited pro forma condensed financial information is presented for illustrative purposes only and is not necessarily indicative of the results of operations that would have been realized if the acquisition had taken place on February 1, 2017.

Note 8. Acquisition-related Intangible Assets, Net

Acquisition-related intangible assets, net consisted of the following (in thousands):

	October 31, 2018	January 31, 2018
Developed technology	$186,800	$69,700
Customer relationships	189,000	1,000
Trade name	12,000	—
Backlog	11,000	—
	398,800	70,700
Less accumulated amortization	(66,217)	(36,466)
Acquisition-related intangible assets, net	$332,583	$34,234

Amortization expense related to acquisition-related intangible assets was $20 million and $4 million for the three months ended October 31, 2018 and 2017, respectively, and $30 million and $14 million for the nine months ended October 31, 2018 and 2017, respectively.

As of October 31, 2018, our future estimated amortization expense related to acquisition-related intangible assets is as follows (in thousands):

Fiscal Period:	
2019	$19,343
2020	68,856
2021	48,142
2022	43,733
2023	41,009

Thereafter	111,500
Total	$332,583

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Note 9. Other Assets

Other assets consisted of the following (in thousands):

	October 31, 2018	January 31, 2018
Non-marketable equity and other investments	$ 40,203	$ 29,205
Prepayments for computing infrastructure platform	10,738	13,588
Technology patents, net	10,980	11,217
Acquired land leasehold interest, net	9,491	9,570
Deposits	4,966	4,492
Net deferred tax assets	3,726	1,884
Other	52,125	39,762
Total	$ 132,229	$ 109,718

Note 10. Derivative Instruments

We conduct business on a global basis in multiple foreign currencies, subjecting Workday to foreign currency risk. To mitigate this risk, we utilize hedging contracts as described below. We do not enter into any derivatives for trading or speculative purposes.

Our foreign currency contracts are classified within Level 2 of the fair value hierarchy because the valuation inputs are based on quoted prices and market observable data of similar instruments in active markets, such as currency spot and forward rates.

Cash Flow Hedges

We are exposed to foreign currency fluctuations resulting from customer contracts denominated in foreign currencies. We have a hedging program in which we enter into foreign currency forward contracts related to certain customer contracts. We designate these forward contracts as cash flow hedging instruments as the accounting criteria for such designation have been met. The effective portion of the gains or losses resulting from changes in the fair value of these hedges is recorded in Accumulated other comprehensive income (loss) (“OCI”) on the condensed consolidated balance sheets and will be subsequently reclassified to the related revenue line item on the condensed consolidated statements of operations in the same period that the underlying revenues are earned. The changes in value of these contracts resulting from changes in forward points are excluded from the assessment of hedge effectiveness and are recorded as incurred in Other income (expense), net on the condensed consolidated statements of operations. Cash flows from such forward contracts are classified as operating activities.

As of October 31, 2018 and January 31, 2018, we had outstanding foreign currency forward contracts designated as cash flow hedges with total notional values of $711 million and $549 million, respectively. All contracts have maturities not greater than 36 months. The notional value represents the amount that will be bought or sold upon maturity of the forward contract.

Foreign Currency Forward Contracts not Designated as Hedges

We also enter into foreign currency forward contracts to hedge a portion of our net outstanding monetary assets and liabilities. These forward contracts are not designated as hedging instruments under applicable accounting guidance, and therefore all changes in the fair value of the forward contracts are recorded in Other income (expense), net on the condensed consolidated statements of operations. These forward contracts are intended to offset the foreign currency gains or losses associated with the underlying monetary assets and liabilities. Cash flows from such forward contracts are classified as operating activities.

As of October 31, 2018 and January 31, 2018, we had outstanding forward contracts not designated as hedges with total notional values of $213 million and $75 million, respectively.

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The fair values of outstanding derivative instruments were as follows (in thousands):

	Condensed Consolidated Balance Sheets Location	October 31, 2018	January 31, 2018
Derivative Assets:			
Foreign currency forward contracts designated as cash flow hedges	Prepaid expenses and other current assets	$ 18,417	$ 15
Foreign currency forward contracts designated as cash flow hedges	Other assets	16,481	4
Foreign currency forward contracts not designated as hedges	Prepaid expenses and other current assets	1,445	79
Foreign currency forward contracts not designated as hedges	Other assets	73	—
Total Derivative Assets		$ 36,416	$ 98
Derivative Liabilities:			
Foreign currency forward contracts designated as cash flow hedges	Accrued expenses and other current liabilities	$ 213	$ 18,355
Foreign currency forward contracts designated as cash flow hedges	Other liabilities	10	11,650
Foreign currency forward contracts not designated as hedges	Accrued expenses and other current liabilities	317	2,805
Foreign currency forward contracts not designated as hedges	Other liabilities	—	102
Total Derivative Liabilities		$ 540	$ 32,912

Gains (losses) associated with foreign currency forward contracts designated as cash flow hedges were as follows (in thousands):

	Condensed Consolidated Statements of Operations and Statements of Comprehensive Loss Locations	Three Months Ended October 31,		Nine Months Ended October 31,	
		2018	2017	2018	2017
Gains (losses) recognized in OCI (effective portion) [(1)]	Net change in market value of effective foreign currency forward exchange contracts	$16,341	$7,372	$52,506	$(16,526)
Gains (losses) reclassified from OCI into income (effective portion)	Revenues	(2,373)	679	(5,450)	1,386
Gains (losses) recognized in income (amount excluded from effectiveness testing and ineffective portion)	Other income (expense), net	2,700	350	8,958	1,740

(1) Of the total effective portion of foreign currency forward contracts designated as cash flow hedges as of October 31, 2018, net gains of $0.4 million are expected to be reclassified out of OCI within the next 12 months.

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Gains (losses) associated with foreign currency forward contracts not designated as cash flow hedges were as follows (in thousands):

Derivative Type	Condensed Consolidated Statements of Operations Location	Three Months Ended October 31, 2018	2017	Nine Months Ended October 31, 2018	2017
Foreign currency forward contracts not designated as hedges	Other income (expense), net	$2,488	$829	$6,166	$(1,796)

We are subject to master netting agreements with certain counterparties of the foreign exchange contracts, under which we are permitted to net settle transactions of the same currency with a single net amount payable by one party to the other. It is our policy to present the derivatives gross on the condensed consolidated balance sheets. Our foreign currency forward contracts are not subject to any credit contingent features or collateral requirements. We manage our exposure to counterparty risk by entering into contracts with a diversified group of major financial institutions and by actively monitoring outstanding positions.

As of October 31, 2018, information related to these offsetting arrangements was as follows (in thousands):

	Gross Amounts of Recognized Assets	Gross Amounts Offset on the Condensed Consolidated Balance Sheets	Net Amounts of Assets Presented on the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset on the Condensed Consolidated Balance Sheets: Financial Instruments	Cash Collateral Received	Net Assets Exposed
Derivative Assets:						
Counterparty A	$ 8,172	$ —	$ 8,172	$ (91)	$ —	$ 8,081
Counterparty B	23,879	—	23,879	(337)	—	23,542
Counterparty C	4,365	—	4,365	(112)	—	4,253
Total	$ 36,416	$ —	$ 36,416	$ (540)	$ —	$ 35,876

	Gross Amounts of Recognized Liabilities	Gross Amounts Offset on the Condensed Consolidated Balance Sheets	Net Amounts of Liabilities Presented on the Condensed Consolidated Balance Sheets	Gross Amounts Not Offset on the Condensed Consolidated Balance Sheets: Financial Instruments	Cash Collateral Pledged	Net Liabilities Exposed
Derivative Liabilities:						
Counterparty A	$ 91	$ —	$ 91	$ (91)	$ —	$ —
Counterparty B	337	—	337	(337)	—	—
Counterparty C	112	—	112	(112)	—	—
Total	$ 540	$ —	$ 540	$ (540)	$ —	$ —

Note 11. Convertible Senior Notes, Net

Convertible Senior Notes

In June 2013, we issued 0.75% convertible senior notes due July 15, 2018 with a principal amount of $350 million. The 2018 Notes were unsecured, unsubordinated obligations, and interest was payable in cash in arrears at a fixed rate of 0.75% on January 15 and July 15 of each year. During the second quarter of fiscal 2019, the 2018 Notes were converted by note holders and we repaid the $350 million principal balance in cash. We also distributed approximately 1.5 million shares of our Class A common stock to note holders during the second quarter of fiscal

2019, which represents the conversion value in excess of the principal amount.

In June 2013, we issued 1.50% convertible senior notes due July 15, 2020 with a principal amount of $250 million. The 2020 Notes are unsecured, unsubordinated obligations, and interest is payable in cash in arrears at a fixed rate of 1.50% on January 15 and July 15 of each year. The 2020 Notes mature on July 15, 2020 unless repurchased or converted in accordance with their terms prior to such date. We cannot redeem the 2020 Notes prior to maturity.

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In September 2017, we issued 0.25% convertible senior notes due October 1, 2022 with a principal amount of $1.15 billion. The 2022 Notes are unsecured, unsubordinated obligations, and interest is payable in cash in arrears at a fixed rate of 0.25% on April 1 and October 1 of each year. The 2022 Notes mature on October 1, 2022 unless repurchased or converted in accordance with their terms prior to such date. We cannot redeem the 2022 Notes prior to maturity.
The terms of the Notes are governed by Indentures by and between us and Wells Fargo Bank, National Association, as Trustee (the “Indentures”). Upon conversion, holders of the Notes will receive cash, shares of Class A common stock, or a combination of cash and shares of Class A common stock, at our election.
For the 2020 Notes, the initial conversion rate is 12.2340 shares of Class A common stock per $1,000 principal amount, which is equal to an initial conversion price of approximately $81.74 per share of Class A common stock, subject to adjustment. Prior to the close of business on March 13, 2020, conversion of the 2020 Notes is subject to the satisfaction of certain conditions, as described below. For the 2022 Notes, the initial conversion rate is 6.7982 shares of Class A common stock per $1,000 principal amount, which is equal to an initial conversion price of approximately $147.10 per share of Class A common stock, subject to adjustment. Prior to the close of business on May 31, 2022, conversion of the 2022 Notes is subject to the satisfaction of certain conditions, as described below.
Holders of the Notes who convert their Notes in connection with certain corporate events that constitute a make-whole fundamental change (as defined in the Indentures) are, under certain circumstances, entitled to an increase in the conversion rate. Additionally, in the event of a corporate event that constitutes a fundamental change (as defined in the Indentures), holders of the Notes may require us to repurchase all or a portion of their Notes at a price equal to 100% of the principal amount of the Notes, plus any accrued and unpaid interest.
Holders of the 2020 Notes and 2022 Notes may convert all or a portion of their Notes prior to the close of business on March 13, 2020 and May 31, 2022, respectively, in multiples of $1,000 principal amount, only under the following circumstances:

- if the last reported sale price of Class A common stock for at least 20 trading days during a period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is greater than or equal to 130% of the conversion price of the respective Notes on each applicable trading day;
- during the five business day period after any five consecutive trading day period in which the trading price per $1,000 principal amount of the respective Notes for each day of that five day consecutive trading day period was less than 98% of the product of the last reported sale price of Class A common stock and the conversion rate of the respective Notes on such trading day; or
- upon the occurrence of specified corporate events, as noted in the Indentures.

On or after March 15, 2020 for the 2020 Notes and June 1, 2022 for the 2022 Notes, holders of the respective Notes may convert their Notes at any time until the close of business on the second scheduled trading day immediately preceding the respective maturity date of their Notes.
In accounting for the issuance of the Notes, we separated each of the Notes into liability and equity components. The carrying amounts of the liability components were calculated by measuring the fair value of similar liabilities that do not have associated convertible features. The carrying amount of the equity components representing the conversion option were determined by deducting the fair value of the liability components from the par value of the respective Notes. These differences represent debt discounts that are amortized to interest expense over the respective terms of the Notes using the effective interest rate method. The equity components are not remeasured as long as they continue to meet the conditions for equity classification.
In accounting for the issuance costs related to the Notes, we allocated the total amount of issuance costs incurred to liability and equity components based on their relative values. Issuance costs attributable to the liability components are being amortized on a straight-line basis, which approximates the effective interest rate method, to interest expense over the respective terms of the Notes. The issuance costs attributable to the equity components were netted against the respective equity components in Additional paid-in capital. For the 2018 Notes, we recorded liability issuance costs of $7 million and equity issuance costs of $2 million. Amortization expense for the liability issuance costs was $0.4 million for the three months ended October 31, 2017 and $0.6 million and $1 million for the nine months ended October 31, 2018 and 2017, respectively. There was no related amortization expense for the three months ended October 31, 2018 as the 2018 Notes were converted and repaid during the second quarter of fiscal 2019. For the 2020

Notes, we recorded liability issuance costs of $5 million and equity issuance costs of $2 million. Amortization expense for the liability issuance costs was $0.2 million and $0.5 million for each of the three and nine month periods ended October 31, 2018 and 2017, respectively. For the 2022 Notes, we recorded liability issuance costs of $14 million and equity issuance costs of $4 million. Amortization expense for the liability issuance costs was $0.7 million and $0.4 million for the three months ended October 31, 2018 and 2017, respectively, and $2.1 million and $0.4 million for the nine months ended October 31, 2018 and 2017, respectively.

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The Notes, net consisted of the following (in thousands):

	October 31, 2018			January 31, 2018		
	2018 Notes	2020 Notes	2022 Notes	2018 Notes	2020 Notes	2022 Notes
Principal amounts:						
Principal	$—	$249,997	$1,150,000	$350,000	$250,000	$1,150,000
Unamortized debt discount	—	(19,163)	(177,659)	(7,850)	(26,968)	(208,188)
Unamortized debt issuance costs	—	(1,150)	(11,202)	(641)	(1,654)	(13,345)
Net carrying amount	$—	$229,684	$961,139	$341,509	$221,378	$928,467
Carrying amount of the equity component [(1)]	$74,887	$66,007	$219,702	$74,892	$66,007	$219,702

(1) Included on the condensed consolidated balance sheets within Additional paid-in capital, net of $2 million, $2 million, and $4 million for the 2018 Notes, 2020 Notes, and 2022 Notes, respectively, in equity issuance costs.

As of October 31, 2018, the 2020 Notes and 2022 Notes have remaining lives of approximately 20 months and 47 months, respectively.

For more than 20 trading days during the 30 consecutive trading days ended April 30, 2018, July 31, 2018, and October 31, 2018, the last reported sale price of our Class A common stock exceeded 130% of the conversion price of the 2020 Notes. As a result, the 2020 Notes were convertible at the option of the holders during the second and third quarter of fiscal 2019 and will continue to be convertible during the fourth quarter of fiscal 2019. Accordingly, the 2020 Notes are classified as current on the condensed consolidated balance sheet as of October 31, 2018. From May 1, 2018 through the date of this filing, the amount of the principal balance of the 2020 Notes that has been converted or for which conversion has been requested was not material.

The effective interest rates of the liability components of the 2018 Notes, 2020 Notes, and 2022 Notes are 5.75%, 6.25%, and 4.60%, respectively. These interest rates were based on the interest rates of similar liabilities at the time of issuance that did not have associated convertible features. The following table sets forth total interest expense recognized related to the Notes (in thousands):

	Three Months Ended October 31,						Nine Months Ended October 31,					
	2018			2017			2018			2017		
	2018 Notes	2020 Notes	2022 Notes	2018 Notes	2020 Notes	2022 Notes	2018 Notes	2020 Notes	2022 Notes	2018 Notes	2020 Notes	2022 Notes
Contractual interest expense	$—	$937	$718	$656	$938	$367	$1,196	$2,812	$2,156	$1,969	$2,813	$367
Interest cost related to amortization of debt issuance costs	—	167	714	352	168	365	641	504	2,143	1,056	503	365
Interest cost related to amortization of the debt discount	—	2,643	10,293	4,162	2,482	5,042	7,850	7,805	30,529	12,310	7,332	5,042

We capitalized interest costs related to the Notes of $3 million for each of the three month periods ended October 31, 2018 and 2017, and $7 million and $6 million for the nine months ended October 31, 2018 and 2017, respectively.

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Notes Hedges

In connection with the issuance of the Notes, we entered into convertible note hedge transactions with respect to our Class A common stock ("Purchased Options"). The Purchased Options relating to the 2018 Notes gave us the option to purchase, subject to anti-dilution adjustments substantially identical to those in the 2018 Notes, approximately 4.2 million shares of our Class A common stock for $83.28 per share, exercisable upon conversion of the 2018 Notes. During the second quarter of fiscal 2019, we received approximately 1.5 million shares of our Class A common stock from the exercise of the Purchased Options relating to the 2018 Notes. These shares were recorded as treasury stock. The Purchased Options relating to the 2020 Notes give us the option to purchase, subject to anti-dilution adjustments substantially identical to those in the 2020 Notes, approximately 3.1 million shares of our Class A common stock for $81.74 per share, exercisable upon conversion of the 2020 Notes. The Purchased Options relating to the 2022 Notes give us the option to purchase, subject to anti-dilution adjustments substantially identical to those in the 2022 Notes, approximately 7.8 million shares of our Class A common stock for $147.10 per share, exercisable upon conversion of the 2022 Notes. The Purchased Options will expire in 2020 for the 2020 Notes and in 2022 for the 2022 Notes, if not exercised earlier.

The Purchased Options are intended to offset potential economic dilution to our Class A common stock upon any conversion of the Notes. The Purchased Options are separate transactions and are not part of the terms of the Notes. We paid an aggregate amount of $144 million for the Purchased Options relating to the 2018 Notes and 2020 Notes, and $176 million for the Purchased Options relating to the 2022 Notes. The amount paid for the Purchased Options is included in Additional paid-in capital on the condensed consolidated balance sheets.

Warrants

In connection with the issuance of the Notes, we also entered into warrant transactions to sell warrants ("Warrants") to acquire, subject to anti-dilution adjustments, up to approximately 4.2 million shares over 60 scheduled trading days beginning in October 2018, 3.1 million shares over 60 scheduled trading days beginning in October 2020, and 7.8 million shares over 60 scheduled trading days beginning in January 2023 of our Class A common stock at an exercise price of $107.96, $107.96, and $213.96 per share, respectively. If the Warrants are not exercised on their exercise dates, they will expire. If the market value per share of our Class A common stock exceeds the applicable exercise price of the Warrants, the Warrants will have a dilutive effect on our earnings per share assuming that we are profitable. The Warrants are separate transactions and are not part of the terms of the Notes or the Purchased Options. We received aggregate proceeds of $93 million from the sale of the Warrants related to the 2018 Notes and the 2020 Notes, and $81 million from the sale of the Warrants related to the 2022 Notes. The proceeds from the sale of the Warrants are recorded in Additional paid-in capital on the condensed consolidated balance sheets.

During the three months ended October 31, 2018, Warrants related to the 2018 Notes were exercised, and we distributed approximately 0.1 million shares of our Class A common stock to warrant holders utilizing treasury stock. The number of net shares distributed was determined based on the number of Warrants exercised multiplied by the difference between the exercise price of the Warrants and their daily volume weighted-average stock price. As of October 31, 2018, there were 3.5 million Warrants outstanding related to the 2018 Notes.

Note 12. Commitments and Contingencies

Facility and Computing Infrastructure-related Commitments

We have entered into non-cancelable agreements for certain of our offices and data centers with various expiration dates. Certain of our office leases are with an affiliate of our Chairman, David Duffield, who is also a significant stockholder (see Note 18). Our operating lease agreements generally provide for rental payments on a graduated basis and for options to renew, which could increase future minimum lease payments if exercised. This includes payments for office and data center square footage as well as data center power capacity for certain data centers. We generally recognize these expenses on a straight-line basis over the period in which we benefit from the lease. Total rent expense was $25 million and $21 million for the three months ended October 31, 2018 and 2017, respectively, and $72 million and $60 million for the nine months ended October 31, 2018 and 2017, respectively.

In January 2014, we entered into a 95-year lease for a 6.9-acre parcel of vacant land in Pleasanton, California, under which we paid $2 million for base rent from commencement through December 31, 2020. Annual rent payments of $0.2 million plus increases based on increases in the consumer price index begin on January 1, 2021 and continue through the end of the lease.

Additionally, we have entered into non-cancelable agreements with computing infrastructure vendors with various expiration dates.

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Legal Matters

We are a party to various legal proceedings and claims that arise in the ordinary course of business. We make 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 at least quarterly and adjusted to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular matter. In our opinion, as of October 31, 2018, there was not at least a reasonable possibility that we had incurred a material loss, or a material loss in excess of a recorded accrual, with respect to such loss contingencies.

Note 13. Common Stock and Stockholders' Equity

Common Stock

As of October 31, 2018, there were 151 million shares of Class A common stock, net of treasury stock, and 67 million shares of Class B common stock outstanding. The rights of the holders of Class A common stock and Class B common stock are identical, except with respect to voting and conversion. Each share of Class A common stock is entitled to one vote per share and each share of Class B common stock is entitled to 10 votes per share. Each share of Class B common stock can be converted into a share of Class A common stock at any time at the option of the holder.

Employee Equity Plans

Our 2012 Equity Incentive Plan ("EIP") serves as the successor to our 2005 Stock Plan (together with the EIP, the "Stock Plans"). Pursuant to the terms of the EIP, the share reserve increased by 11 million shares in March 2018. As of October 31, 2018, we had approximately 65 million shares of Class A common stock available for future grants.

In connection with the acquisition of Adaptive Insights, we assumed unvested awards that had been granted under the Adaptive Insights, Inc. 2013 Equity Incentive Plan.

We also have a 2012 Employee Stock Purchase Plan ("ESPP"). Under the ESPP, eligible employees are granted options to purchase shares at the lower of 85% of the fair market value of the stock at the time of grant or 85% of the fair market value at the time of exercise. Options to purchase shares are granted twice yearly on or about June 1 and December 1 and exercisable on or about the succeeding November 30 and May 31, respectively, of each year. As of October 31, 2018, approximately 7 million shares of Class A common stock were available for issuance under the ESPP.

Restricted Stock Units

The Stock Plans provide for the issuance of restricted stock units ("RSUs") to employees and non-employees. RSUs generally vest over four years. A summary of information related to RSU activity during the nine months ended October 31, 2018 is as follows:

	Number of Shares	Weighted-Average Grant Date Fair Value
Balance as of January 31, 2018	12,819,516	$ 84.77
RSUs granted	6,408,869	127.78
RSUs vested	(4,722,787)	84.06
RSUs forfeited	(699,400)	94.52
Balance as of October 31, 2018	13,806,198	$ 104.48

As of October 31, 2018, there was a total of $1.3 billion in unrecognized compensation cost related to unvested RSUs, which is expected to be recognized over a weighted-average period of approximately 2.8 years.

Performance-based Restricted Stock Units

During fiscal 2018, 0.4 million shares of performance-based restricted stock units ("PRSUs") were granted to all employees other than executive management that included both service conditions and performance conditions related to company-wide goals. These performance conditions were met and the PRSUs vested on March 15, 2018. During the nine months ended October 31, 2018, we recognized $7 million in compensation cost related to these PRSUs.

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Additionally, during fiscal 2019, 0.5 million shares of PRSUs were granted to all employees other than executive management that included both service conditions and performance conditions related to company-wide goals. We expect to grant additional shares related to this program for employees hired in fiscal 2019. These PRSU awards will vest if the performance conditions are achieved for the fiscal year ended January 31, 2019 and if the individual employee continues to provide service through the vesting date of March 15, 2019. During the three and nine months ended October 31, 2018, we recognized $20 million and $29 million, respectively, in compensation cost related to these PRSUs, and there is a total of $31 million in unrecognized compensation cost which is expected to be recognized over a weighted-average period of approximately five months.

Stock Options

The Stock Plans provide for the issuance of incentive and nonstatutory options to employees and non-employees. Options issued under the Stock Plans generally are exercisable for periods not to exceed 10 years and generally vest over five years. A summary of information related to stock option activity during the nine months ended October 31, 2018 is as follows (in millions, except share and per share data):

	Outstanding Stock Options	Weighted-Average Exercise Price	Aggregate Intrinsic Value
Balance as of January 31, 2018	6,595,486	$ 4.23	$ 763
Stock options assumed	1,103,942	26.84	
Stock options exercised	(1,153,579)	9.10	
Stock options canceled	(33,320)	15.06	
Balance as of October 31, 2018	6,512,529	$ 7.14	$ 820
Vested and expected to vest as of October 31, 2018	6,446,090	$ 7.41	$ 810
Exercisable as of October 31, 2018	5,643,205	$ 4.58	$ 725

As of October 31, 2018, there was a total of $84 million in unrecognized compensation cost related to unvested assumed stock options, which is expected to be recognized over a weighted-average period of approximately 2.5 years.

Note 14. Unearned Revenue and Performance Obligations

$547 million and $421 million of subscription services revenue was recognized during the three months ended October 31, 2018 and 2017, respectively, that was included in the unearned revenue balances as of July 31, 2018 and 2017, respectively. $1.2 billion and $904 million of subscription services revenue was recognized during the nine months ended October 31, 2018 and 2017, respectively, that was included in the unearned revenue balances as of January 31, 2018 and 2017, respectively. Professional services revenue recognized in the same periods from unearned revenue balances at the beginning of the respective periods was not material.

Transaction Price Allocated to the Remaining Performance Obligations

As of October 31, 2018, approximately $5.9 billion of revenue is expected to be recognized from remaining performance obligations for subscription contracts. We expect to recognize revenue on approximately $4.02 billion of these remaining performance obligations over the next 24 months, with the balance recognized thereafter. Revenue from remaining performance obligations for professional services contracts as of October 31, 2018 was not material.

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Note 15. Other Income (Expense), Net

Other income (expense), net consisted of the following (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Interest income	$6,995	$6,394	$33,923	$15,474
Interest expense [1]	(12,348)	(12,285)	(48,165)	(26,111)
Other [2]	31,970	2,149	38,624	6,170
Other income (expense), net	$26,617	$(3,742)	$24,382	$(4,467)

(1) Interest expense includes the contractual interest expense related to the 2018 Notes, 2020 Notes, and 2022 Notes and non-cash interest expense related to amortization of the debt discount and debt issuance costs, net of capitalized interest costs (see Note 11).

(2) Other includes the net gains (losses) from our equity investments (see Note 3).

Note 16. Income Taxes

We compute the year-to-date income tax provision by applying the estimated annual effective tax rate to the year-to-date pre-tax income or loss and adjusting for discrete tax items in the period. We reported an income tax benefit of $5 million and an income tax provision of $6 million for the nine months ended October 31, 2018 and 2017, respectively. The income tax benefit for the nine months ended October 31, 2018 was primarily attributable to the application of intra-period tax allocation rules related to gains from comprehensive income and excess tax benefits in certain foreign jurisdictions from share-based compensation. The income tax benefit was partially offset by state taxes and income tax expenses in profitable foreign jurisdictions. The income tax provision for the nine months ended October 31, 2017 was primarily attributable to state taxes and income tax expenses in profitable foreign jurisdictions.

We are subject to income tax audits in the U.S. and foreign jurisdictions. We record liabilities related to uncertain tax positions and believe that we have provided adequate reserves for income tax uncertainties in all open tax years. Due to our history of tax losses, all years remain open to tax audit.

We periodically evaluate the realizability of our net deferred tax assets based on all available evidence, both positive and negative. The realization of net deferred tax assets is dependent on our ability to generate sufficient future taxable income during periods prior to the expiration of tax attributes to fully utilize these assets. As of October 31, 2018, we continue to maintain a full valuation allowance on our deferred tax assets except in certain jurisdictions.

In December 2017, the SEC staff issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act, which allows companies to record provisional amounts for the Tax Act during a measurement period not to extend beyond one year of the enactment date. As of October 31, 2018, we did not have any significant adjustments to our initial assessment performed as of January 31, 2018. We will continue our analysis for all the tax effects of the Tax Act, which are still subject to change during the measurement period, and anticipate further guidance on accounting interpretations from the FASB and application of the Tax Act from the Department of the Treasury.

Note 17. Net Loss Per Share

Basic net loss per share attributable to common stockholders is computed by dividing the net loss attributable to common stockholders by the weighted-average number of shares of common stock outstanding during the period, net of treasury stock. Diluted net loss per share is computed by giving effect to all potential shares of common stock, including our outstanding stock options, outstanding warrants, common stock related to unvested early exercised stock options, common stock related to unvested restricted stock units and awards and convertible senior notes to the extent dilutive, and common stock issuable pursuant to the ESPP. Basic and diluted net loss per share was the same for each period presented, as the inclusion of all potential common shares outstanding would have been anti-dilutive.

The net loss per share attributable to common stockholders is allocated based on the contractual participation rights of the Class A common shares and Class B common shares as if the loss for the period had been distributed. As the liquidation and dividend rights are identical, the net loss attributable to common stockholders is allocated on a proportionate basis.

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The following table presents the calculation of basic and diluted net loss attributable to common stockholders per share (in thousands, except per share data):

	Three Months Ended October 31,				Nine Months Ended October 31,			
	2018		2017		2018		2017	
	Class A	Class B	Class A	Class B	Class A	Class B	Class A	Class B
Net loss per share, basic and diluted:								
Numerator:								
Allocation of distributed net loss	$(105,549)	$(47,782)	$(55,592)	$(29,954)	$(213,961)	$(99,936)	$(149,179)	$(82,943)
Denominator:								
Weighted-average common shares outstanding	149,855	67,839	135,941	73,247	146,951	68,637	132,851	73,864
Basic and diluted net loss per share	$(0.70)	$(0.70)	$(0.41)	$(0.41)	$(1.46)	$(1.46)	$(1.12)	$(1.12)

The anti-dilutive securities excluded from the weighted-average shares used to calculate the diluted net loss per common share were as follows (in thousands):

	As of October 31,	
	2018	2017
Outstanding common stock options	6,513	7,070
Shares subject to repurchase	—	15
Unvested restricted stock awards, units, and PRSUs	14,302	13,680
Shares related to the convertible senior notes	10,876	15,079
Shares subject to warrants related to the issuance of convertible senior notes	14,379	15,079
Shares issuable pursuant to the ESPP	418	375
	46,488	51,298

Note 18. Related Party Transactions

We lease certain office space from an affiliate of our Chairman, Mr. Duffield, adjacent to our corporate headquarters in Pleasanton, California, under various lease agreements. The average term of the agreements is 8 years. The total rent expense under these agreements was $3 million and $2 million for the three months ended October 31, 2018 and 2017, respectively, and $8 million and $6 million for the nine months ended October 31, 2018 and 2017, respectively.

Note 19. Geographic Information

Disaggregation of Revenue

We sell our subscription contracts and related services in two primary geographical markets: to customers located in the United States and to customers located outside of the United States. Revenue by geography is generally based on the address of the customer as specified in our master subscription agreement. The following table sets forth revenue by geographic area (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
United States	$573,473	$439,794	$1,568,812	$1,242,431
Other countries	169,716	115,595	464,740	318,139
Total	$743,189	$555,389	$2,033,552	$1,560,570

No single country other than the United States had revenues greater than 10% of total revenues for the three and nine months ended October 31, 2018 and 2017. No customer individually accounted for more than 10% of our trade and other receivables, net as of October 31, 2018 or January 31, 2018.

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Long-Lived Assets

We attribute our long-lived assets, which primarily consist of property and equipment, to a country based on the physical location of the assets. The following table sets forth Property and equipment, net by geographic area (in thousands):

	October 31, 2018	January 31, 2018
United States	$ 661,942	$ 479,996
Ireland	57,771	52,904
Other countries	15,730	13,709
Total	$ 735,443	$ 546,609

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements, which are subject to safe harbor protection under the Private Securities Litigation Reform Act of 1995. All statements contained in this report other than statements of historical fact, including statements regarding our future results of operations and financial position, our business strategy and plans, and our objectives for future operations, are forward-looking statements. The words “believe,” “may,” “will,” “estimate,” “continue,” “anticipate,” “intend,” “expect,” “seek,” “plan,” and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described in the “Risk Factors” section, which we encourage you to read carefully. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this report may not occur and actual results could differ materially and adversely from those anticipated or implied by the forward-looking statements.

You should not rely upon forward-looking statements as predictions of future events. The events and circumstances reflected in the forward-looking statements may not be achieved or occur. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activities, performance, or achievements. We are under no duty to update any of these forward-looking statements after the date of this report or to conform these statements to actual results or revised expectations.

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

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and notes thereto included elsewhere in this report.

Overview

Workday provides financial management, human capital management, and analytics applications designed for the world’s largest companies, educational institutions, and government agencies. We offer innovative and adaptable technology focused on the consumer Internet experience and cloud delivery model. Our applications are designed for global enterprises to manage complex and dynamic operating environments. We provide our customers with highly adaptable, accessible, and reliable applications to manage critical business functions that enable them to optimize their financial and human capital resources.

We were founded in 2005 to deliver cloud applications to global enterprises. Our applications are designed around the way people work today—in an environment that is global, collaborative, fast-paced, and mobile. Our cycle of frequent updates has facilitated rapid innovation and the introduction of new applications throughout our history. We began offering our HCM application in 2006 and our Financial Management application in 2007. Since then we have continued to invest in innovation and have consistently introduced new services to our customers.

We offer Workday applications to our customers on an enterprise-wide subscription basis, typically with contract terms of three years or longer and with subscription fees largely based on the size of the customer’s workforce. We generally recognize revenues from subscription fees ratably over the term of the contract. We currently derive a substantial majority of our subscription services revenues from subscriptions to our HCM application. We market our applications primarily through our direct sales force.

Our diverse customer base includes medium-sized and large, global companies. We have achieved significant growth in a relatively short period of time with a substantial amount of our growth coming from new customers. Our current financial focus is on growing our revenues and expanding our customer base. While we are incurring losses today, we strive to invest in a disciplined manner across all of our functional areas to sustain continued near-term revenue growth and support our long-term initiatives. Our operating expenses have increased significantly in absolute dollars in recent periods, primarily due to the significant growth of our employee population. We had approximately 10,200 and approximately 7,900 employees as of October 31, 2018 and 2017, respectively.

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We intend to continue investing for long-term growth. We have invested, and expect to continue to invest, heavily in our product development efforts to deliver additional compelling applications and to address customers' evolving needs. In addition, we plan to continue to expand our ability to sell our applications globally, particularly in Europe and Asia, by investing in product development and customer support to address the business needs of local markets, increasing our sales and marketing organizations, acquiring, building, and/or leasing additional office space, and expanding our ecosystem of service partners to support local deployments. We expect to make further significant investments in our data center infrastructure as we plan for future growth. We are also investing in personnel to service our growing customer base. These investments will increase our costs on an absolute basis in the near-term. Many of these investments will occur in advance of experiencing any direct benefit from them and will make it difficult to determine if we are allocating our resources efficiently. We expect our product development, sales and marketing, and general and administrative expenses as a percentage of total revenues to decrease over time as we grow our revenues, and we anticipate that we will gain economies of scale by increasing our customer base without direct incremental development costs and by utilizing more of the capacity of our data centers.

Since inception, we have invested heavily in our professional services organization to help ensure that customers successfully deploy and adopt our applications. Additionally, we continue to expand our professional service partner ecosystem to further support our customers. We believe our investment in professional services, as well as partners building consulting practices around Workday, will drive additional customer subscriptions and continued growth in revenues. Due to our ability to leverage the expanding partner ecosystem, we expect that the rate of professional services revenue growth will decline over time and continue to be lower than subscription revenue growth.

Components of Results of Operations

Revenues

We primarily derive our revenues from subscription services and professional services. Subscription services revenues primarily consist of fees that give our customers access to our cloud applications, which include related customer support. Professional services fees include deployment services, optimization services, and training.

Subscription services revenues accounted for 84% of our total revenues during the three and nine months ended October 31, 2018 and represented 96% of our total unearned revenue as of October 31, 2018. Subscription services revenues are driven primarily by the number of customers, the number of workers at each customer, the specific applications subscribed to by each customer, and the price of our applications.

The mix of the applications to which a customer subscribes can affect our financial performance due to price differentials in our applications. Pricing for our applications varies based on many factors, including the complexity and maturity of the application and its acceptance in the marketplace. New products or services offerings by competitors in the future could also impact the mix and pricing of our offerings.

Subscription services revenues are recognized over time as they are delivered and consumed concurrently over the contractual term, beginning on the date our service is made available to the customer. Our subscription contracts typically have a term of three years or longer and are generally non-cancelable. We generally invoice our customers annually in advance. Amounts that have been invoiced are initially recorded as unearned revenue.

The majority of our consulting engagements are billed on a time and materials basis, and revenues are typically recognized over time as the services are performed. In some cases, we supplement our consulting teams by subcontracting resources from our service partners and deploying them on customer engagements. As our professional services organization and the Workday-related consulting practices of our partner firms continue to develop, we expect the partners to increasingly contract directly with our subscription customers. As a result of this trend, and the increase of our subscription services revenues, we expect professional services revenues as a percentage of total revenues to decline over time.

Costs and Expenses

Costs of subscription services revenues. Costs of subscription services revenues consist primarily of employee-related expenses related to hosting our applications and providing customer support, the costs of data center capacity, and depreciation of computer equipment and software.

Costs of professional services revenues. Costs of professional services revenues consist primarily of employee-related expenses associated with these services, the cost of subcontractors, and travel.

Product development. Product development expenses consist primarily of employee-related costs. We continue to focus our product development efforts on adding new features and applications, increasing the functionality, and enhancing the ease of use of our cloud applications.

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Sales and marketing. Sales and marketing expenses consist primarily of employee-related costs, sales commissions, marketing programs, and travel. Marketing programs consist of advertising, events, corporate communications, brand building, and product marketing activities. Sales commissions are considered incremental costs of obtaining a contract with a customer and are deferred and amortized. Sales commissions for initial contracts are deferred and then amortized on a straight-line basis over a period of benefit that we have determined to be five years. Sales commissions for renewal contracts are deferred and then amortized on a straight-line basis over the related contractual renewal period.

General and administrative. General and administrative expenses consist of employee-related costs for finance and accounting, legal, human resources, information systems personnel, professional fees, and other corporate expenses.

Results of Operations

Revenues

Our total revenues for the three and nine months ended October 31, 2018 and 2017 were as follows (in thousands, except percentages):

	Three Months Ended October 31,			Nine Months Ended October 31,		
	2018	2017	% Change	2018	2017	% Change
Revenues:						
Subscription services	$624,416	$463,568	35%	$1,712,224	$1,297,831	32%
Professional services	118,773	91,821	29%	321,328	262,739	22%
Total revenues	$743,189	$555,389	34%	$2,033,552	$1,560,570	30%

Total revenues were $743 million for the three months ended October 31, 2018, compared to $555 million during the prior year period, an increase of $188 million, or 34%. Subscription services revenues were $624 million for the three months ended October 31, 2018, compared to $464 million for the prior year period, an increase of $160 million, or 35%. The increase in subscription services revenues was due primarily to an increased number of customer contracts as compared to the prior year period. Professional services revenues were $119 million for the three months ended October 31, 2018, compared to $92 million for the prior year period, an increase of $27 million, or 29%. The increase in professional services revenues was due primarily to Workday performing deployment and integration services for a greater number of customers than in the prior year period.

Total revenues were $2.0 billion for the nine months ended October 31, 2018, compared to $1.6 billion during the prior year period, an increase of $0.4 billion, or 30%. Subscription services revenues were $1.7 billion for the nine months ended October 31, 2018, compared to $1.3 billion for the prior year period, an increase of $0.4 billion, or 32%. The increase in subscription services revenues was due primarily to an increased number of customer contracts as compared to the prior year period. Professional services revenues were $321 million for the nine months ended October 31, 2018, compared to $263 million for the prior year period, an increase of $58 million, or 22%. The increase in professional services revenues was due primarily to Workday performing deployment and integration services for a greater number of customers than in the prior year period.

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Operating Expenses

GAAP operating expenses were $926 million for the three months ended October 31, 2018, compared to $635 million for the prior year period, an increase of $291 million, or 46%. The increase was primarily due to an increase of $207 million in employee-related costs driven by higher headcount, $32 million in outside services expenses, $23 million in depreciation and amortization expenses, $7 million in facility and IT-related expenses, $7 million in third-party costs for hardware maintenance and data center capacity, and $4 million in marketing expenses. These increases are partially attributable to the acquisition of Adaptive Insights, including one-time transaction and integration-related costs.

GAAP operating expenses were $2.4 billion for the nine months ended October 31, 2018, compared to $1.8 billion for the prior year period, an increase of $0.6 billion, or 33%. The increase was primarily due to an increase of $0.4 billion in employee-related costs driven by higher headcount and $0.1 billion in expenses related to outside services, depreciation, amortization, and third-party costs for hardware maintenance and data center capacity. These increases are partially attributable to the acquisition of Adaptive Insights, including one-time transaction and integration-related costs.

We use the non-GAAP financial measure of non-GAAP operating expenses to understand and compare operating results across accounting periods, for internal budgeting and forecasting purposes, for short- and long-term operating plans, and to evaluate our financial performance and the ability of operations to generate cash. We believe that non-GAAP operating expenses reflect our ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in our business, as they exclude expenses that are not reflective of ongoing operating results. We also believe that non-GAAP operating expenses provide useful information to investors and others in understanding and evaluating our operating results and prospects in the same manner as management and in comparing financial results across accounting periods and to those of peer companies.

Non-GAAP operating expenses are calculated by excluding share-based compensation expenses, and certain other expenses, which consist of employer payroll tax-related items on employee stock transactions and amortization of acquisition-related intangible assets.

Non-GAAP operating expenses were $694 million for the three months ended October 31, 2018, compared to $505 million for the prior year period, an increase of $189 million, or 37%. The increase was primarily due to an increase of $119 million in employee-related costs driven by higher headcount, $32 million in outside services expenses, $9 million in depreciation and amortization expenses, $7 million in facility and IT-related expenses, and $7 million in third-party costs for hardware maintenance and data center capacity. These increases are partially attributable to the acquisition of Adaptive Insights, including one-time transaction and integration-related costs.

Non-GAAP operating expenses were $1.8 billion for the nine months ended October 31, 2018, compared to $1.4 billion for the prior year period, an increase of $0.4 billion, or 31%. The increase was primarily due to an increase of $0.3 billion in employee-related costs driven by higher headcount and $0.1 billion in expenses related to outside services, depreciation, amortization, and third-party costs for hardware maintenance and data center capacity. These increases are partially attributable to the acquisition of Adaptive Insights, including one-time transaction and integration-related costs.

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Reconciliations of our GAAP to non-GAAP operating expenses were as follows (in thousands):

	Three Months Ended October 31, 2018			
	GAAP Operating Expenses	Share-Based Compensation Expenses (1)	Other Operating Expenses (2)	Non-GAAP Operating Expenses (3)
Costs of subscription services	$103,310	$ (10,205)	$(11,432)	$ 81,673
Costs of professional services	119,691	(15,702)	(495)	103,494
Product development	318,003	(86,304)	(3,082)	228,617
Sales and marketing	246,156	(38,720)	(7,717)	199,719
General and administrative	138,784	(57,993)	(758)	80,033
Total costs and expenses	$925,944	$ (208,924)	$(23,484)	$ 693,536

	Three Months Ended October 31, 2017			
	GAAP Operating Expenses	Share-Based Compensation Expenses (1)	Other Operating Expenses (2)	Non-GAAP Operating Expenses (3)
Costs of subscription services	$71,898	$ (6,899)	$(2,468)	$ 62,531
Costs of professional services	91,657	(9,956)	(200)	81,501
Product development	239,588	(59,116)	(3,780)	176,692
Sales and marketing	176,121	(25,517)	(598)	150,006
General and administrative	56,184	(20,991)	(683)	34,510
Total costs and expenses	$635,448	$ (122,479)	$(7,729)	$ 505,240

	Nine Months Ended October 31, 2018			
	GAAP Operating Expenses	Share-Based Compensation Expenses (1)	Other Operating Expenses (2)	Non-GAAP Operating Expenses (3)
Costs of subscription services	$271,078	$ (26,603)	$(19,671)	$224,804
Costs of professional services	330,124	(39,012)	(2,715)	288,397
Product development	874,427	(230,169)	(15,839)	628,419
Sales and marketing	641,391	(93,699)	(11,336)	536,356
General and administrative	259,533	(99,163)	(3,356)	157,014
Total costs and expenses	$2,376,553	$ (488,646)	$(52,917)	$1,834,990

	Nine Months Ended October 31, 2017			
	GAAP Operating Expenses	Share-Based Compensation Expenses (1)	Other Operating Expenses (2)	Non-GAAP Operating Expenses (3)
Costs of subscription services	$197,627	$ (19,170)	$(3,222)	$175,235
Costs of professional services	260,834	(27,278)	(1,485)	232,071
Product development	657,130	(167,068)	(19,344)	470,718
Sales and marketing	503,782	(74,618)	(3,398)	425,766
General and administrative	163,085	(63,656)	(2,755)	96,674
Total costs and expenses	$1,782,458	$ (351,790)	$(30,204)	$1,400,464

(1) Share-based compensation expenses were $209 million and $122 million for the three months ended October 31, 2018 and 2017, respectively, and $489 million and $352 million for the nine months ended October 31, 2018 and 2017, respectively. The increase in share-based compensation expenses was primarily due to assumed Adaptive Insights, Inc. (“Adaptive Insights”) awards and grants of restricted stock units (“RSUs”) to existing and new

employees.

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(2) Other operating expenses include employer payroll tax-related items on employee stock transactions of $4 million and $3 million for the three months ended October 31, 2018 and 2017, respectively, and $23 million and $16 million for the nine months ended October 31, 2018 and 2017, respectively. In addition, other operating expenses included amortization of acquisition-related intangible assets of $19 million and $4 million for the three months ended October 31, 2018 and 2017, respectively, and $30 million and $14 million for the nine months ended October 31, 2018 and 2017, respectively.

(3) See "Non-GAAP Financial Measures" below for further information.

Costs of Subscription Services

See the table above for a reconciliation of GAAP to non-GAAP operating expenses.

GAAP operating expenses in costs of subscription services were $103 million for the three months ended October 31, 2018, compared to $72 million for the prior year period, an increase of $31 million, or 43%. The increase was primarily due to increases of $14 million in depreciation expense related to equipment in our data centers, $10 million in employee-related costs driven by higher headcount, and $7 million in third-party costs for hardware maintenance and data center capacity.

GAAP operating expenses in costs of subscription services were $271 million for the nine months ended October 31, 2018, compared to $198 million for the prior year period, an increase of $73 million, or 37%. The increase was primarily due to increases of $28 million in depreciation expense related to equipment in our data centers, $25 million in employee-related costs driven by higher headcount, and $16 million in third-party costs for hardware maintenance and data center capacity.

Non-GAAP operating expenses in costs of subscription services were $82 million for the three months ended October 31, 2018, compared to $63 million for the prior year period, an increase of $19 million, or 30%. The increase was primarily due to increases of $7 million in third-party costs for hardware maintenance and data center capacity, $6 million in employee-related costs driven by higher headcount, and $5 million in depreciation expense related to equipment in our data centers.

Non-GAAP operating expenses in costs of subscription services were $225 million for the nine months ended October 31, 2018, compared to $175 million for the prior year period, an increase of $50 million, or 29%. The increase was primarily due to increases of $17 million in employee-related costs driven by higher headcount, $16 million in third-party costs for hardware maintenance and data center capacity, and $12 million in depreciation expense related to equipment in our data centers.

We expect that GAAP and non-GAAP operating expenses in costs of subscription services will continue to increase in absolute dollars as we improve and expand our data center capacity and operations.

Costs of Professional Services

See the table above for a reconciliation of GAAP to non-GAAP operating expenses.

GAAP operating expenses in costs of professional services were $120 million for the three months ended October 31, 2018, compared to $92 million for the prior year period, an increase of $28 million, or 30%. The increase was primarily due to additional costs of $24 million to staff our deployment and integration engagements and $2 million in facility and IT-related expenses.

GAAP operating expenses in costs of professional services were $330 million for the nine months ended October 31, 2018, compared to $261 million for the prior year period, an increase of $69 million, or 26%. The increase was primarily due to additional costs of $59 million to staff our deployment and integration engagements and $5 million in facility and IT-related expenses.

Non-GAAP operating expenses in costs of professional services were $103 million for the three months ended October 31, 2018, compared to $82 million for the prior year period, an increase of $21 million, or 26%. The increase was primarily due to additional costs of $18 million to staff our deployment and integration engagements and $2 million in facility and IT-related expenses.

Non-GAAP operating expenses in costs of professional services were $288 million for the nine months ended October 31, 2018, compared to $232 million for the prior year period, an increase of $56 million, or 24%. The increase was primarily due to additional costs of $46 million to staff our deployment and integration engagements and $5 million in facility and IT-related expenses.

Going forward, we expect GAAP and non-GAAP costs of professional services as a percentage of total revenues to continue to decline as we continue to rely on our service partners to deploy our applications and as the number of our customers continues to grow. For fiscal 2019, we anticipate GAAP and non-GAAP professional services margins to be lower than fiscal 2018 as we invest in programs to ensure ongoing customer success.

Product Development

See the table above for a reconciliation of GAAP to non-GAAP operating expenses.

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GAAP operating expenses in product development were $318 million for the three months ended October 31, 2018, compared to $240 million for the prior year period, an increase of $78 million, or 33%. The increase was primarily due to increases of $71 million in employee-related costs driven by higher headcount and $6 million in facility and IT-related expenses.

GAAP operating expenses in product development were $874 million for the nine months ended October 31, 2018, compared to $657 million for the prior year period, an increase of $217 million, or 33%. The increase was primarily due to increases of $192 million in employee-related costs driven by higher headcount and $23 million in facility and IT-related expenses.

Non-GAAP operating expenses in product development were $229 million for the three months ended October 31, 2018, compared to $177 million for the prior year period, an increase of $52 million, or 29%. The increase was primarily due to increases of $44 million in employee-related costs driven by higher headcount and $6 million in facility and IT-related expenses.

Non-GAAP operating expenses in product development were $628 million for the nine months ended October 31, 2018, compared to $471 million for the prior year period, an increase of $157 million, or 33%. The increase was primarily due to increases of $124 million in employee-related costs driven by higher headcount and $23 million in facility and IT-related expenses.

We expect that GAAP and non-GAAP product development expenses will continue to increase in absolute dollars as we invest to improve and expand our applications and develop new technologies.

Sales and Marketing

See the table above for a reconciliation of GAAP to non-GAAP operating expenses.

GAAP operating expenses in sales and marketing were $246 million for the three months ended October 31, 2018, compared to $176 million for the prior year period, an increase of $70 million, or 40%. The increase was primarily due to increases of $52 million in employee-related costs driven by higher headcount and higher commissionable sales volume, $3 million in advertising, marketing, and event costs, and $3 million in facility and IT-related expenses.

GAAP operating expenses in sales and marketing were $641 million for the nine months ended October 31, 2018, compared to $504 million for the prior year period, an increase of $137 million, or 27%. The increase was primarily due to increases of $101 million in employee-related costs driven by higher headcount and higher commissionable sales volume, $13 million in advertising, marketing, and event costs, and $8 million in facility and IT-related expenses.

Non-GAAP operating expenses in sales and marketing were $200 million for the three months ended October 31, 2018, compared to $150 million for the prior year period, an increase of $50 million, or 33%. The increase was primarily due to increases of $38 million in employee-related costs driven by higher headcount and higher commissionable sales volume, $3 million in advertising, marketing, and event costs, and $3 million in facility and IT-related expenses.

Non-GAAP operating expenses in sales and marketing were $536 million for the nine months ended October 31, 2018, compared to $426 million for the prior year period, an increase of $110 million, or 26%. The increase was primarily due to increases of $81 million in employee-related costs driven by higher headcount and higher commissionable sales volume, $13 million in advertising, marketing, and event costs, and $8 million in facility and IT-related expenses.

We expect that GAAP and non-GAAP sales and marketing expenses will continue to increase in absolute dollars as we continue to invest in the expansion of our domestic and international selling and marketing activities to build brand awareness and attract new customers.

General and Administrative

See the table above for a reconciliation of GAAP to non-GAAP operating expenses.

GAAP operating expenses in general and administrative were $139 million for the three months ended October 31, 2018, compared to $56 million for the prior year period, an increase of $83 million, or 148%. The increase was primarily due to additional employee-related costs driven by higher headcount and one-time transaction and integration-related costs due to the acquisition of Adaptive Insights.

GAAP operating expenses in general and administrative were $260 million for the nine months ended October 31, 2018, compared to $163 million for the prior year period, an increase of $97 million, or 60%. The increase was primarily due to additional employee-related costs driven by higher headcount and one-time transaction and integration-related costs due to the acquisition of Adaptive Insights.

Non-GAAP operating expenses in general and administrative were $80 million for the three months ended October 31, 2018, compared to $35 million for the prior year period, an increase of $45 million, or 129%. The increase was primarily due to increases in outside services expenses, additional employee-related costs driven by higher headcount, and one-time transaction and integration-related costs due to the acquisition of Adaptive Insights.

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Non-GAAP operating expenses in general and administrative were $157 million for the nine months ended October 31, 2018, compared to $97 million for the prior year period, an increase of $60 million, or 62%. The increase was primarily due to increases in outside services expenses, additional employee-related costs driven by higher headcount, and one-time transaction and integration-related costs due to the acquisition of Adaptive Insights.

We expect GAAP and non-GAAP general and administrative expenses will continue to increase in absolute dollars as we further invest in our infrastructure and support our global expansion.

Operating Margins

GAAP operating margins declined from (14.4)% for the three months ended October 31, 2017 to (24.6)% for the three months ended October 31, 2018. The reduction in our GAAP operating margins in the three months ended October 31, 2018 were primarily due to higher share-based compensation and other operating expenses related to the Adaptive Insights acquisition, including one-time transaction and integration-related costs, offset by higher revenues.

GAAP operating margins declined from (14.2)% for the nine months ended October 31, 2017 to (16.9)% for the nine months ended October 31, 2018. The reduction in our GAAP operating margins in the nine months ended October 31, 2018 were primarily due to higher share-based compensation and other operating expenses related to the Adaptive Insights acquisition, including one-time transaction and integration-related costs, offset by higher revenues.

We use the non-GAAP financial measure of non-GAAP operating margins to understand and compare operating results across accounting periods, for internal budgeting and forecasting purposes, for short- and long-term operating plans, and to evaluate our financial performance and the ability of operations to generate cash. We believe that non-GAAP operating margins reflect our ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in our business, as they exclude expenses that are not reflective of ongoing operating results. We also believe that non-GAAP operating margins provide useful information to investors and others in understanding and evaluating our operating results and prospects in the same manner as management and in comparing financial results across accounting periods and to those of peer companies.

Non-GAAP operating margins are calculated using GAAP revenues and non-GAAP operating expenses. See “Non-GAAP Financial Measures” below for further information.

Non-GAAP operating margins declined from 9.0% for the three months ended October 31, 2017 to 6.7% for the three months ended October 31, 2018. The reduction in our non-GAAP operating margins in the three months ended October 31, 2018 were primarily due to higher operating expenses related to the Adaptive Insights acquisition, including one-time transaction and integration-related costs, offset by higher revenues.

Non-GAAP operating margins declined from 10.3% for the nine months ended October 31, 2017 to 9.8% for the nine months ended October 31, 2018. The reduction in our non-GAAP operating margins in the nine months ended October 31, 2018 were primarily due to higher operating expenses related to the Adaptive Insights acquisition, including one-time transaction and integration-related costs, offset by higher revenues.

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Reconciliations of our GAAP to non-GAAP operating margins were as follows:

	Three Months Ended October 31, 2018			
	GAAP Operating Expenses	Share-Based Compensation Expenses	Other Operating Expenses	Non-GAAP Operating Expenses [1]
Operating margin	(24.6)%	28.1 %	3.2 %	6.7 %

	Three Months Ended October 31, 2017			
	GAAP Operating Expenses	Share-Based Compensation Expenses	Other Operating Expenses	Non-GAAP Operating Expenses [1]
Operating margin	(14.4)%	22.1 %	1.3 %	9.0 %

	Nine Months Ended October 31, 2018			
	GAAP Operating Expenses	Share-Based Compensation Expenses	Other Operating Expenses	Non-GAAP Operating Expenses [1]
Operating margin	(16.9)%	24.0 %	2.7 %	9.8 %

	Nine Months Ended October 31, 2017			
	GAAP Operating Expenses	Share-Based Compensation Expenses	Other Operating Expenses	Non-GAAP Operating Expenses [1]
Operating margin	(14.2)%	22.5 %	2.0 %	10.3 %

[1] See “Non-GAAP Financial Measures” below for further information.

Other Income (Expense), Net

Other income, net increased $30 million for the three months ended October 31, 2018 as compared to the prior year period. The increase was primarily due to an increase in the net gain from our equity investments of $29 million.

Other income, net increased $29 million for the nine months ended October 31, 2018 as compared to the prior year period. The increase was due to an increase in other income of $32 million primarily related to the net gain from our equity investments and an increase in interest income of $18 million. This was offset by an increase in interest expense of $22 million primarily related to the 0.25% convertible senior notes issued in September 2017.

Liquidity and Capital Resources

As of October 31, 2018, our principal sources of liquidity were cash, cash equivalents, and marketable securities totaling $1.6 billion, which were held for working capital purposes. Our cash equivalents and marketable securities are composed primarily of U.S. agency obligations, U.S. treasury securities, corporate bonds, commercial paper, and money market funds.

We have financed our operations primarily through customer payments, sales of equity securities, and issuance of debt. Our future capital requirements will depend on many factors, including our customer growth rate, subscription renewal activity, the timing of construction of facilities in Pleasanton, California, and the acquisition of additional facilities, the timing and extent of development efforts, the expansion of sales and marketing activities, the introduction of new and enhanced services offerings, the continuing market acceptance of our services, and acquisition activities. We may enter into arrangements to acquire or invest in complementary businesses, services, technologies, or intellectual property rights in the future. We also may choose to seek additional equity or debt financing.

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Our cash flows for the three and nine months ended October 31, 2018 and 2017 were as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Net cash provided by (used in):				
Operating activities	$114,296	$144,031	$356,145	$339,179
Investing activities	(1,268,079)	(595,458)	(640,358)	(617,002)
Financing activities	2,704	1,039,314	(306,120)	1,073,765
Effect of exchange rate changes	(213)	(322)	(795)	261
Net increase (decrease) in cash, cash equivalents and restricted cash	$(1,151,292)	$587,565	$(591,128)	$796,203

Operating Activities

Cash provided by operating activities was $114 million and $144 million for the three months ended October 31, 2018 and 2017, respectively. The decrease in cash flow provided by operating activities was primarily due to higher operating expenses driven by increased headcount and the Adaptive Insights acquisition, including one-time transaction and integration-related costs, partially offset by increases in sales and the related cash collections.

Cash provided by operating activities was $356 million and $339 million for the nine months ended October 31, 2018 and 2017, respectively. The improvement in cash flow provided by operating activities was primarily due to increases in sales and the related cash collections, partially offset by higher operating expenses driven by increased headcount and the Adaptive Insights acquisition, including one-time transaction and integration-related costs.

Investing Activities

Cash used in investing activities for the three months ended October 31, 2018 was $1.3 billion, which was primarily the result of a net cash outflow of $1.4 billion related to the Adaptive Insights acquisition, capital expenditures for data center and office space projects of $55 million, capital expenditures related to the construction of our development center of $35 million, and purchases of non-marketable equity and other investments of $29 million. These payments were partially offset by the timing of purchases and maturities of marketable securities and proceeds of $18 million from the sales and maturities of non-marketable equity and other investments.

Cash used in investing activities for the three months ended October 31, 2017 was $595 million, which was primarily the result of the timing of purchases and maturities of marketable securities, capital expenditures for owned real estate projects (including construction of our development center) of $28 million, capital expenditures for data center and office space projects of $36 million, and purchases of non-marketable equity and other investments of $5 million. These payments were partially offset by proceeds of $33 million from the sale of marketable securities.

Cash used in investing activities for the nine months ended October 31, 2018 was $640 million, which was primarily the result of a net cash outflow of $1.4 billion related to the Adaptive Insights acquisition, capital expenditures for data center and office space projects of $158 million, capital expenditures related to the construction of our development center of $110 million, and purchases of non-marketable equity and other investments of $33 million. These payments were partially offset by the timing of purchases and maturities of marketable securities, proceeds of $946 million from the sale of marketable securities, and proceeds of $18 million from the sales and maturities of non-marketable equity and other investments. The sale of marketable securities during fiscal 2019 was to prepare for the Adaptive Insights acquisition.

Cash used in investing activities for the nine months ended October 31, 2017 was $617 million, which was primarily the result of the timing of purchases and maturities of marketable securities, capital expenditures for owned real estate projects (including construction of our development center) of $80 million, capital expenditures for data center and office space projects of $105 million, and purchases of non-marketable equity and other investments of $11 million. These payments were partially offset by proceeds of $223 million from the sale of marketable securities.

We expect capital expenditures related to the construction of our development center will be approximately $200 million for fiscal 2019. We expect capital expenditures, excluding the development center project, will be approximately $200 million for fiscal 2019. We expect that these capital outlays will largely be used to expand the infrastructure of our data centers and to build out additional office space to support our growth.

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Financing Activities

Cash provided by financing activities was $3 million for the three months ended October 31, 2018, which was primarily due to proceeds from the issuance of common stock from employee equity plans.

Cash provided by financing activities for the three months ended October 31, 2017 was $1.0 billion, which was primarily due to the issuance of $1.15 billion principal amount of 0.25% convertible senior notes due October 1, 2022, net of issuance costs of $18 million, and the related sale of warrants for $81 million and purchase of note hedges for $176 million. For further information, see Note 11 of the notes to condensed consolidated financial statements. In addition, cash flows from financing activities included $2 million of proceeds from the issuance of common stock from employee equity plans.

Cash used in financing activities was $306 million for the nine months ended October 31, 2018, which was primarily due to the principal payment of $350 million of 0.75% convertible senior notes, offset by proceeds from the issuance of common stock from employee equity plans.

Cash provided by financing activities for the nine months ended October 31, 2017 was $1.1 billion, which was primarily due to the issuance of $1.15 billion principal amount of 0.25% convertible senior notes due October 1, 2022, net of issuance costs of $18 million, and the related sale of warrants for $81 million and purchase of note hedges for $176 million. For further information, see Note 11 of the notes to condensed consolidated financial statements. In addition, cash flows from financing activities included $37 million of proceeds from the issuance of common stock from employee equity plans.

Convertible Senior Notes

In June 2013, we completed an offering of $350 million of 0.75% convertible senior notes due July 15, 2018 (“2018 Notes”), which were subsequently converted by note holders during the second quarter of fiscal 2019. In June 2013, concurrent with the 2018 Notes offering, we issued $250 million of 1.50% convertible senior notes due July 15, 2020 (“2020 Notes”). In September 2017, we completed an offering of $1.15 billion of 0.25% convertible senior notes due October 1, 2022 (“2022 Notes” and together with the 2018 Notes and 2020 Notes, the “Notes”).

Holders may convert the Notes prior to maturity upon the occurrence of certain circumstances. Upon conversion, holders of the Notes will receive cash, shares of Class A common stock, or a combination of cash and shares of Class A common stock, at our election. It is our intent to settle the 2020 Notes using a combination of cash and shares of Class A common stock.

The 2020 Notes were convertible at the option of the holders during the second and third quarter of fiscal 2019 and will continue to be convertible during the fourth quarter of fiscal 2019 since the trigger for early conversion was met. Specifically, the last reported sale price of our Class A common stock exceeded 130% of the conversion price of the 2020 Notes for more than 20 trading days during the 30 consecutive trading days ended April 30, 2018, July 31, 2018, and October 31, 2018. Accordingly, the 2020 Notes are classified as current on the condensed consolidated balance sheet as of October 31, 2018. From May 1, 2018 through the date of this filing, the amount of the principal balance of the 2020 Notes that has been converted or for which conversion has been requested was not material.

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Free Cash Flows

In evaluating our performance internally, we focus on long-term, sustainable growth in free cash flows. We define free cash flows, a non-GAAP financial measure, as net cash provided by (used in) operating activities minus capital expenditures (excluding owned real estate projects). See “Non-GAAP Financial Measures” below for further information.

Free cash flows decreased by $49 million to $59 million for the three months ended October 31, 2018, compared to $108 million for the prior year period. The decrease was primarily due to increases in capital expenditures (excluding owned real estate projects) and higher operating expenses driven by increased headcount and the Adaptive Insights acquisition, including one-time transaction and integration-related costs, partially offset by increases in sales and the related cash collections.

Free cash flows decreased by $35 million to $199 million for the nine months ended October 31, 2018, compared to $234 million for the prior year period. The decrease was primarily due to increases in capital expenditures (excluding owned real estate projects) and higher operating expenses driven by increased headcount and the Adaptive Insights acquisition, including one-time transaction and integration-related costs, partially offset by increases in sales and the related cash collections.

Reconciliations of Net cash provided by (used in) operating activities to free cash flows were as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2018	2017	2018	2017
Net cash provided by (used in) operating activities	$114,296	$144,031	$356,145	$339,179
Capital expenditures, excluding owned real estate projects	(55,427)	(36,356)	(157,635)	(105,477)
Free cash flows	$58,869	$107,675	$198,510	$233,702

	Trailing Twelve Months Ended October 31,	
	2018	2017
Net cash provided by (used in) operating activities	$ 482,693	$ 448,910
Capital expenditures, excluding owned real estate projects	(193,694)	(137,755)
Free cash flows	$ 288,999	$ 311,155

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Non-GAAP Financial Measures

Regulation S-K Item 10(e), "Use of non-GAAP financial measures in Commission filings," defines and prescribes the conditions for use of non-GAAP financial information. Our measures of non-GAAP operating expenses, non-GAAP operating margin, and free cash flows each meet the definition of a non-GAAP financial measure.

Non-GAAP Operating Expenses and Non-GAAP Operating Margins

We define non-GAAP operating expenses as our total operating expenses excluding the following components, which we believe are not reflective of our ongoing operational expenses. Similarly, the same components are also excluded from the calculation of non-GAAP operating margins. In each case, for the reasons set forth below, management believes that excluding the component provides useful information to investors and others in understanding and evaluating our operating results and prospects in the same manner as management, in comparing financial results across accounting periods and to those of peer companies, and to better understand the long-term performance of our core business.

- Share-Based Compensation Expenses. Although share-based compensation is an important aspect of the compensation of our employees and executives, management believes it is useful to exclude share-based compensation expenses to better understand the long-term performance of our core business and to facilitate comparison of our results to those of peer companies. Share-based compensation expenses are determined using a number of factors, including our stock price, volatility, and forfeiture rates that are beyond our control and generally unrelated to operational decisions and performance in any particular period. Further, share-based compensation expenses are not reflective of the value ultimately received by the grant recipients.
- Other Operating Expenses. Other operating expenses includes employer payroll tax-related items on employee stock transactions and amortization of acquisition-related intangible assets. The amount of employer payroll tax-related items on employee stock transactions is dependent on our stock price and other factors that are beyond our control and do not correlate to the operation of the business. For business combinations, we generally allocate a portion of the purchase price to intangible assets. The amount of the allocation is based on estimates and assumptions made by management and is subject to amortization. The amount of purchase price allocated to intangible assets and the term of its related amortization can vary significantly and are unique to each acquisition and thus we do not believe it is reflective of our ongoing operations.

Free Cash Flows

We define free cash flows as net cash provided by (used in) operating activities minus capital expenditures (excluding owned real estate projects). Capital expenditures deducted from cash flows from operations do not include purchases of land and buildings, and construction costs related to our new development center and other owned buildings. We exclude these owned real estate projects as they are infrequent in nature. For the current fiscal year, these costs primarily represent the construction of our new development center, which is anticipated to be completed in fiscal 2020. We use free cash flows as a measure of financial progress in our business, as it balances operating results, cash management, and capital efficiency. We believe information regarding free cash flows provides investors and others with an important perspective on the cash available to make strategic acquisitions and investments, to fund ongoing operations, and to fund other capital expenditures.

Limitations on the Use of Non-GAAP Financial Measures

A limitation of our non-GAAP financial measures of non-GAAP operating expenses, non-GAAP operating margin, and free cash flows is that they do not have uniform definitions. Our definitions will likely differ from the definitions used by other companies, including peer companies, and therefore comparability may be limited. Further, the non-GAAP financial measure of non-GAAP operating expenses has certain limitations because it does not reflect all items of expense that affect our operations and are reflected in the GAAP financial measure of total operating expenses. In the case of share-based compensation, if we did not pay out a portion of compensation in the form of share-based compensation and related employer payroll tax-related items, the cash salary expense included in costs of revenues and operating expenses would be higher, which would affect our cash position.

We compensate for these limitations by reconciling the non-GAAP financial measures to the most comparable GAAP financial measures. These non-GAAP financial measures should be considered in addition to, not as a substitute for or in isolation from, measures prepared in accordance with GAAP. We encourage investors and others to review our financial information in its entirety, not to rely on any single financial measure, and to view our non-GAAP financial measures in conjunction with the most comparable GAAP financial measures.

See Results of Operations—Operating Expenses and Results of Operations—Operating Margins for reconciliations from the most directly comparable GAAP financial measures, GAAP operating expenses and GAAP operating margins, to the non-GAAP financial measures, non-GAAP operating expenses and non-GAAP operating margins, for the three and nine months ended October 31, 2018 and 2017.

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See Liquidity and Capital Resources—Free Cash Flows for a reconciliation from the most comparable GAAP financial measure, Net cash provided by (used in) operating activities, to the non-GAAP financial measure, free cash flow, for the three and nine months ended October 31, 2018 and 2017.

Contractual Obligations

Our contractual obligations primarily consist of our convertible senior notes, as well as obligations under leases for office space, co-location facilities for data center capacity, and agreements related to computing infrastructure platforms for business operations. As of October 31, 2018, the future non-cancelable minimum payments under operating leases and computing infrastructure agreements were $452 million. During the remainder of fiscal 2019, we anticipate leasing additional office space near our headquarters and in various other locations around the world to support our growth. In addition, our existing lease agreements often provide us with options to renew. We expect our future operating lease obligations will increase as we expand our operations.

We are not required to make principal payments under the 2020 Notes and 2022 Notes prior to maturity. If the 2020 Notes and 2022 Notes are not converted to Class A common stock prior to their maturity dates, we are required to repay $250 million in principal on July 15, 2020 and $1.15 billion in principal on October 1, 2022. We are also required to make interest payments on a semi-annual basis at the interest rates described in Note 11 of the notes to condensed consolidated financial statements.

In January 2014, we entered into a 95-year lease for a 6.9-acre parcel of land in Pleasanton, California, under which we paid $2 million for base rent from commencement through December 31, 2020. Annual rent payments of $0.2 million plus increases based on increases in the consumer price index begin on January 1, 2021 and continue through the end of the lease. Our new development center, consisting of approximately 410,000 square feet of office space, is being constructed on this property.

We do not consider outstanding purchase orders to be contractual obligations as they represent authorizations to purchase rather than binding agreements.

Off-Balance Sheet Arrangements

Through October 31, 2018, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities, that would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Critical Accounting Policies and Estimates

Our condensed consolidated financial statements are prepared in accordance with GAAP. The preparation of these condensed consolidated financial statements requires us to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses, and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

During the nine months ended October 31, 2018, there were no significant changes to our critical accounting policies and estimates as described in the financial statements contained in the Annual Report on Form 10-K for the year ended January 31, 2018 filed with the Securities and Exchange Commission (“SEC”) on March 14, 2018, other than the addition of Business Combinations as described below.

Business Combinations

Accounting for business combinations requires us to make significant estimates and assumptions. We allocate the purchase consideration to the tangible and intangible assets acquired and liabilities assumed based on their estimated fair values, with the excess recorded to goodwill. Estimates in the valuation include, but are not limited to, future expected cash flows, expected asset lives, royalty rates, and discount rates.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Risk

We transact business globally in multiple currencies. As a result, our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates. As of October 31, 2018 and 2017, our most significant currency exposures were the Euro, Canadian dollar, British pound, and Australian dollar.

Due to our exposure to market risks that may result from changes in foreign currency exchange rates, we enter into foreign currency derivative hedging transactions to mitigate these risks. For further information, see Note 10 of the notes to condensed consolidated financial statements.

Interest Rate Sensitivity

We had cash, cash equivalents, and marketable securities totaling $1.6 billion and $3.3 billion as of October 31, 2018 and January 31, 2018, respectively. Cash equivalents and marketable securities were invested primarily in U.S. agency obligations, U.S. treasury securities, corporate bonds, commercial paper, and money market funds. The cash, cash equivalents, and marketable securities are held for working capital purposes. Our investment portfolios are managed to preserve capital and meet liquidity needs. We do not enter into investments for trading or speculative purposes.

Our cash equivalents and our portfolio of debt securities are subject to market risk due to changes in interest rates. Fixed rate securities may have their market value adversely affected due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fluctuate due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However, because we classify our debt securities as "available-for-sale", no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or declines in fair value are determined to be other-than-temporary.

An immediate increase of 100-basis points in interest rates would have resulted in a $2 million and $10 million market value reduction in our investment portfolio as of October 31, 2018 and January 31, 2018, respectively. An immediate decrease of 100-basis points in interest rates would have increased the market value by $2 million and $10 million as of October 31, 2018 and January 31, 2018, respectively. This estimate is based on a sensitivity model that measures market value changes when changes in interest rates occur. Fluctuations in the value of our investment securities caused by a change in interest rates (gains or losses on the carrying value) are recorded in Accumulated other comprehensive income (loss) and are realized only if we sell the underlying securities before maturity.

Market Risk and Market Interest Risk

In June 2013, we completed an offering of $350 million of 0.75% convertible senior notes due July 15, 2018, which were subsequently converted by note holders during the second quarter of fiscal 2019. In June 2013, concurrent with the 2018 Notes offering, we issued $250 million of 1.50% convertible senior notes due July 15, 2020. In September 2017, we completed an offering of $1.15 billion of 0.25% convertible senior notes due October 1, 2022.

Holders may convert the Notes prior to maturity upon the occurrence of certain circumstances. Upon conversion, holders of the Notes will receive cash, shares of Class A common stock, or a combination of cash and shares of Class A common stock, at our election.

Concurrently with the issuance of the Notes, we entered into separate note hedge and warrant transactions. These separate transactions were completed to reduce the potential economic dilution from the conversion of the Notes.

The 2020 Notes and 2022 Notes have fixed annual interest rates of 1.50% and 0.25%, respectively, and therefore we do not have economic interest rate exposure on our Notes. However, the values of the 2020 Notes and 2022 Notes are exposed to interest rate risk. Generally, the fair market value of our fixed interest rate 2020 Notes and 2022 Notes will increase as interest rates fall and decrease as interest rates rise. In addition, the fair values of the 2020 Notes and 2022 Notes are affected by our stock price. The carrying values of the 2020 Notes and 2022 Notes were $230 million and $961 million, respectively, as of October 31, 2018. These represent the liability component of the principal balance of our Notes as of October 31, 2018. The total estimated fair values of the 2020 Notes and 2022 Notes as of October 31, 2018 were $418 million and $1.3 billion, respectively. The fair values were determined based on the quoted bid prices of the 2020 Notes and 2022 Notes in an over-the-counter market as of the last day of trading for the current fiscal quarter, which were $167.32 and $110.85, respectively. For further information, see Note 11 of the notes to condensed consolidated financial statements.

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ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"), as of the end of the period covered by this report.

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on management's evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are designed to, and are effective to, provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures.

(b) Changes in Internal Control Over Financial Reporting

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our most recently completed fiscal quarter. Based on that evaluation, our principal executive officer and principal financial officer concluded that there has not been any material change in our internal control over financial reporting during the quarter covered by this report that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we are or may be involved in various legal proceedings arising from the normal course of business including matters related to alleged infringement of third-party patents and other intellectual property rights, commercial, employment, and other claims. We are not presently a party to any litigation the outcome of which we believe, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, cash flows, or financial condition. Defending such proceedings is costly and can impose a significant burden on management and employees, we may receive unfavorable preliminary or interim rulings in the course of litigation, and there can be no assurances that favorable final outcomes will be obtained. The resolution of legal matters could prevent us from offering one or more of our applications, services or features to others, could require us to change our technology or business practices, pay monetary damages or enter into short- or long-term royalty or licensing agreements, or could otherwise be material to our financial condition or cash flows, or both, or adversely affect our operating results.

ITEM 1A. RISK FACTORS

Investing in our securities involves a high degree of risk. You should consider carefully the risks and uncertainties described below, together with all of the other information in this report, including the condensed consolidated financial statements and the related notes included elsewhere in this report, before making an investment decision. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that materially and adversely affect our business. If any of the following risks actually occurs, our business operations, financial condition, results of operations, and prospects could be materially and adversely affected. The market price of our securities could decline due to the materialization of these or any other risks, and you could lose part or all of your investment.

Risk Factors Related to Our Business

If our security measures are breached or unauthorized access to customer data is otherwise obtained, our applications may be perceived as not being secure, customers may reduce the use of or stop using our applications, and we may incur significant liabilities.

Our applications involve the storage and transmission of our customers' sensitive and proprietary information, including personal or identifying information regarding their employees, customers, and suppliers as well as their finance and payroll data. As a result, unauthorized access or use of this data could expose us to regulatory actions, litigation, investigations, remediation obligations, damage to our reputation and brand, supplemental disclosure obligations, loss of customer and partner confidence in the security of our applications, destruction of information, indemnity obligations, and resulting fees, costs, expenses, loss of revenues, and other potential liabilities. We devote significant financial and personnel resources to implement and maintain security measures. While we have security measures in place designed to protect the integrity of customer information and prevent data loss, misappropriation, and other security breaches, if these measures are compromised as a result of third-party action, including intentional misconduct by computer hackers, employee error, malfeasance, or otherwise, and someone obtains unauthorized access to or use of our customers' data, our reputation could be damaged, our business may suffer, and we could incur significant liabilities as well as incur significant costs to remediate any incidents. Cyber security challenges, including threats to our own IT infrastructure or those of our customers or third-party providers, are often targeted at companies such as ours, and may take a variety of forms ranging from individual and groups of hackers to sophisticated organizations. Key cyber security risks range from viruses, worms, and other malicious software programs to "mega breaches" targeted against cloud services and other hosted software, any of which can result in disclosure of confidential information and intellectual property, defective products, production downtimes, supply shortages, and compromised data. Because the techniques used to obtain unauthorized access or sabotage systems change frequently and generally are not identified until they are launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, if a high-profile security breach occurs with respect to an industry peer, our customers and potential customers may generally lose trust in the security of financial management and HCM applications or analytics platforms. Any or all of these issues could negatively affect our ability to attract new customers, cause existing customers to elect to terminate or not renew their subscriptions, result in reputational damage, cause us to pay remediation costs and/or issue service credits or refunds to customers for prepaid and unused subscription services, or result in lawsuits, regulatory fines, or other action or liabilities, which could adversely affect our business and operating results.

We depend on data centers and computing infrastructure operated by third parties and any disruption in these operations could adversely affect our business.

We host our applications and serve our customers from data centers located in Ashburn, Virginia; Atlanta, Georgia; Portland, Oregon; Dublin, Ireland; Amsterdam, the Netherlands; and Toronto, Canada. While we control and have access to our servers and all of the components of our network that are located in our external data centers, we do not control the operation and security of these facilities. The owners of our data center facilities have no obligation to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew these agreements on commercially reasonable terms, or if one of our data center operators is acquired or ceases business, we may be required to transfer our servers and other infrastructure to new data center facilities, and we may incur significant costs and experience possible service interruption in connection with doing so.

In addition, we rely upon third-party hosted infrastructure partners, including Amazon Web Services (“AWS”), to serve customers and operate certain aspects of our services, such as environments for development testing, training, and sales demonstrations, as well as others. Given this, any disruption of or interference at our hosted infrastructure partners would impact our operations and our business could be adversely impacted.

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Problems faced by our third-party data center operations or hosted infrastructure partners, with the telecommunications network providers with whom we or they contract, or with the systems by which our telecommunications providers allocate capacity among their customers, including us, could adversely affect the experience of our customers. Our third-party data center operators or hosted infrastructure partners could decide to close their facilities without adequate notice. In addition, any financial difficulties, such as bankruptcy, faced by our third-party data center operators, our hosted infrastructure partners or any of the other service providers with whom we or they contract may have negative effects on our business, the nature and extent of which are difficult to predict. Additionally, if our data centers or hosted infrastructure partners are unable to keep up with our needs for capacity, this could have an adverse effect on our business. Any changes in third-party service levels at our data centers or at our hosted infrastructure partners or any errors, defects, disruptions, or other performance problems with our applications or the hosted infrastructure on which they run could adversely affect our reputation and may damage our customers' stored files or result in lengthy interruptions in our services. Interruptions in our services might adversely affect our reputation and operating results, cause us to issue refunds or service credits to customers for prepaid and unused subscription services, subject us to potential liabilities, result in contract terminations, or adversely affect our renewal rates.

Furthermore, our financial management application is essential to Workday's and our customers' financial projections, reporting, and compliance programs, particularly customers who are public reporting companies. Any interruption in our service may affect the availability, accuracy or timeliness of such projections, reporting and compliance programs and as a result could damage our reputation, cause our customers to terminate their use of our applications, require us to issue refunds for prepaid and unused subscription services, require us to indemnify our customers against certain losses, and prevent us from gaining additional business from current or future customers as well as impact our ability to accurately and timely meet our reporting and other compliance obligations.

If we fail to manage our technical operations infrastructure or experience service outages or delays in the deployment of our applications, we may be subject to liabilities and our reputation and operating results may be adversely affected.

We have experienced significant growth in the number of users, transactions, and data that our operations infrastructure supports. We seek to maintain sufficient excess capacity in our operations infrastructure to meet the needs of all of our customers, as well as our own needs, and to ensure that our services and solutions are accessible within an acceptable load time. We also seek to maintain excess capacity to facilitate the rapid provision of new customer deployments and the expansion of existing customer deployments. In addition, we need to properly manage our technological operations infrastructure in order to support version control, changes in hardware and software parameters, updates, the evolution of our applications, and to reduce infrastructure latency associated with dispersed geographic locations. However, the provision of new hosting infrastructure requires significant lead time. If we do not accurately predict our infrastructure requirements, our existing customers may experience service outages. If our operations infrastructure fails to scale, customers may experience delays as we seek to obtain additional capacity.

We have experienced, and may in the future experience, system disruptions, outages, and other performance problems. These problems may be caused by a variety of factors, including infrastructure changes, vendor issues, human or software errors, viruses, security attacks (internal and external), fraud, spikes in customer usage, and denial of service issues. In some instances, we may not be able to identify the cause or causes of these performance problems within an acceptable period of time. Our customer agreements typically provide service level commitments on a monthly basis. If we are unable to meet the stated service level commitments or suffer extended periods of unavailability for our applications, we may be contractually obligated to issue service credits or refunds to customers for prepaid and unused subscription services, our customers may make warranty or other claims against us, or we could face contract terminations which would adversely affect our attrition rates. Any extended service outages could result in customer losses, and adversely affect our reputation, business, and operating results.

Privacy concerns and domestic or foreign laws and regulations may reduce the effectiveness of our applications, result in significant costs and compliance challenges, and adversely affect our business.

Our customers can use our applications to collect, use, and store personal or identifying information regarding their employees, customers, and suppliers. National and local governments and agencies in the countries in which our customers operate have adopted, are considering adopting, or may adopt laws and regulations regarding the collection, use, storage, processing, and disclosure of personal information obtained from consumers and individuals, which could impact our ability to offer our services in certain jurisdictions or our customers' ability to deploy our solutions globally. Privacy-related laws are particularly stringent in Europe. The costs of compliance with and other burdens imposed by privacy-related laws, regulations, and standards may limit the use and adoption of our services, reduce overall demand for our services, lead to significant fines, penalties, or liabilities for noncompliance, or slow the pace at which we close sales transactions, any of which could harm our business. Moreover, if we or our subprocessors fail to adhere to adequate data protection practices around the usage of our customers' personal data, it may damage our reputation and brand.

Additionally, we expect that existing laws, regulations, and standards may be interpreted in new and differing manners in the future, and may be inconsistent among jurisdictions. Future laws, regulations, standards, and other obligations, and changes in the interpretation of existing laws, regulations, standards, and other obligations could result in increased regulation, increased costs of compliance and penalties for non-compliance, and limitations on data collection, use, disclosure, and transfer for Workday and our customers. In 2016, the European Union ("EU") and United States agreed to a framework for data transferred from the EU to the United States, called the Privacy Shield, but this new framework has been challenged by private parties and may face additional challenges by national regulators or additional private parties. Additionally, in 2016 the EU adopted a new regulation governing data privacy called the General Data Protection Regulation ("GDPR"), which became effective in May 2018. The GDPR establishes new requirements applicable to the handling of personal data and imposes penalties for non-compliance of up to 4% of worldwide revenue. Customers, particularly in the EU, are seeking assurances from their suppliers, including us, that their processing of personal data of EU nationals is in accordance with the GDPR, and if we are unable to provide adequate assurances to such customers, demand for our applications could be adversely affected. In addition, we must continue to seek assurances from our subprocessors that they are handling personal data in accordance with GDPR requirements in order to meet our own obligations under the GDPR.

The costs of compliance with, and other burdens imposed by, privacy laws and regulations that are applicable to the businesses of our customers may adversely affect our customers' ability and willingness to process, handle, store, use, and transmit demographic and personal data of their employees, customers, and suppliers, which in turn could limit the use, effectiveness, and adoption of our applications and reduce overall demand. In addition, the other bases on which we and our customers rely for the transfer of data, such as model contracts, continue to be subjected to regulatory and judicial scrutiny. In 2017, another legal challenge to the validity of the EU Standard Contractual Clauses (a data transfer mechanism) was referred to the Court of Justice of the EU for review. If we or our customers are unable to transfer data between and among countries and regions in which we operate, it could decrease demand for our applications, require us to restrict our business operations, and impair our ability to maintain and grow our customer base and increase our revenue. Even the perception of privacy concerns, whether or not valid, may inhibit the adoption, effectiveness, or use of our applications.

In addition to government activity, privacy advocacy and other industry groups have established or may establish various new, additional, or different self-regulatory standards that may place additional burdens on us. Our customers may expect us to meet voluntary certifications or adhere to other standards established by third parties. If we are unable to maintain these certifications or meet these standards, it could reduce demand for our applications and adversely affect our business.

We have experienced rapid growth. If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service and operational controls, or adequately address competitive challenges.

We have experienced, and are continuing to experience, a period of rapid growth in our customers, headcount, and operations. In particular, we grew from approximately 1,550 employees at the time of our initial public offering ("IPO") in October 2012 to approximately 10,200 employees as of October 31, 2018, and we have also significantly increased the size of our customer base. We anticipate that we will continue to expand our operations and headcount in the near term, and to expand our customer base. This growth has placed, and future growth will place, a significant strain on our management, general and administrative resources, and operational infrastructure. Our success will depend in part on our ability to manage this growth effectively and to scale our operations. To manage the expected growth of our operations and personnel, we will need to continue to improve our operational, financial, and management controls as well as our reporting systems and procedures. As we continue to grow, we also need to ensure that our policies and procedures evolve to reflect our current operations and are appropriately communicated to and observed by employees, and that we appropriately manage our corporate information assets, including confidential and proprietary information. Failure to effectively manage growth could result in difficulty or delays in deploying customers, declines in quality or customer satisfaction, increases in costs, difficulties in introducing new features, or other operational difficulties, and any of these difficulties could adversely impact our business performance and results of operations.

We depend on our senior management team and the loss of one or more key employees could adversely affect our business.

Our success and future growth depend largely upon the continued services of our executive officers and other key employees. We also rely on our leadership team in the areas of product development, marketing, sales, services, and general and administrative functions and on mission-critical individual contributors in product development. From time to time, there may be changes in our executive management team resulting from the hiring or departure of executives, which could disrupt our business. We do not have employment agreements with our executive officers or other key personnel that require them to continue to work for us for any specified period, and they could terminate their employment with us at any time. The loss of one or more of our executive officers or other key employees and any failure to develop an appropriate succession plan for these persons could have a serious adverse effect on our business and results of operations.

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The failure to attract and retain highly skilled employees could adversely affect our business and our future growth prospects.

To execute our growth plan, we must attract and retain highly qualified personnel, and our managers must be successful in hiring employees who share our values and have the competencies to succeed at Workday. Competition for these personnel is intense, especially for engineers with high levels of experience in designing and developing software and Internet-related services, and for senior sales executives. From time to time, we have experienced, and we expect to continue to experience, difficulty in hiring and retaining employees with appropriate qualifications, and we may not be able to fill positions in desired geographic areas or at all.

Many of the companies with which we compete for experienced personnel have greater resources than we have and some of these companies may offer more lucrative compensation packages. Particularly in the San Francisco Bay Area, job candidates and existing employees carefully consider the value of the equity awards they receive in connection with their employment. If the perceived value of our equity awards declines, or if the mix of equity and cash compensation that we offer is unattractive, it may adversely affect our ability to recruit and retain highly skilled employees. Job candidates may also be threatened with legal action under agreements with their existing employers if we attempt to hire them, which could have a chilling effect on hiring and result in a diversion of our time and resources. Additionally, laws and regulations, such as restrictive immigration laws, and restrictions on travel or availability of visas, may limit our ability to recruit internationally. We must also continue to retain and motivate existing employees through our compensation practices, company culture, and career development opportunities. If we fail to attract new personnel or to retain our current personnel, our business and future growth prospects could be adversely affected.

If we cannot maintain our corporate culture, we could lose the innovation, teamwork, and passion that we believe contribute to our success, and our business may be harmed.

We believe that a critical component of our success has been our corporate culture, as reflected in our core values: employees, customer service, innovation, integrity, fun, and profitability. We have invested substantial time and resources in building our team. As we continue to grow, both organically and through acquisitions of employee teams, and develop the infrastructure associated with being a more mature public company, we will need to maintain our corporate culture among a larger number of employees dispersed in various geographic regions. Any failure to preserve our culture could negatively affect our future success, including our ability to retain and recruit personnel and to effectively focus on and pursue our corporate objectives.

The markets in which we participate are intensely competitive, and if we do not compete effectively, our operating results could be adversely affected.

The markets for financial management and HCM applications are highly competitive, with relatively low barriers to entry for some applications or services. Our primary competitors are SAP and Oracle, well-established providers of financial management and HCM applications, which have long-standing relationships with many customers. Some customers may be hesitant to switch vendors or to adopt cloud applications such as ours, and prefer to maintain their existing relationships with competitors. SAP and Oracle are larger and have greater name recognition, significantly longer operating histories, larger marketing budgets, and significantly greater resources than we do. These vendors, as well as other competitors, could offer financial management and HCM applications on a standalone basis at a low price or bundled as part of a larger sale. In order to take advantage of customer demand for cloud applications, legacy vendors are expanding their cloud applications through acquisitions, strategic alliances and organic development. We also face competition from vendors of specific applications, some of which offer cloud-based solutions. These vendors include, without limitation: The Ultimate Software Group, Inc., Automatic Data Processing, Inc., Infor Global Solutions, and Ceridian, Inc. We may also face competition from a variety of vendors of cloud-based and on-premise software applications that address only one or a portion of our applications. In addition, other companies that provide cloud applications in different target markets may develop applications or acquire companies that operate in our target markets, and some potential customers may elect to develop their own internal applications. With the introduction of new technologies and market entrants, we expect this competition to intensify in the future.

Many of our competitors are able to devote greater resources to the development, promotion, and sale of their products and services. Furthermore, our current or potential competitors may be acquired by third parties with greater available resources and the ability to initiate or withstand substantial price competition. In addition, many of our competitors have established marketing relationships, access to larger customer bases, and major distribution agreements with consultants, system integrators, and resellers. Our competitors may also establish cooperative relationships among themselves or with third parties that may further enhance their offerings or resources. If our competitors' products, services, or technologies become more accepted than our products, if they are successful in bringing their products or services to market earlier than ours, or if their products or services are more technologically capable than ours, then our revenues could be adversely affected. In addition, some of our competitors may offer their products and services at a lower price. If we are unable to achieve our target pricing levels, our operating results would be negatively affected. Pricing pressures and increased competition could result in reduced sales, reduced margins, losses, or a failure to maintain or improve our competitive market position, any of which could adversely affect our business.

If we expand the capabilities of our cloud applications and/or seek to operate in new markets, we may not be effective in convincing prospective customers that our solutions will address their needs. Also, we may not be able to properly price our solutions in these markets, which could negatively affect our ability to sell to customers. Furthermore, customers may demand more features and professional services, which may require us to devote greater research and development, sales, support, and professional services resources to these customers. This could strain our resources and result in increased costs. If we are not able to address these challenges, or if our investments in selling and marketing our solutions to new markets are unsuccessful, our business could be adversely affected.

If the market for enterprise cloud computing grows more slowly than in recent years, our business could be adversely affected.

Our success will depend to a substantial extent on the continued growth of cloud computing in general, and of financial management and HCM services in particular. Many enterprises have invested substantial personnel and financial resources to integrate traditional enterprise software into their businesses, and therefore may be reluctant or unwilling to migrate to cloud computing. It is difficult to predict customer adoption rates and demand for our applications, the future growth rate and size of the cloud computing market, or the entry of competitive applications. The continued expansion of the cloud computing market depends on a number of factors, including the cost, performance, and perceived value associated with cloud computing as well as the ability of cloud computing companies to address security and privacy concerns. Further, the cloud computing market is less developed in many jurisdictions outside of the United States. If we or other cloud computing providers experience security incidents, loss of customer data, disruptions in delivery, or other problems, the market for cloud computing applications as a whole, including our applications, may be negatively affected. If there is a reduction in demand for cloud computing caused by a lack of customer acceptance, technological challenges, weakening economic conditions, security or privacy concerns, competing technologies and applications, decreases in corporate spending, or otherwise, it could result in decreased revenues or growth rates and our business could be adversely affected.

If we are not able to provide successful enhancements, new features and modifications, our business and results of operations could be adversely affected.

If we are unable to provide enhancements and new features for our existing applications or new applications that achieve market acceptance or that keep pace with rapid technological developments, our business and results of operations could be adversely affected. For example, we are focused on enhancing the features and functionality of our applications to improve their utility to larger customers with complex, dynamic, and global operations. The success of enhancements, new features, and applications depends on several factors, including their timely completion, introduction, and market acceptance as well as access to the technologies required to build and improve our applications, such as the datasets required to train our machine learning models. Failure in this regard may significantly impair our revenue growth by negatively impacting customer renewal rates or result in an inability to attract new customers. In addition, because our applications are designed to operate on a variety of systems, we will need to continuously modify and enhance our applications to keep pace with changes in Internet-related hardware, iOS, Android, and other mobile-related technologies and other software, communication, browser, and database technologies. We may not be successful in either developing these modifications and enhancements or in bringing them to market in a timely fashion. We must also appropriately balance the application capability demands of our current customers with the capabilities required to address the broader market. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could increase our product development expenses. Any failure of our applications to operate effectively with future network platforms and technologies could reduce the demand for our applications, result in customer dissatisfaction, and adversely affect our business and results of operations.

Our applications must integrate with or incorporate a variety of third-party technologies, and if we are unable to ensure that our solutions integrate with or incorporate such technologies, demand for our applications and our operating results could be adversely affected.

Our applications must integrate with or incorporate a variety of technologies and we must continuously modify and enhance our applications to adapt to changes in operating systems, hardware, software, communication, browser, and database technologies. Any failure of our solutions to operate effectively with future technologies or our failure to respond to changes in a timely and effective manner could reduce the demand for our applications, result in customer dissatisfaction, and harm our operating results and business.

If our applications fail to perform properly, our reputation could be adversely affected, our market share could decline, and we could be subject to liability claims.

Our applications are inherently complex and may contain material defects or errors. Any defects in functionality or that cause interruptions in the availability of our applications could result in:

- loss or delayed market acceptance and sales;
- legal claims, including breach of warranty claims;
- issuance of refunds or service credits to customers for prepaid and unused subscription services;

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- loss of customers;
- diversion of development and customer service resources; and
- injury to our reputation.

The costs incurred in correcting any material defects or errors might be substantial and could adversely affect our operating results.

Because of the large amount of data that we collect and process, it is possible that hardware failures or errors in our systems could result in data loss or corruption, or cause the information that we collect to be incomplete or contain inaccuracies that our customers regard as significant. Furthermore, the availability or performance of our applications could be adversely affected by a number of factors, including customers' inability to access the Internet, the failure of our network or software systems, security breaches, or variability in user traffic for our services. For example, our customers access our applications through their Internet service providers. If a service provider fails to provide sufficient capacity to support our applications or otherwise experiences service outages, such failure could interrupt our customers' access to our applications, which could adversely affect their perception of our applications' reliability and our revenues. We may be required to issue credits or refunds for prepaid amounts related to unused services or otherwise be liable to our customers for damages they may incur resulting from certain of these events. In addition to potential liability, if we experience interruptions in the availability of our applications, our reputation could be adversely affected and we could lose customers.

Our errors and omissions insurance may be inadequate or may not be available in the future on acceptable terms, or at all. In addition, our policy may not cover all claims made against us and defending a suit, regardless of its merit, could be costly and divert management's attention.

Catastrophic events may disrupt our business.

Our corporate headquarters are located in Pleasanton, California, and we have data centers located in Ashburn, Virginia; Atlanta, Georgia; Portland, Oregon; Dublin, Ireland; Amsterdam, the Netherlands; and Toronto, Canada. We also rely on AWS's distributed computing infrastructure platform. The west coast of the United States contains active earthquake zones and the southeast is subject to seasonal hurricanes. Additionally, we rely on our network and third-party infrastructure and enterprise applications, internal technology systems, and our website for our development, marketing, operational support, hosted services, and sales activities. In the event of a major earthquake, hurricane, or other catastrophic event such as fire, power loss, telecommunications failure, vandalism, civil unrest, cyber-attack, geopolitical instability, war, terrorist attack, or the effects of climate change (such as drought, flooding, wildfires, increased storm severity, and sea level rise), we may be unable to continue our operations and may endure system interruptions, reputational harm, delays in our product development, lengthy interruptions in our services, breaches of data security, and loss of critical data, all of which could have an adverse effect on our business and operating results.

Because we sell applications to manage complex operating environments of large customers, we encounter long sales cycles, which could adversely affect our operating results in a given period.

Our ability to increase revenues and achieve and maintain profitability depends, in large part, on widespread acceptance of our applications by large businesses and other organizations. Sales efforts targeted at these large customers involve greater costs, longer sales cycles, and less predictability in completing some of our sales. Our customers' deployment timeframes vary based on many factors including the number and type of applications being deployed, the complexity and scale of the customers' businesses, the configuration requirements, the number of integrations with other systems, and other factors, many of which are beyond our control. In the large enterprise market, the customer's decision to use our applications may be an enterprise-wide decision and, therefore, these types of sales require us to provide greater levels of education regarding the use and benefits of our applications. In addition, our target customers may prefer to purchase applications that are critical to their business from one of our larger, more established competitors. Our typical sales cycles are six to twelve months but can extend for 18 months or more, and we expect that this lengthy sales cycle may continue or expand as customers increasingly adopt our applications beyond HCM. Longer sales cycles could cause our operating and financial results to suffer in a given period.

The loss of one or more of our key customers, or a failure to renew our subscription agreements with one or more of our key customers, could negatively affect our ability to market our applications.

We rely on our reputation and recommendations from key customers in order to promote subscriptions to our applications. The loss of, or failure to renew by, any of our key customers could have a significant impact on our revenues, reputation, and our ability to obtain new customers. In addition, acquisitions of our customers could lead to cancellation of our contracts with those customers or by the acquiring companies, thereby reducing the number of our existing and potential customers.

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Our business could be adversely affected if our customers are not satisfied with the deployment services provided by us or our partners.

Our business depends on our ability to satisfy our customers, both with respect to our application offerings and the professional services that are performed to help our customers use features and functions that address their business needs. Professional services may be performed by our own staff, by a third party, or by a combination of the two. Our strategy is to work with third parties to increase the breadth of capability and depth of capacity for delivery of these services to our customers, and third parties provide a majority of our deployment services. If customers are not satisfied with the quality of work performed by us or a third party or with the type of professional services or applications delivered, then we could incur additional costs to address the situation, the revenue recognition of the contract could be impacted, and the dissatisfaction with our services could damage our ability to expand the applications subscribed to by our customers. We must also align our product development and professional services operations in order to ensure that customers' evolving needs are met. Negative publicity related to our customer relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

Any failure to offer high-quality technical support services may adversely affect our relationships with our customers and our financial results.

Our customers depend on our support organization to provision the environments used by our customers and to resolve technical issues relating to our applications. We may be unable to respond quickly enough to accommodate short-term increases in customer demand for support services. We also may be unable to modify the format of our support services to compete with changes in support services provided by our competitors. Increased customer demand for these services, without corresponding revenues, could increase costs and adversely affect our operating results. In addition, our sales process is highly dependent on our applications and business reputation and on positive recommendations from our existing customers. Any failure to maintain high-quality technical support, or a market perception that we do not maintain high-quality support, could adversely affect our reputation, our ability to sell our applications to existing and prospective customers, and our business, operating results, and financial position.

Sales to customers outside the United States or with international operations expose us to risks inherent in global operations.

A key element of our growth strategy is to develop a worldwide customer base. Operating globally requires significant resources and management attention and will subject us to regulatory, economic, and political risks that are different from those in the United States. Our international expansion efforts may not be successful in creating demand for our applications outside of the United States or in effectively selling subscriptions to our applications in all of the markets we enter. In addition, we will face risks in doing business on a global scale that could adversely affect our business, including:

- the need to localize and adapt our applications for specific countries, including translation into foreign languages, localization of contracts for different legal jurisdictions, and associated expenses;
- the need for a go-to-market strategy that aligns application management efforts and the development of supporting infrastructure;
- stricter data privacy laws including requirements that customer data be stored and processed in a designated territory and obligations on us as a data processor;
- difficulties in appropriately staffing and managing foreign operations and providing appropriate compensation for local markets;
- difficulties in leveraging executive presence and company culture globally;
- different pricing environments, longer sales cycles, and longer trade receivables payment cycles, and collections issues;
- new and different sources of competition;
- potentially weaker protection for intellectual property and other legal rights than in the United States and practical difficulties in enforcing intellectual property and other rights;
- laws, customs, and business practices favoring local competitors;
-

restrictive governmental actions focused on cross-border trade, such as import and export restrictions, duties, quotas, tariffs, trade disputes and barriers or sanctions that may prevent us from offering certain portions of our products or services to a particular market, may increase our operating costs, or may subject us to monetary fines or penalties in case of unintentional noncompliance due to factors beyond our control;

- compliance challenges related to the complexity of multiple, conflicting and changing governmental laws and regulations, including employment, tax, privacy, and data protection laws and regulations;
- increased financial accounting and reporting burdens and complexities;
- restrictions on the transfer of funds;
- ensuring compliance with anti-corruption laws including the Foreign Corrupt Practices Act;
- the effects of currency fluctuations on our revenues and customer demand for our services;
- the cost and potential outcomes of any international claims or litigation;

- adverse tax consequences and tax rulings; and
- unstable economic and political conditions.

Any of the above factors may negatively impact our ability to sell our applications and offer services globally, reduce our competitive position in foreign markets, increase our costs of global operations, and reduce demand for our applications and services from global customers. Additionally, the majority of our international costs are denominated in local currencies and we anticipate that over time an increasing portion of our sales contracts outside the U.S. may be denominated in local currencies. Therefore, fluctuations in the value of the U.S. dollar and foreign currencies may impact our operating results when translated into U.S. dollars. We have a hedging program, but we cannot ensure that this hedging program will be effective, and we will continue to have risk of exchange rate fluctuations.

We have acquired, and may in the future acquire, other companies, employee teams, or technologies, which could divert our management's attention, result in additional dilution to our stockholders, and otherwise disrupt our operations and adversely affect our operating results.

We have acquired, and may in the future acquire, other companies, employee teams, or technologies to complement or expand our applications, enhance our technical capabilities, obtain personnel, or otherwise offer growth opportunities. For example, during the third quarter of fiscal 2019, we acquired Adaptive Insights. The pursuit of acquisitions may divert the attention of management and cause us to incur various expenses in identifying, investigating, and pursuing suitable acquisitions, whether or not they are consummated.

We have limited experience in acquisitions. We may not be able to integrate acquired personnel, operations, and technologies successfully, or effectively manage the combined operations following the acquisition. We also may not achieve the anticipated benefits from the acquisitions due to a number of factors, including:

- inability to integrate or benefit from acquisitions in a profitable manner;
- acquisition-related costs, liabilities, or tax impacts, some of which may be unanticipated;
- difficulty integrating the intellectual property, technology infrastructure, and operations of the acquired business;
- difficulty integrating and retaining the personnel of the acquired business;
- ineffective or inadequate controls, procedures, or policies at the acquired company;
- multiple product lines or services offerings, as a result of our acquisitions, that are offered, priced, and supported differently;
- difficulties and additional expenses associated with synchronizing product offerings, customer relationships, and contract portfolio terms and conditions between Workday and the acquired business;
- potential unknown liabilities or risks associated with the acquired businesses, including those arising from existing contractual obligations or litigation matters;
- adverse effects on our existing business relationships with business partners and customers as a result of the acquisition;
- inability to maintain relationships with key customers, suppliers, and partners of the acquired business;
- difficulty predicting and controlling the effect of integrating multiple acquisitions concurrently;
- lack of experience in new markets, products, or technologies;
- diversion of management's attention from other business concerns;
- use of resources that are needed in other parts of our business; and
- use of substantial portions of our available cash to consummate the acquisition.

In addition, a significant portion of the purchase price of companies we acquire may be allocated to acquired goodwill and other intangible assets, which must be assessed for impairment at least annually. In the future, if our acquisitions do not yield expected returns, we may be required to take charges to our operating results based on this impairment assessment process, which could adversely affect our results of operations.

Acquisitions could also result in dilutive issuances of equity securities or the issuance of debt, which could adversely affect our operating results. In addition, if an acquired business fails to meet our expectations, our operating results, business, and financial position may suffer.

In addition, from time to time we invest in private growth stage companies for strategic reasons and to support key business initiatives, and we may not realize a return on these investments. All of our venture investments are subject to a risk of partial or total loss of investment capital.

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We have a history of cumulative losses and we do not expect to be profitable on a GAAP basis for the foreseeable future.

We have incurred significant losses in each period since our inception in 2005. These losses and our accumulated deficit reflect the substantial investments we made to acquire new customers and develop our applications. We expect our operating expenses to increase in the future due to anticipated increases in sales and marketing expenses, product development expenses, operations costs, and general and administrative costs, and therefore we expect our losses on a GAAP basis to continue for the foreseeable future. Furthermore, to the extent we are successful in increasing our customer base, we will also incur increased losses in the acquisition period because costs associated with acquiring customers are generally incurred up front, while subscription services revenues are generally recognized ratably over the terms of the agreements, which are typically three years or longer. You should not consider our recent growth in revenues as indicative of our future performance. We cannot assure you that we will achieve GAAP profitability in the future, nor that, if we do become profitable, we will sustain profitability.

We may not receive significant revenues from our current development efforts for several years, if at all.

Developing software applications is expensive and the investment in product development often involves a long return on investment cycle. We have made and expect to continue to make significant investments in development and related opportunities. Accelerated application introductions and short application life cycles require high levels of expenditures that could adversely affect our operating results if not offset by revenue increases. We believe that we must continue to dedicate a significant amount of resources to our development efforts to maintain our competitive position. However, we may not receive significant revenues from these investments for several years, if at all.

If we experience significant fluctuations in our rate of anticipated growth and fail to balance our expenses with our revenue forecasts, our results could be harmed.

Our ability to forecast our future rate of growth is limited and subject to a number of uncertainties, including general economic and market conditions. We plan our expense levels and investment on estimates of future revenue and future anticipated rates of growth. We may not be able to adjust our spending quickly enough if our growth rates fall short of our expectations.

Moreover, we have encountered and will encounter risks and uncertainties frequently experienced by growing companies in rapidly changing industries, such as the risks and uncertainties described herein. If our assumptions regarding these risks and uncertainties (which we use to plan our business) are incorrect or change due to changes in our markets, or if we do not address these risks successfully, our operating and financial results could differ materially from our expectations and our business could suffer.

We may not be able to sustain our revenue growth rates in the future.

You should not consider our historical revenue growth rates as indicative of our future performance. Our revenue growth rates have declined, and may decline in future periods, as the size of our customer base increases and as we achieve higher market penetration rates. Other factors may also contribute to declines in our growth rates, including slowing demand for our services, increasing competition, a decrease in the growth of our overall market, our failure to continue to capitalize on growth opportunities, and the maturation of our business, among others. As our growth rates decline, investors’ perceptions of our business and the trading price of our securities could be adversely affected.

Our quarterly results may fluctuate significantly and may not fully reflect the underlying performance of our business.

Our quarterly results of operations, including the levels of our revenues, gross margin, operating margin, profitability, cash flow, unearned revenue, and remaining subscription revenue performance obligations, which we also refer to as backlog, may vary significantly in the future and period-to-period comparisons of our operating results may not be meaningful. Accordingly, the results of any one quarter should not be relied upon as an indication of future performance. Our quarterly financial results may fluctuate as a result of a variety of factors, many of which are outside of our control, and as a result, may not fully reflect the underlying performance of our business. Fluctuation in quarterly results may negatively impact the value of our securities. Factors that may cause fluctuations in our quarterly financial results include, without limitation, those listed below:

- our ability to attract new customers;
- the addition or loss of large customers, including through acquisitions or consolidations;
- customer renewal rates;

- the timing of operating expenses and recognition of revenues;
- the amount and timing of operating expenses related to the maintenance and expansion of our business, operations, and infrastructure;
- network outages or security breaches;
- general economic and market conditions;
- increases or decreases in the number of elements of our services or pricing changes upon any renewals of customer agreements;
- changes in our pricing policies or those of our competitors;

- the mix of applications sold during a period;
- seasonal variations in sales of our applications, which have historically been highest in our fiscal fourth quarter;
- the timing and success of new application and service introductions by us or our competitors;
- changes in the competitive dynamics of our industry, including consolidation among competitors, customers, or strategic partners;
- changes in laws and regulations that impact our business; and
- the timing of expenses related to acquisitions and potential future charges for impairment of goodwill.

Because we recognize subscription services revenues over the term of the contract, downturns or upturns in new sales will not be immediately reflected in our operating results and may be difficult to discern.

We generally recognize subscription services revenues from customers when control of the promised services is transferred, which typically occurs over a period of three years or longer. As a result, most of the subscription services revenues we report in each quarter are derived from the recognition of unearned revenue relating to subscriptions entered into during previous quarters. Consequently, a decline in new or renewed subscription contracts in any single quarter will likely have a minor impact on our revenue results for that quarter. However, such a decline will negatively affect our revenues in future quarters. Accordingly, the effect of significant downturns in sales and market acceptance of our applications, and potential changes in our pricing policies or rate of renewals may not be fully reflected in our results of operations until future periods. We may be unable to adjust our cost structure to reflect the changes in revenues. In addition, a majority of our costs are expensed as incurred, while revenues are recognized over the life of the customer agreement. As a result, increased growth in the number of our customers could result in our recognition of more costs than revenues in the earlier periods of the terms of our agreements. Our subscription model also makes it difficult for us to rapidly increase our revenues through additional sales in any period, as subscription revenues from new customers generally are recognized over the applicable subscription term.

Our ability to predict the rate of customer subscription renewals or adoptions, and the impact these renewals and adoptions will have on our revenues or operating results, is limited.

As the markets for our applications mature, or as new competitors introduce new products or services that compete with ours, we may be unable to attract new customers at the same price or based on the same pricing model as we have used historically. Moreover, large customers, which are the focus of our sales efforts, may demand greater price concessions. As a result, in the future we may be required to reduce our prices, which could adversely affect our revenues, gross margin, profitability, financial position, and cash flow.

In addition, our customers have no obligation to renew their subscriptions for our applications after the expiration of the initial subscription period. Our customers may renew for fewer elements of our applications or on different pricing terms. Our customers’ renewal rates may decline or fluctuate as a result of a number of factors, including their level of satisfaction with our pricing or our applications and their ability to continue their operations and spending levels. If our customers do not renew their subscriptions for our applications on similar pricing terms, our revenues may decline and our business could suffer. In addition, over time the average term of our contracts could change based on renewal rates or for other reasons.

Our future success also depends in part on our ability to sell additional products to our current customers. This may require increasingly costly sales efforts that are targeted at senior management. If these efforts are not successful, our business may suffer.

Failure to adequately expand and optimize our direct sales force will impede our growth.

We will need to continue to expand and optimize our sales infrastructure, both domestically and internationally, in order to grow our customer base and our business. Identifying and recruiting qualified personnel and training them in the use of our software requires significant time, expense and attention. It can take significant time before our sales representatives are fully trained and productive. Our business may be adversely affected if our efforts to expand and train our direct sales force do not generate a corresponding increase in revenues. In particular, if we are unable to hire, develop, and retain talented sales personnel or if new direct sales personnel are unable to achieve desired productivity levels in a reasonable period of time, we may not be able to realize the expected benefits of this investment or increase our revenues.

If we fail to develop widespread brand awareness cost-effectively, our business may suffer.

We believe that developing and maintaining widespread positive awareness of our brand is critical to achieving widespread acceptance of our applications, attracting new customers, and hiring and retaining employees. Brand promotion activities may not generate customer awareness or increase revenues, and even if they do, any increase in revenues may not offset the significant expenses we incur in building our brand. If we fail to successfully promote and maintain our brand, we may fail to attract or retain customers necessary to realize a sufficient return on our brand-building efforts, or to achieve the widespread brand awareness that is critical for broad customer adoption of our applications. In addition, if our brand is negatively impacted, it may be more difficult to hire and retain employees.

Our growth depends in part on the success of our strategic relationships with third parties.
In order to grow our business, we anticipate that we will continue to depend on relationships with third parties, such as deployment partners, technology and content providers, and other key suppliers. Identifying partners, and negotiating and documenting relationships with them, requires significant time and resources. Our competitors may be effective in providing incentives to third parties to favor their products or services or to prevent or reduce subscriptions to our services, or in negotiating better rates or terms with key suppliers. In addition, acquisitions of our partners by our competitors could result in a decrease in the number of our current and potential customers, as our partners may no longer facilitate the adoption of our applications by potential customers.
If we are unsuccessful in establishing or maintaining our relationships with third parties, our ability to compete in the marketplace or to grow our revenues could be impaired and our operating results may suffer. Even if we are successful, we cannot assure you that these relationships will result in increased customer usage of our applications or increased revenues.
Adverse economic conditions may negatively impact our business.
Our business depends on the overall demand for enterprise software and on the economic health of our current and prospective customers. Any significant weakening of the economy in the United States or Europe and of the global economy, more limited availability of credit, a reduction in business confidence and activity, decreased government spending, economic uncertainty and other difficulties, such as rising interest rates and increased inflation, may affect one or more of the sectors or countries in which we sell our applications. Alternatively, a strong dollar could reduce demand for our applications and services in countries with relatively weaker currencies.
The vote of the United Kingdom (“UK”) to leave the EU, known as Brexit, has created substantial economic and political uncertainty, the impact of which depends on the terms of the UK’s withdrawal from the EU, which may not be determined for several years or more. This uncertainty may cause some of our customers or potential customers to curtail spending and may ultimately result in new regulatory and cost challenges to our UK and global operations.
These adverse conditions could result in reductions in sales of our applications, longer sales cycles, reductions in subscription duration and value, slower adoption of new technologies, and increased price competition. Any of these events would likely have an adverse effect on our business, operating results, and financial position.
Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand.
Our success and ability to compete depend in part upon our intellectual property. We rely on patent, copyright, trade secret and trademark laws, trade secret protection, and confidentiality or license agreements with our employees, customers, partners, and others to protect our intellectual property rights. However, the steps we take to protect our intellectual property rights may be inadequate. While we have patent applications pending in the United States, we may be unable to obtain patent protection for the technology covered in our patent applications. In addition, any patents issued to us in the future may not provide us with competitive advantages or may be successfully challenged by third parties. Furthermore, legal standards relating to the validity, enforceability, and scope of protection of intellectual property rights are uncertain. Despite our precautions, it may be possible for unauthorized third parties to copy our applications and use information that we regard as proprietary to create products and services that compete with ours. Some license provisions protecting against unauthorized use, copying, transfer, and disclosure of our technology may be unenforceable under the laws of jurisdictions outside the United States. In addition, the laws of some countries do not protect proprietary rights to the same extent as the laws of the United States.
We enter into confidentiality and invention assignment agreements with our employees and consultants and enter into confidentiality agreements with the parties with whom we have strategic relationships and business alliances. No assurance can be given that these agreements will be effective in controlling access to and distribution of our applications and proprietary information. Further, these agreements do not prevent our competitors or partners from independently developing technologies that are substantially equivalent or superior to our applications.
We may be required to spend significant resources to monitor and protect our intellectual property rights. Litigation brought to protect and enforce our intellectual property rights could be costly, time-consuming, and distracting to management and could result in the impairment or loss of portions of our intellectual property. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims, and countersuits attacking

the validity and enforceability of our intellectual property rights. Our failure to secure, protect, and enforce our intellectual property rights could seriously adversely affect our brand and our business.

We may be sued by third parties for alleged infringement of their proprietary rights.

There is considerable patent and other intellectual property development activity in our industry. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our industry. From time to time, third parties may claim that we are infringing upon their intellectual property rights, and we may be found to be infringing upon such rights. In the future, they may claim that our applications and underlying technology infringe or violate their intellectual property rights, even if we are unaware of the intellectual property rights that others may claim cover some or all of our technology or services. Any claims or litigation could cause us to incur significant expenses and, if successfully asserted against us, could require that we pay substantial damages or ongoing royalty payments, prevent us from offering our services, or require that we comply with other unfavorable terms. We may also be obligated to indemnify our customers or business partners or pay substantial settlement costs, including royalty payments, in connection with any such claim or litigation and to obtain licenses, modify applications, or refund fees, which could be costly. Even if we were to prevail in such a dispute, any litigation regarding our intellectual property could be costly and time-consuming and divert the attention of our management and key personnel from our business operations.

Some of our applications utilize open source software, and any failure to comply with the terms of one or more of these open source licenses could negatively affect our business.

Some of our applications include software covered by open source licenses, which may include, by way of example, GNU General Public License and the Apache License. The terms of various open source licenses have not been interpreted by United States courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to market our applications. By the terms of certain open source licenses, we could be required to release the source code of our proprietary software, and to make our proprietary software available under open source licenses, if we combine our proprietary software with open source software in a certain manner. In the event that portions of our proprietary software are determined to be impacted by an open source license, we could be required to publicly release the affected portions of our source code, re-engineer all or a portion of our technologies, or otherwise be limited in the licensing of our technologies, each of which could reduce or eliminate the value of our technologies and services. In addition to risks related to license requirements, usage of open source software can lead to greater risks than use of third-party commercial software, as open source licensors generally do not provide warranties or controls on the origin of the software. Many of the risks associated with usage of open source software cannot be eliminated and could negatively affect our business.

We employ third-party licensed software for use in or with our applications, and the inability to maintain these licenses or errors in the software we license could result in increased costs, or reduced service levels, which would adversely affect our business.

Our applications incorporate certain third-party software obtained under licenses from other companies. We anticipate that we will continue to rely on such third-party software and development tools from third parties in the future. Although we believe that there are commercially reasonable alternatives to the third-party software we currently license, this may not always be the case, or it may be difficult or costly to replace. Our use of additional or alternative third-party software would require us to enter into license agreements with third parties. In addition, integration of the software used in our applications with new third-party software may require significant work and require substantial investment of our time and resources. To the extent that our applications depend upon the successful operation of third-party software in conjunction with our software, any undetected errors or defects in this third-party software could prevent the deployment or impair the functionality of our applications, delay new application introductions, result in a failure of our applications, and injure our reputation.

Changes in laws and regulations related to the Internet or changes in the Internet infrastructure itself may diminish the demand for our applications and could have a negative impact on our business.

Federal, state, or foreign government bodies or agencies have in the past adopted, and may in the future adopt, laws or regulations relating to Internet usage. Changes in these laws or regulations could require us to modify our applications in order to comply with these laws or regulations. In addition, government agencies or private organizations may begin to impose taxes, fees, or other charges for accessing the Internet or commerce conducted via the Internet. These laws or charges could limit the growth of Internet-related commerce or communications, or negatively impact demand for Internet-based applications such as ours.

In addition, businesses could be adversely affected due to delays in the development or adoption of new standards and protocols to handle increased demands of Internet activity, security, reliability, cost, ease of use, accessibility, and quality of service. Businesses have been adversely affected by “viruses,” “worms,” and similar malicious programs and have experienced a variety of outages and other delays as a result of damage to Internet infrastructure. These issues could negatively impact demand for our cloud-based applications.

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We may discover weaknesses in our internal controls over financial reporting, which may adversely affect investor confidence in the accuracy and completeness of our financial reports and consequently the market price of our securities.

As a public company, we are required to design and maintain proper and effective internal controls over financial reporting and to report any material weaknesses in such internal controls. Section 404 of the Sarbanes-Oxley Act of 2002 requires that we evaluate and determine the effectiveness of our internal controls over financial reporting and provide a management report on the internal controls over financial reporting, which must be attested to by our independent registered public accounting firm. If we have a material weakness in our internal controls over financial reporting, we may not detect errors on a timely basis and our financial statements may be materially misstated.

The process of compiling the system and processing documentation necessary to perform the evaluation needed to comply with Section 404 is challenging and costly. In the future, we may not be able to complete our evaluation, testing, and any required remediation in a timely fashion. If we identify material weaknesses in our internal controls over financial reporting, if we are unable to comply with the requirements of Section 404 in a timely manner, if we are unable to assert that our internal controls over financial reporting are effective, or if our independent registered public accounting firm is unable to express an opinion as to the effectiveness of our internal controls over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our securities could be negatively affected, and we could become subject to investigations by the Financial Industry Regulatory Authority, the SEC, or other regulatory authorities, which could require additional financial and management resources. In addition, because we use Workday’s financial management application, any problems that we experience with financial reporting and compliance could be negatively perceived by prospective or current customers, and negatively impact demand for our applications.

We may not be able to utilize a portion of our net operating loss or research tax credit carryforwards, which could adversely affect our profitability.

As of October 31, 2018, we had federal and state net operating loss carryforwards due to prior period losses, which if not utilized will begin to expire in fiscal 2027 and 2020 for federal and state purposes, respectively. We also have federal research tax credit carryforwards, which if not utilized will begin to expire in fiscal 2026. These net operating loss and research tax credit carryforwards could expire unused and be unavailable to reduce future income tax liabilities, which could adversely affect our profitability. In addition, under Section 382 of the Internal Revenue Code of 1986, as amended, our ability to utilize net operating loss carryforwards or other tax attributes, such as research tax credits, in any taxable year may be limited if we experience an “ownership change.” A Section 382 “ownership change” generally occurs if one or more stockholders or groups of stockholders who own at least 5% of our stock increase their ownership by more than 50 percentage points over their lowest ownership percentage within a rolling three-year period. Similar rules may apply under state tax laws. It is possible that an ownership change, or any future ownership change, could have a material effect on the use of our net operating loss carryforwards or other tax attributes, which could adversely affect our profitability.

Adverse tax laws or regulations could be enacted or existing laws could be applied to us or our customers, which could increase the costs of our services and adversely impact our business.

We operate and are subject to taxes in the United States and numerous other jurisdictions throughout the world. Changes to federal, state, local, or international tax laws on income, sales, use, indirect, or other tax laws, statutes, rules, regulations, or ordinances on multinational corporations are currently being considered by the United States and other countries where we do business. These contemplated legislative initiatives include, but are not limited to, changes to transfer pricing policies and definitional changes to permanent establishment that could be applied solely or disproportionately to services provided over the Internet. These contemplated tax initiatives, if finalized and adopted by countries, may ultimately impact our effective tax rate and could adversely affect our sales activity resulting in a negative impact on our operating results and cash flows.

In addition, existing tax laws, statutes, rules, regulations, or ordinances could be interpreted, changed, modified, or applied adversely to us (possibly with retroactive effect), which could require us to pay additional tax amounts, fines or penalties, and interest for past amounts. Existing tax laws, statutes, rules, regulations, or ordinances could also be interpreted, changed, modified, or applied adversely to our customers (possibly with retroactive effect), which could require our customers to pay additional tax amounts with respect to services we have provided, fines or penalties, and interest for past amounts. If we are unsuccessful in collecting such taxes from our customers, we could be held liable for such costs, thereby adversely impacting our operating results and cash flows. If our customers must pay additional fines or penalties, it could adversely affect demand for our services.

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The 2017 Tax Cuts and Jobs Act (the “Tax Act”) was enacted on December 22, 2017, and significantly affected U.S. tax law by changing how the U.S. imposes income tax on multinational corporations. The U.S. Department of Treasury has broad authority to issue regulations and interpretative guidance that may significantly impact how we will apply the law and impact our results of operations in the period issued. The Tax Act requires complex computations not previously provided in U.S. tax law. As such, the application of accounting guidance for such items is currently uncertain. Further, compliance with the Tax Act and the accounting for such provisions require accumulation of information not previously required or regularly produced. As additional regulatory guidance is issued by the applicable taxing authorities and as accounting treatment is clarified, we will perform additional analysis on the application of the law and refine estimates in calculating the effect, which may produce different results and will be reflected in the period the analysis is completed.

Our reported financial results may be adversely affected by changes in accounting principles generally accepted in the United States.

Generally accepted accounting principles in the United States are subject to interpretation by the Financial Accounting Standards Board, the SEC, and various bodies formed to promulgate and interpret appropriate accounting principles. A change in these principles or interpretations could have a significant effect on our reported financial results, and may even affect the reporting of transactions completed before the announcement or effectiveness of a change.

We have broad discretion in the use of our cash balances and may not use them effectively.

We have broad discretion in the use of our cash balances and may not use them effectively. The failure by our management to apply these funds effectively could adversely affect our business and financial condition. Pending their use, we may invest our cash balances in a manner that does not produce income or that loses value. Our investments may not yield a favorable return to our investors and may negatively impact the price of our securities.

Risks Related to Our Class A Common Stock

Our Chairman and CEO have control over key decision making as a result of their control of a majority of our voting stock.

As of October 31, 2018, our co-founder and Chairman David Duffield, together with his affiliates, held voting rights with respect to approximately 57 million shares of Class B common stock, 0.1 million shares of Class A common stock, and less than 0.1 million RSUs, which will be settled in an equivalent number of shares of Class A common stock. As of October 31, 2018, our co-founder and CEO Aneel Bhusri, together with his affiliates, held voting rights with respect to approximately 8 million shares of Class B common stock and 0.2 million shares of Class A common stock. In addition, Mr. Bhusri holds exercisable options to acquire approximately 2 million shares of Class B common stock and 0.2 million RSUs, which will be settled in an equivalent number of shares of Class A common stock. Further, Messrs. Duffield and Bhusri have entered into a voting agreement under which each has granted a voting proxy with respect to certain Class B common stock beneficially owned by him effective upon his death or incapacity as described in our registration statement on Form S-1 filed in connection with our IPO. Messrs. Duffield and Bhusri have each initially designated the other as their respective proxies. Accordingly, upon the death or incapacity of either Mr. Duffield or Mr. Bhusri, the other would individually continue to control the voting of shares subject to the voting proxy. Collectively, the shares described above represent a substantial majority of the voting power of our outstanding capital stock. As a result, Messrs. Duffield and Bhusri have the ability to control the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, consolidation, or sale of all or substantially all of our assets. In addition, they have the ability to control the management and affairs of our company as a result of their positions as our Chairman and CEO, respectively, and their ability to control the election of our directors. Mr. Duffield, in his capacity as a board member, and Mr. Bhusri, in his capacity as a board member and officer, each owe a fiduciary duty to our stockholders and must act in good faith in a manner they reasonably believe to be in the best interests of our stockholders. As stockholders, even as controlling stockholders, they are entitled to vote their shares in their own interests, which may not always be in the interests of our stockholders generally.

The dual class structure of our common stock has the effect of concentrating voting control with our Chairman and CEO, and also with other executive officers, directors, and affiliates; this will limit or preclude the ability of non-affiliates to influence corporate matters.

Our Class B common stock has 10 votes per share and our Class A common stock, which is the stock that is publicly traded, has one vote per share. Stockholders who hold shares of Class B common stock, including our executive officers, directors, and other affiliates, together hold a substantial majority of the voting power of our outstanding capital stock as of October 31, 2018. Because of the ten-to-one voting ratio between our Class B and Class A common stock, the holders of our Class B common stock collectively will continue to control a majority of the combined voting power of our common stock and therefore be able to control all matters submitted to our stockholders for approval until the conversion of all shares of all Class A and Class B shares to a single class of common stock on the date that is the first to occur of (i) October 11, 2032, (ii) such time as the shares of Class B common stock represent less than 9% of the outstanding Class A and Class B common stock, (iii) nine months following the death of both Mr. Duffield and Mr. Bhusri, or (iv) the date on which the holders of a majority of the shares of Class B common stock elect to convert all shares of Class A common stock and Class B common stock into a single class of common stock. This concentrated control will limit or preclude the ability of non-affiliates to influence corporate matters for the foreseeable future.

Future transfers by holders of Class B common stock will generally result in those shares converting to Class A common stock, subject to limited exceptions, such as certain transfers effected for estate planning purposes. The conversion of Class B common stock to Class A common stock will have the effect, over time, of increasing the relative voting power of those holders of Class B common stock who retain their shares in the long term. If, for example, our Chairman and CEO retain a significant portion of their holdings of Class B common stock for an extended period of time, they could, in the future, continue to control a majority of the combined voting power of our Class A common stock and Class B common stock.

Our stock price has been volatile in the past and may be subject to volatility in the future.

The trading price of our Class A common stock has been volatile historically and could be subject to wide fluctuations in response to various factors described below. These factors, as well as the volatility of our Class A common stock, could also impact the price of our convertible senior notes. The factors that may affect the trading price of our securities, some of which are beyond our control, include:

- overall performance of the equity markets;
- fluctuations in the valuation of companies perceived by investors to be comparable to us, such as high-growth or cloud companies, or in valuation metrics, such as our price to revenues ratio;
- guidance as to our operating results that we provide to the public, differences between our guidance and market expectations, our failure to meet our guidance, or changes in recommendations by securities analysts that follow our securities;
- announcements of technological innovations, new applications or enhancements to services, acquisitions, strategic alliances, or significant agreements by us or by our competitors;
- disruptions in our services due to computer hardware, software, or network problems;
- announcements of customer additions and customer cancellations or delays in customer purchases;
- recruitment or departure of key personnel;
- the economy as a whole, market conditions in our industry, and the industries of our customers;
- trading activity by directors, executive officers and significant stockholders, or the perception in the market that the holders of a large number of shares intend to sell their shares;
- the exercise of rights held by certain of our stockholders, subject to some conditions, to require us to file registration statements covering their shares or to include their shares in registration statements that we may file for ourselves or our stockholders;
- the size of our market float and significant option exercises;
- any future issuances of securities;
- sales and purchases of any Class A common stock issued upon conversion of our convertible senior notes or in connection with the convertible note hedge and warrant transactions related to such convertible senior notes;

- our operating performance and the performance of other similar companies; and
- the sale or availability for sale of a large number of shares of our Class A common stock in the public market.

Additionally, the stock markets have at times experienced extreme price and volume fluctuations that have affected and may in the future affect the market prices of equity securities of many companies. These fluctuations have, in some cases, been unrelated or disproportionate to the operating performance of these companies. Further, the trading prices of publicly traded shares of companies in our industry have been particularly volatile and may be very volatile in the future.

In the past, some companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could harm our business.

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We have indebtedness in the form of convertible senior notes.

In June 2013, we issued the 2020 Notes, and in September 2017, we issued the 2022 Notes. As a result of these convertible notes offerings, we incurred $250 million principal amount of indebtedness, which we may be required to pay at maturity in 2020, and $1.15 billion principal amount of indebtedness, which we may be required to pay at maturity in 2022, or upon the occurrence of a fundamental change (as defined in the applicable indenture). There can be no assurance that we will be able to repay this indebtedness when due, or that we will be able to refinance this indebtedness on acceptable terms or at all. In addition, this indebtedness could, among other things:

- make it difficult for us to pay other obligations;
- make it difficult to obtain favorable terms for any necessary future financing for working capital, capital expenditures, debt service requirements, or other purposes;
- require us to dedicate a substantial portion of our cash flow from operations to service and repay the indebtedness, reducing the amount of cash flow available for other purposes; and
- limit our flexibility in planning for and reacting to changes in our business.

Exercise of the warrants associated with the Notes may affect the price of our Class A common stock.

In connection with our offering of the 2018 Notes, we sold warrants to acquire up to approximately 4.2 million shares of our Class A common stock at an initial strike price of $107.96, which became exercisable beginning on October 15, 2018. In connection with our offering of the 2020 Notes, we sold warrants to acquire up to approximately 3.1 million shares of our Class A common stock at an initial strike price of $107.96, which become exercisable beginning on October 15, 2020. In connection with our offering of the 2022 Notes, we sold warrants to acquire up to approximately 7.8 million shares of our Class A common stock at an initial strike price of $213.96, which become exercisable beginning on January 1, 2023. The warrants may be settled in shares or in cash. The exercise of the warrants could have a dilutive effect if the market price per share of our Class A common stock exceeds the strike price of the warrants. The counterparties to the warrant transactions and note hedge transactions relating to the Notes are likely to enter into or unwind various derivative instruments with respect to our Class A common stock or purchase or sell shares of our Class A common stock or other securities linked to or referencing our Class A common stock in secondary market transactions prior to the respective maturity of the Notes. These activities could adversely affect the trading price of our Class A common stock.

Delaware law and provisions in our restated certificate of incorporation and restated bylaws could make a merger, tender offer, or proxy contest difficult, thereby depressing the market price of our Class A common stock.

Our status as a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay, or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change of control would be beneficial to our existing stockholders. In addition, our restated certificate of incorporation and restated bylaws contain provisions that may make the acquisition of our company more difficult, including the following:

- any transaction that would result in a change in control of our company requires the approval of a majority of our outstanding Class B common stock voting as a separate class;
- our dual class common stock structure, which provides our chairman and CEO with the ability to control the outcome of matters requiring stockholder approval, even if they own significantly less than a majority of the shares of our outstanding Class A and Class B common stock;
- our board of directors is classified into three classes of directors with staggered three-year terms and directors are only able to be removed from office for cause;
- when the outstanding shares of our Class B common stock represent less than a majority of the combined voting power of common stock:
- certain amendments to our restated certificate of incorporation or restated bylaws will require the approval of two-thirds of the combined vote of our then-outstanding shares of Class A and Class B common stock;
- our stockholders will only be able to take action at a meeting of stockholders and not by written consent; and
- vacancies on our board of directors will be able to be filled only by our board of directors and not by stockholders;
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only our chairman of the board, chief executive officer, either co-president, or a majority of our board of directors are authorized to call a special meeting of stockholders;

- certain litigation against us can only be brought in Delaware;

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- we will have two classes of common stock until the date that is the first to occur of (i) October 11, 2032, (ii) such time as the shares of Class B common stock represent less than 9% of the outstanding Class A and Class B common stock, (iii) nine months following the death of both Mr. Duffield and Mr. Bhusri, or (iv) the date on which the holders of a majority of the shares of Class B common stock elect to convert all shares of Class A common stock and Class B common stock into a single class of common stock;
- our restated certificate of incorporation authorizes undesignated preferred stock, the terms of which may be established, and shares of which may be issued, without the approval of the holders of Class A common stock; and
- advance notice procedures apply for stockholders to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders.

These anti-takeover defenses could discourage, delay, or prevent a transaction involving a change in control of our company. These provisions could also discourage proxy contests and make it more difficult for stockholders to elect directors of their choosing and to cause us to take other corporate actions they desire, any of which, under certain circumstances, could depress the market price of our securities.

If securities or industry analysts publish inaccurate or unfavorable research about our business, or discontinue publishing research about our business, the price and trading volume of our securities could decline.

The trading market for our securities will depend in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our Class A common stock or publish inaccurate or unfavorable research about our business, the price of our securities would likely decline. If one or more of these analysts cease coverage of us or fail to publish reports on us regularly, demand for our securities could decrease, which might cause the price and trading volume of our securities to decline.

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

We have never declared nor paid cash dividends on our capital stock. We currently intend to retain any future earnings to finance the operation and expansion of our business, and we do not expect to declare or pay any dividends in the foreseeable future. Consequently, stockholders must rely on sales of their common stock after price appreciation as the only way to realize any future gains on their investment.

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

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ITEM 6. EXHIBITS

The Exhibits listed below are filed as part of this Form 10-Q.

Exhibit Number		Incorporation by Reference Form	File No.	Filing Date	Exhibit No.	Filed Herewith
10.1†	2012 Employee Stock Purchase Plan					X
10.2	Adaptive Insights, Inc. 2013 Equity Incentive Plan	S-8	333-226907	August 17, 2018	99.1	
10.3	Forms of Award Agreements to the Adaptive Insights, Inc. 2013 Equity Incentive Plan	S-8	333-226907	August 17, 2018	99.2	
31.1	Certification of Principal Executive Officer Required Under Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended					X
31.2	Certification of Principal Financial Officer Required Under Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended					X
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101.INS	XBRL Instance Document					X
101.SCH	XBRL Taxonomy Schema Linkbase Document					X
101.CAL	XBRL Taxonomy Calculation Linkbase Document					X
101.DEF	XBRL Taxonomy Definition Linkbase Document					X
101.LAB	XBRL Taxonomy Labels Linkbase Document					X
101.PRE	XBRL Taxonomy Presentation Linkbase Document					X

† Indicates a management contract or compensatory plan.

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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.

Dated: December 3, 2018

Workday, Inc.

/s/ Robynne D. Sisco
Robynne D. Sisco
Co-President and Chief Financial Officer
(Principal Financial Officer)