
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2015

or

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

For the transition period from _____ to _____

Commission File Number: 001-35198

Pandora Media, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

**2101 Webster Street, Suite 1650
Oakland, CA**

(Address of principal executive offices)

94-3352630

(I.R.S. Employer
Identification No.)

94612

(Zip Code)

(510) 451-4100

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Non-accelerated filer

(Do not check if a smaller reporting company)

Accelerated filer

Smaller reporting company

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

The number of shares of registrant's common stock outstanding as of July 22, 2015 was: 212,280,921.

Pandora Media, Inc.
FORM 10-Q Quarterly Report
Table of Contents

| | <u>Page No.</u> |
|--|-----------------|
| <u>PART I. FINANCIAL INFORMATION</u> | |
| <u>Item 1.</u> <u>Financial Statements (unaudited)</u> | <u>3</u> |
| <u>Condensed Consolidated Balance Sheets as of December 31, 2014 and June 30, 2015</u> | <u>3</u> |
| <u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2014 and 2015</u> | <u>4</u> |
| <u>Condensed Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended June 30, 2014 and 2015</u> | <u>5</u> |
| <u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2014 and 2015</u> | <u>6</u> |
| <u>Notes to Condensed Consolidated Financial Statements</u> | <u>7</u> |
| <u>Item 2</u> <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>18</u> |
| <u>Item 3</u> <u>Quantitative and Qualitative Disclosures About Market Risk</u> | <u>33</u> |
| <u>Item 4</u> <u>Controls and Procedures</u> | <u>34</u> |
| <u>PART II. OTHER INFORMATION</u> | |
| <u>Item 1.</u> <u>Legal Proceedings</u> | <u>35</u> |
| <u>Item 1A.</u> <u>Risk Factors</u> | <u>35</u> |
| <u>Item 6.</u> <u>Exhibits</u> | <u>36</u> |
| <u>Signatures</u> | <u>37</u> |

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

Pandora Media, Inc.
Condensed Consolidated Balance Sheets
(in thousands, except share and per share amounts)
(unaudited)

| | <u>As of December 31,</u> <u>2014</u> | <u>As of June 30,</u> <u>2015</u> |
|---|--|--------------------------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 175,957 | \$ 204,103 |
| Short-term investments | 178,631 | 168,339 |
| Accounts receivable, net of allowance of \$1,218 at December 31, 2014 and \$1,579 at June 30, 2015 | 218,437 | 233,715 |
| Prepaid expenses and other current assets | 15,389 | 16,664 |
| Total current assets | <u>588,414</u> | <u>622,821</u> |
| Long-term investments | 104,243 | 89,013 |
| Property and equipment, net | 42,921 | 54,741 |
| Other long-term assets | 13,712 | 13,857 |
| Total assets | <u>\$ 749,290</u> | <u>\$ 780,432</u> |
| Liabilities and stockholders' equity | | |
| Current liabilities | | |
| Accounts payable | \$ 10,825 | \$ 16,386 |
| Accrued liabilities | 15,754 | 25,006 |
| Accrued royalties | 73,693 | 81,351 |
| Deferred revenue | 14,412 | 27,097 |
| Accrued compensation | 34,476 | 39,905 |
| Total current liabilities | <u>149,160</u> | <u>189,745</u> |
| Other long-term liabilities | 16,773 | 15,177 |
| Total liabilities | <u>165,933</u> | <u>204,922</u> |
| Stockholders' equity | | |
| Common stock: 209,071,488 shares issued and outstanding at December 31, 2014 and 212,251,439 at June 30, 2015 | 21 | 21 |
| Additional paid-in capital | 781,009 | 837,356 |
| Accumulated deficit | (196,997) | (261,319) |
| Accumulated other comprehensive loss | (676) | (548) |
| Total stockholders' equity | <u>583,357</u> | <u>575,510</u> |
| Total liabilities and stockholders' equity | <u>\$ 749,290</u> | <u>\$ 780,432</u> |

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

Pandora Media, Inc.
Condensed Consolidated Statements of Operations
(in thousands, except per share amounts)
(unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|--------------------------------|-------------|------------------------------|-------------|
| | 2014 | 2015 | 2014 | 2015 |
| Revenue | | | | |
| Advertising | \$ 177,324 | \$ 230,921 | \$ 317,958 | \$ 409,660 |
| Subscription and other | 41,570 | 54,639 | 95,251 | 106,664 |
| Total revenue | 218,894 | 285,560 | 413,209 | 516,324 |
| Cost of revenue | | | | |
| Cost of revenue - Content acquisition costs | 111,461 | 130,134 | 219,736 | 256,157 |
| Cost of revenue - Other | 13,989 | 20,043 | 28,968 | 36,276 |
| Total cost of revenue | 125,450 | 150,177 | 248,704 | 292,433 |
| Gross profit | 93,444 | 135,383 | 164,505 | 223,891 |
| Operating expenses | | | | |
| Product development | 13,076 | 18,742 | 24,907 | 34,617 |
| Sales and marketing | 66,232 | 94,035 | 128,096 | 178,309 |
| General and administrative | 25,865 | 38,812 | 52,226 | 75,566 |
| Total operating expenses | 105,173 | 151,589 | 205,229 | 288,492 |
| Loss from operations | (11,729) | (16,206) | (40,724) | (64,601) |
| Other income, net | 100 | 256 | 192 | 453 |
| Loss before provision for income taxes | (11,629) | (15,950) | (40,532) | (64,148) |
| Provision for income taxes | (99) | (115) | (127) | (174) |
| Net loss | \$ (11,728) | \$ (16,065) | \$ (40,659) | \$ (64,322) |
| Weighted-average common shares outstanding used in computing basic and diluted net loss per share | 205,706 | 211,742 | 202,798 | 210,840 |
| Net loss per share, basic and diluted | \$ (0.06) | \$ (0.08) | \$ (0.20) | \$ (0.31) |

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

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|--------------------|------------------------------|--------------------|
| | 2014 | 2015 | 2014 | 2015 |
| Net loss | \$ (11,728) | \$ (16,065) | \$ (40,659) | \$ (64,322) |
| Change in foreign currency translation adjustment | (2) | (48) | 16 | (147) |
| Change in net unrealized losses on marketable securities | 85 | (283) | 200 | 275 |
| Other comprehensive income (loss) | 83 | (331) | 216 | 128 |
| Total comprehensive loss | <u>\$ (11,645)</u> | <u>\$ (16,396)</u> | <u>\$ (40,443)</u> | <u>\$ (64,194)</u> |

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

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

| | Six months ended June 30, | |
|--|------------------------------|-------------------|
| | 2014 | 2015 |
| Operating activities | | |
| Net loss | \$ (40,659) | \$ (64,322) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities | | |
| Depreciation and amortization | 7,109 | 9,365 |
| Stock-based compensation | 38,005 | 50,679 |
| Amortization of premium on investments, net | 1,380 | 1,229 |
| Other operating activities | 446 | 944 |
| Changes in operating assets and liabilities | | |
| Accounts receivable | (13,542) | (16,123) |
| Prepaid expenses and other assets | (3,253) | (2,104) |
| Accounts payable and accrued liabilities | 1,095 | 10,363 |
| Accrued royalties | 6,145 | 7,697 |
| Accrued compensation | 10,748 | 5,897 |
| Deferred revenue | (19,887) | 12,685 |
| Reimbursement of cost of leasehold improvements | 3,161 | 749 |
| Net cash provided by (used in) operating activities | <u>(9,252)</u> | <u>17,059</u> |
| Investing activities | | |
| Purchases of property and equipment | (16,424) | (17,947) |
| Purchases of investments | (194,122) | (111,541) |
| Proceeds from maturities of investments | 116,831 | 132,119 |
| Proceeds from sale of investments | — | 3,662 |
| Payments related to acquisition | — | (200) |
| Net cash provided by (used in) investing activities | <u>(93,715)</u> | <u>6,093</u> |
| Financing activities | | |
| Proceeds from employee stock purchase plan | 2,482 | 3,275 |
| Proceeds from exercise of stock options | 12,562 | 2,862 |
| Tax payments from net share settlements of restricted stock units | — | (907) |
| Net cash provided by financing activities | <u>15,044</u> | <u>5,230</u> |
| Effect of exchange rate changes on cash and cash equivalents | 16 | (236) |
| Net increase (decrease) in cash and cash equivalents | (87,907) | 28,146 |
| Cash and cash equivalents at beginning of period | 245,755 | 175,957 |
| Cash and cash equivalents at end of period | <u>\$ 157,848</u> | <u>\$ 204,103</u> |
| Supplemental disclosures of cash flow information | | |
| Cash paid during the period for interest | \$ 246 | \$ 219 |
| Purchases of property and equipment recorded in accounts payable and accrued liabilities | \$ 3,337 | \$ 3,637 |

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

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

1. Description of Business and Basis of Presentation

Pandora Media, Inc. provides an internet radio service offering a personalized experience for each listener wherever and whenever they want to listen to radio on a wide range of smartphones, tablets, computers and car audio systems, as well as a range of other internet-connected devices. We have pioneered a new form of radio—one that uses intrinsic qualities of music to initially create stations and then adapts playlists in real-time based on the individual feedback of each listener. We generate a majority of our revenue by offering local and national advertisers an opportunity to deliver targeted messages to our listeners using a combination of audio, display and video advertisements. We also generate revenue by offering a paid subscription service which we call Pandora One. We were incorporated as a California corporation in January 2000 and reincorporated as a Delaware corporation in December 2010. Our principal operations are located in the United States; we also operate in Australia and New Zealand.

As used herein, “Pandora,” “we,” “our,” the “Company” and similar terms include Pandora Media, Inc. and its subsidiaries, unless the context indicates otherwise.

Basis of Presentation

The interim unaudited condensed consolidated financial statements and accompanying notes have been prepared in accordance with United States generally accepted accounting principles (“U.S. GAAP”) along with the instructions to Form 10-Q and Article 10 of Securities and Exchange Commission (“SEC”) Regulation S-X, and include the accounts of Pandora and our wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. In the opinion of our management, the interim unaudited condensed consolidated financial statements include all adjustments, which include only normal recurring adjustments, necessary for the fair presentation of our financial position for the periods presented. These interim unaudited condensed consolidated financial statements are not necessarily indicative of the results expected for the full fiscal year or for any subsequent period and should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2014.

Certain changes in presentation have been made to conform the prior period presentation to current period reporting. We have reclassified certain non-cash amounts from the amortization of debt issuance costs and the change in accounts receivable line items to the other operating activities line item in our condensed consolidated statements of cash flows. We have also reclassified certain non-cash amounts from the purchases of property and equipment line item to the prepaid expenses and other assets line item of our condensed consolidated statements of cash flows.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Estimates are used in several areas including, but not limited to determining accrued royalties, selling prices for elements sold in multiple-element arrangements, the allowance for doubtful accounts, the fair value of stock options, market stock units (“MSUs”) and the Employee Stock Purchase Plan (“ESPP”), the impact of forfeitures on stock-based compensation, the provision for (benefit from) income taxes and the subscription return reserve. To the extent there are material differences between these estimates, judgments, or assumptions and actual results, our financial statements could be affected. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. GAAP and does not require management’s judgment in its application. There are also areas in which management’s judgment in selecting among available alternatives would not produce a materially different result.

2. Summary of Significant Accounting Policies

Other than discussed below, there have been no material changes to our significant accounting policies as compared to those described in our Annual Report on Form 10-K for the year ended December 31, 2014.

Stock-Based Compensation — MSUs

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

We implemented a market stock unit program in March 2015 for certain key executives. Specifically, MSUs measure Pandora's total stockholder return ("TSR") performance against that of the Russell 2000 Index across three performance periods.

We have determined the grant-date fair value of the MSUs using a Monte Carlo simulation performed by a third-party valuation specialist. The Monte Carlo simulation model utilizes multiple input variables to estimate the probability that market conditions will be achieved. These variables include our expected stock price volatility over the expected term of the award, actual and projected employee stock option exercise behaviors and the risk-free interest rate for the expected term of the award. The variables used in these models are reviewed on an annual basis and adjusted, as needed. We recognize stock-based compensation for the MSUs over the requisite service period using the accelerated attribution method.

Concentration of Credit Risk

For the three and six months ended June 30, 2014 and 2015, we had no customers that accounted for more than 10% of our total revenue. As of December 31, 2014 and June 30, 2015, we had no customers that accounted for more than 10% of our total accounts receivable.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-9, *Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-9"). ASU 2014-9 outlines a single comprehensive model for entities to use in accounting for revenue. Under the guidance, revenue is recognized when a company transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The standard may be effective for public entities with annual and interim reporting periods beginning after December 15, 2017. Entities have the option of using either a full retrospective or a modified retrospective approach to adopt the guidance. We are currently evaluating implementation methods and the effect that implementation of this standard will have on our consolidated financial statements upon adoption.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, *Going Concern (Subtopic 205-40)* ("ASU 2014-15"). ASU 2014-15 requires management of all entities to evaluate whether there are conditions and events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the financial statements are issued (or available to be issued when applicable). The guidance is effective for fiscal years beginning after December 15, 2016 and for interim periods within that fiscal year. We do not expect the adoption of this guidance to have a material effect on our consolidated financial statements.

3. Cash, Cash Equivalents and Investments

Cash, cash equivalents and investments consisted of the following:

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

| | As of December 31, 2014 | As of June 30, 2015 |
|---|-------------------------------|---------------------------|
| (in thousands) | | |
| Cash and cash equivalents | | |
| Cash | \$ 72,487 | \$ 99,001 |
| Money market funds | 89,113 | 94,948 |
| Commercial paper | 9,349 | 7,749 |
| Corporate debt securities | 5,008 | 2,405 |
| Total cash and cash equivalents | \$ 175,957 | \$ 204,103 |
| Short-term investments | | |
| Commercial paper | \$ 45,443 | \$ 42,582 |
| Corporate debt securities | 128,691 | 123,255 |
| U.S. government and government agency debt securities | 4,497 | 2,502 |
| Total short-term investments | \$ 178,631 | \$ 168,339 |
| Long-term investments | | |
| Corporate debt securities | \$ 100,998 | \$ 89,013 |
| U.S. government and government agency debt securities | 3,245 | — |
| Total long-term investments | \$ 104,243 | \$ 89,013 |
| Cash, cash equivalents and investments | \$ 458,831 | \$ 461,455 |

Our short-term investments have maturities of twelve months or less and are classified as available-for-sale. Our long-term investments have maturities of greater than twelve months and are classified as available-for-sale.

The following tables summarize our available-for-sale securities' adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category as of December 31, 2014 and June 30, 2015.

| | As of December 31, 2014 | | | |
|---|-------------------------|---------------------|----------------------|---------------|
| | Adjusted Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| (in thousands) | | | | |
| Money market funds | \$ 89,113 | \$ — | \$ — | \$ 89,113 |
| Commercial paper | 54,792 | — | — | 54,792 |
| Corporate debt securities | 235,135 | 6 | (444) | 234,697 |
| U.S. government and government agency debt securities | 7,751 | — | (9) | 7,742 |
| Total cash equivalents and marketable securities | \$ 386,791 | \$ 6 | \$ (453) | \$ 386,344 |

| | As of June 30, 2015 | | | |
|---|---------------------|---------------------|----------------------|---------------|
| | Adjusted Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| (in thousands) | | | | |
| Money market funds | \$ 94,948 | \$ — | \$ — | \$ 94,948 |
| Commercial paper | 50,331 | — | — | 50,331 |
| Corporate debt securities | 214,847 | 35 | (209) | 214,673 |
| U.S. government and government agency debt securities | 2,500 | 2 | — | 2,502 |
| Total cash equivalents and marketable securities | \$ 362,626 | \$ 37 | \$ (209) | \$ 362,454 |

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

The following table presents available-for-sale investments by contractual maturity date as of December 31, 2014 and June 30, 2015.

| | As of December 31, 2014 | |
|--|-------------------------|-------------------|
| | Adjusted Cost | Fair Value |
| | (in thousands) | |
| Due in one year or less | \$ 282,206 | \$ 282,101 |
| Due after one year through three years | 104,585 | 104,243 |
| Total | \$ 386,791 | \$ 386,344 |

| | As of June 30, 2015 | |
|--|---------------------|-------------------|
| | Adjusted Cost | Fair Value |
| | (in thousands) | |
| Due in one year or less | \$ 273,501 | \$ 273,441 |
| Due after one year through three years | 89,125 | 89,013 |
| Total | \$ 362,626 | \$ 362,454 |

The following tables summarize our available-for-sale securities' fair value and gross unrealized losses aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position as of December 31, 2014 and June 30, 2015.

| | As of December 31, 2014 | | | | | |
|---|-------------------------|-------------------------|-------------------------|-------------------------|-------------------|-------------------------|
| | Twelve Months or Less | | More than Twelve Months | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in thousands) | | | | | |
| Money market funds | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — |
| Commercial paper | — | — | — | — | — | — |
| Corporate debt securities | 192,699 | (422) | 12,148 | (22) | 204,847 | (444) |
| U.S. government and government agency debt securities | 5,240 | (9) | — | — | 5,240 | (9) |
| Total | \$ 197,939 | \$ (431) | \$ 12,148 | \$ (22) | \$ 210,087 | \$ (453) |

| | As of June 30, 2015 | | | | | |
|---|-----------------------|-------------------------|-------------------------|-------------------------|-------------------|-------------------------|
| | Twelve Months or Less | | More than Twelve Months | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in thousands) | | | | | |
| Money market funds | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — |
| Commercial paper | — | — | — | — | — | — |
| Corporate debt securities | 135,552 | (188) | 19,738 | (21) | 155,290 | (209) |
| U.S. government and government agency debt securities | — | — | — | — | — | — |
| Total | \$ 135,552 | \$ (188) | \$ 19,738 | \$ (21) | \$ 155,290 | \$ (209) |

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

Our investment policy requires investments to be investment grade, primarily rated “A1” by Standard & Poor’s or “P1” by Moody’s or better for short-term investments and rated “A” by Standard & Poor’s or “A2” by Moody’s or better for long-term investments, with the objective of minimizing the potential risk of principal loss. In addition, the investment policy limits the amount of credit exposure to any one issuer.

The unrealized losses on our available-for-sale securities as of June 30, 2015 were primarily a result of unfavorable changes in interest rates subsequent to the initial purchase of these securities. As of June 30, 2015, we owned 121 securities that were in an unrealized loss position. We do not intend nor expect to need to sell these securities before recovering the associated unrealized losses. We expect to recover the full carrying value of these securities. As a result, no portion of the unrealized losses at June 30, 2015 is deemed to be other-than-temporary and the unrealized losses are not deemed to be credit losses. When evaluating the investments for other-than-temporary impairment, we review factors such as the length of time and extent to which fair value has been below cost basis, the financial condition of the issuer and any changes thereto, and our intent to sell, or whether it is more likely than not we will be required to sell, the investment before recovery of the investment’s amortized cost basis. During the three and six months ended June 30, 2015, we did not recognize any impairment charges. During the three and six months ended June 30, 2015, we had proceeds from the sale of available-for-sale securities of \$3.7 million. We did not recognize a realized gain or loss in connection with these sales.

4. Fair Value

We record cash equivalents and short-term investments at fair value. Fair value is an exit price, representing the amount that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Fair value measurements are required to be disclosed by level within the following fair value hierarchy:

Level 1 — Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 — Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument’s anticipated life.

Level 3 — Inputs lack observable market data to corroborate management’s estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

When determining fair value, whenever possible we use observable market data and rely on unobservable inputs only when observable market data is not available.

The fair value of these financial assets and liabilities was determined using the following inputs at December 31, 2014 and June 30, 2015:

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

| | As of December 31, 2014 | | |
|---|---|--|-------------------|
| | Fair Value Measurement Using | | |
| | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Total |
| | (in thousands) | | |
| Assets | | | |
| Money market funds | \$ 89,113 | \$ — | \$ 89,113 |
| Commercial paper | — | 54,792 | 54,792 |
| Corporate debt securities | — | 234,697 | 234,697 |
| U.S. government and government agency debt securities | — | 7,742 | 7,742 |
| Total assets measured at fair value | <u>\$ 89,113</u> | <u>\$ 297,231</u> | <u>\$ 386,344</u> |
| | As of June 30, 2015 | | |
| | Fair Value Measurement Using | | |
| | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Total |
| | (in thousands) | | |
| Assets | | | |
| Money market funds | \$ 94,948 | \$ — | \$ 94,948 |
| Commercial paper | — | 50,331 | 50,331 |
| Corporate debt securities | — | 214,673 | 214,673 |
| U.S. government and government agency debt securities | — | 2,502 | 2,502 |
| Total assets measured at fair value | <u>\$ 94,948</u> | <u>\$ 267,506</u> | <u>\$ 362,454</u> |

Our money market funds are classified as Level 1 within the fair value hierarchy because they are valued primarily using quoted market prices. Our other cash equivalents and short-term investments are classified as Level 2 within the fair value hierarchy because they are valued using professional pricing sources for identical or comparable instruments, rather than direct observations of quoted prices in active markets. As of December 31, 2014 and June 30, 2015, we held no Level 3 assets or liabilities.

5. Commitments and Contingencies

Legal Proceedings

We have been in the past, and continue to be, a party to rate-setting, privacy and patent infringement litigation which have consumed, and may continue to consume, financial and managerial resources. We are also from time to time subject to various other legal proceedings and claims arising in the ordinary course of our business. We record a liability when we believe that it is both probable that a loss has been incurred and the amount can be reasonably estimated. Our management periodically evaluates developments that could affect the amount, if any, of liability that we have previously accrued and make adjustments as appropriate. Determining both the likelihood and the estimated amount of a loss requires significant judgment, and management's judgment may be incorrect. We do not believe the ultimate resolution of any pending legal matters is likely to have a material adverse effect on our business, financial position, results of operations or cash flows.

Performing Rights Organization ("PRO") rate-setting litigation

On November 5, 2012, we filed a petition in the rate court in the U.S. District Court for the Southern District of New York established by the consent decree between the American Society of Composers, Authors and Publishers ("ASCAP") and the U.S. Department of Justice for the determination of reasonable license fees and terms for an ASCAP blanket license for the

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

period from January 1, 2011 through December 31, 2015. A trial to determine the royalty rate for this blanket license concluded in February 2014, and in March 2014, the court issued its opinion establishing a royalty rate of 1.85% of revenue before certain deductions. On April 14, 2014, ASCAP, Sony/ATV, EMI Music Publishing, and Universal Publishing Group filed notices of appeal of the district court's decision with the Second Circuit Court of Appeals. Oral arguments were held before the Second Circuit on March 19, 2015. On May 6, 2015 the Second Circuit upheld the district court's ruling. On June 3, 2015, ASCAP petitioned the Second Circuit for a rehearing. On June 26, 2015, that petition was denied.

On June 13, 2013, Broadcast Music, Inc. ("BMI") filed a petition in the rate court in the U.S. District Court for the Southern District of New York established by the consent decree between BMI and the U.S. Department of Justice for the determination of reasonable fees and terms for a BMI blanket license for the period from January 1, 2013 through December 31, 2016. The rate proceeding concluded on March 13, 2015, and in May 2015, the court issued its opinion establishing a royalty rate of 2.5% of revenue before certain deductions. The district court's opinion did not have a material impact on our consolidated statements of operations for the three and six months ended June 30, 2015. On June 26, 2015, we filed a notice of appeal of the court's decision with the Second Circuit Court of Appeals.

Pre-1972 copyright litigation

On April 17, 2014, UMG Recordings, Inc., Sony Music Entertainment, Capitol Records, LLC, Warner Music Group Corp. and ABKCO Music and Records, Inc. filed suit against Pandora Media Inc. in the Supreme Court of the State of New York. The complaint claims common law copyright infringement and unfair competition arising from allegations that Pandora owes royalties for the public performance of sound recordings recorded prior to February 15, 1972.

On October 2, 2014, Flo & Eddie Inc. filed suit against Pandora Media Inc. in the federal district court for the Central District of California. The complaint alleges misappropriation and conversion in connection with the public performance of sound recordings recorded prior to February 15, 1972. On December 19, 2014, Pandora filed a motion to strike the complaint pursuant to California's Anti-Strategic Lawsuit Against Public Participation ("Anti-SLAPP") statute. This motion was denied, and Pandora has appealed the ruling to the Ninth Circuit Court of Appeals. As a result, the district court litigation has been stayed pending the Ninth Circuit's review.

The outcome of any litigation is inherently uncertain. Based on our current knowledge we do not believe it is probable that the final outcome of the matters discussed above will, individually or in the aggregate, have a material adverse effect on our business, financial position, results of operations or cash flows; however, in light of the uncertainties involved in such matters, there can be no assurance that the outcome of each case or the costs of litigation, regardless of outcome, will not have a material adverse effect on our business. In particular, rate court proceedings could take years to complete, could be very costly and may result in current and past royalty rates that are materially less favorable than rates we currently pay or have paid in the past.

Indemnification Agreements, Guarantees and Contingencies

In the ordinary course of business, we are party to certain contractual agreements under which we may provide indemnifications of varying scope, terms and duration to customers, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of breach of such agreements, services to be provided by us or from intellectual property infringement claims made by third parties. In addition, we have entered into indemnification agreements with directors and certain officers and employees that will require us, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. Such indemnification provisions are accounted for in accordance with guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others. To date, we have not incurred, do not anticipate incurring and therefore have not accrued for, any costs related to such indemnification provisions.

While the outcome of these matters cannot be predicted with certainty, we do not believe that the outcome of any claims under indemnification arrangements will have a material adverse effect on our financial position, results of operations or cash flows.

6. Other Long-Term Assets

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

| | As of December 31, 2014 | As of June 30, 2015 |
|-------------------------------------|--|------------------------------------|
| (in thousands) | | |
| Other long-term assets | | |
| Intangible assets | \$ 6,939 | \$ 6,766 |
| Long-term security deposits | 4,947 | 5,370 |
| Other | 1,826 | 1,721 |
| Total other long-term assets | \$ 13,712 | \$ 13,857 |

Acquisition

In June 2013, we entered into an agreement to purchase the assets of KXMZ-FM for a total purchase price of \$0.6 million in cash, which is included in the other long-term assets line item of our condensed consolidated balance sheets. The Federal Communications Commission ("FCC") approved the transfer of the FCC licenses and the acquisition was completed in June 2015. We have accounted for this acquisition as a business combination in the three months ended June 30, 2015.

7. Debt Instruments

We are party to a \$60.0 million credit facility with a syndicate of financial institutions, which expires on September 12, 2018. As of June 30, 2015, we had no borrowings outstanding, \$1.1 million in letters of credit outstanding and \$58.9 million of available borrowing capacity under the credit facility. We are in compliance with all financial covenants associated with the credit facility as of June 30, 2015.

8. Stock-based Compensation Plans and Awards

ESPP

The ESPP allows eligible employees to purchase shares of our common stock through payroll deductions of up to 5% of their eligible compensation. The ESPP provides for six-month offering periods, commencing in February and August of each year.

The per-share fair value of shares to be granted under the ESPP is determined on the first day of the offering period using the Black-Scholes option pricing model using the following assumptions:

| | Three months ended June 30, | | Six months ended June 30, | |
|--------------------------|-----------------------------|-------|---------------------------|---------------|
| | 2014 | 2015 | 2014 | 2015 |
| Expected life (in years) | 0.5 | 0.5 | 0.5 | 0.5 |
| Risk-free interest rate | 0.08% | 0.07% | 0.08% | 0.05% - 0.07% |
| Expected volatility | 42% | 42% | 42% | 42% |
| Expected dividend yield | 0% | 0% | 0% | 0% |

During the three months ended June 30, 2014 and 2015, we withheld \$1.6 million and \$1.7 million in contributions from employees and recognized \$0.6 million and \$0.6 million of stock-based compensation expense related to the ESPP, respectively. During the six months ended June 30, 2014 and 2015, we withheld \$2.5 million and \$3.3 million in contributions from employees and recognized \$0.9 million and \$1.2 million of stock-based compensation expense related to the ESPP, respectively. In the three and six months ended June 30, 2015, 282,966 shares of common stock were issued under the ESPP. There were no shares of common stock issued under the ESPP in the three and six months ended June 30, 2014.

Employee Stock-Based Awards

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

Our 2011 Equity Incentive Plan (the “2011 Plan”) provides for the issuance of stock options, restricted stock units and other stock-based awards to our employees. The 2011 Plan is administered by the compensation committee of our board of directors.

Stock options

We measure stock-based compensation expenses for stock options at the grant date fair value of the award and recognize expenses on a straight-line basis over the requisite service period, which is generally the vesting period. We estimate the fair value of stock options using the Black-Scholes option-pricing model. During the three months ended June 30, 2014 and 2015, we recorded stock-based compensation expense from stock options of approximately \$3.7 million and \$2.4 million. During the six months ended June 30, 2014 and 2015, we recorded stock-based compensation expense from stock options of approximately \$7.2 million and \$5.2 million.

There were no options granted in the three months ended June 30, 2014 or during the three and six months ended June 30, 2015.

Restricted stock units (“RSUs”)

The fair value of the restricted stock units is expensed ratably over the vesting period. RSUs typically have an initial annual cliff vest and then vest quarterly thereafter over the service period, which is generally four years. During the three months ended June 30, 2014 and 2015, we recorded stock-based compensation expense from RSUs of approximately \$16.3 million and \$24.1 million. During the six months ended June 30, 2014 and 2015, we recorded stock-based compensation expense from RSUs of approximately \$29.9 million and \$43.7 million.

Market stock units

We implemented a market stock unit program in March 2015 for certain key executives. Specifically, MSUs measure Pandora’s TSR performance against that of the Russell 2000 Index across three performance periods. Pandora’s relative TSR is calculated using the average adjusted closing stock price of Pandora stock, and the Russell 2000 Index, for ninety calendar days prior to the beginning of each performance period and the last ninety calendar days of the performance period. The target MSUs are divided across three performance periods as follows:

- One-third of the target MSUs are eligible to be earned for a performance period that is the first calendar year of the MSU grant (the “One-Year Performance Period”);
- One-third of the target MSUs are eligible to be earned for a performance period that is the first two calendar years of the MSU grant (the “Two-Year Performance Period”); and
- Any remaining portion of the target MSUs are eligible to be earned for a performance period that is the entire three calendar years of the MSU grant (the “Three-Year Performance Period”).

For each performance period, a “performance multiplier” is calculated by comparing Pandora’s relative TSR for the period to the Russell 2000 Index TSR for the same period. The target number of shares will vest if the Pandora TSR is equal to the Russell 2000 Index TSR for the period. For each percentage point that the Pandora TSR falls below the Russell 2000 Index TSR for the period, the performance multiplier is decreased by three percentage points. The performance multiplier is capped at 100% for the One-Year and Two-Year Performance Periods. However, the full award is eligible for a payout up to 200% of target with all upside tied to the Three-Year Performance Period. For each percentage point that the Pandora TSR exceeds the Russell 2000 Index TSR for the Three-Year Performance Period, the performance multiplier is increased by 2%.

We have determined the grant-date fair value of the MSUs using a Monte Carlo simulation performed by a third-party valuation firm. We recognize stock-based compensation for the MSUs over the requisite service period, which is approximately three years, using the accelerated attribution method. During the three and six months ended June 30, 2015, we granted 776,000 MSUs at a total grant-date fair value of \$4.3 million. During the three and six months ended June 30, 2015, we recorded stock-based compensation expense from MSUs of approximately \$0.5 million and \$0.6 million.

Stock-based Compensation Expense

Stock-based compensation expense related to all employee and non-employee stock-based awards was as follows:

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|------------------|-------------------------------|------------------|
| | 2014 | 2015 | 2014 | 2015 |
| | (in thousands) (unaudited) | | (in thousands) (unaudited) | |
| Stock-based compensation expense | | | | |
| Cost of revenue - Other | \$ 1,032 | \$ 1,406 | \$ 1,913 | \$ 2,613 |
| Product development | 4,426 | 5,354 | 7,887 | 9,959 |
| Sales and marketing | 9,922 | 13,327 | 18,233 | 24,671 |
| General and administrative | 5,233 | 7,397 | 9,972 | 13,436 |
| Total stock-based compensation expense | <u>\$ 20,613</u> | <u>\$ 27,484</u> | <u>\$ 38,005</u> | <u>\$ 50,679</u> |

9. Net Loss Per Share

Basic net loss per share is computed by dividing the net loss by the weighted-average number of shares of common stock outstanding during the period.

Diluted net loss per share is computed by giving effect to all potential shares of common stock, including stock options, restricted stock units and market stock units, to the extent dilutive. Basic and diluted net loss per share were the same for the three and six months ended June 30, 2014 and 2015, as the inclusion of all potential common shares outstanding would have been anti-dilutive.

The following table sets forth the computation of historical basic and diluted net loss per share:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|--|------------------|--|------------------|
| | 2014 | 2015 | 2014 | 2015 |
| | (in thousands except per share amounts) | | (in thousands except per share amounts) | |
| Numerator | | | | |
| Net loss | \$ (11,728) | \$ (16,065) | \$ (40,659) | \$ (64,322) |
| Denominator | | | | |
| Weighted-average common shares outstanding used in computing basic and diluted net loss per share | 205,706 | 211,742 | 202,798 | 210,840 |
| Net loss per share, basic and diluted | <u>\$ (0.06)</u> | <u>\$ (0.08)</u> | <u>\$ (0.20)</u> | <u>\$ (0.31)</u> |

The following potential common shares outstanding were excluded from the computation of diluted net loss per share because including them would have been anti-dilutive:

| | As of June 30, | |
|----------------------------------|----------------|---------------|
| | 2014 | 2015 |
| | (in thousands) | |
| Options to purchase common stock | 12,647 | 10,478 |
| Restricted stock units | 11,797 | 16,189 |
| Market stock units | — | 776 |
| Total common stock equivalents | <u>24,444</u> | <u>27,443</u> |

Pandora Media, Inc.
Notes to Condensed Consolidated Financial Statements - Continued
(unaudited)

10. Subsequent Event

On July 1, 2015, we completed the acquisition of Next Big Sound, Inc. ("NBS"), a privately-held company that provides analytics for online music, including analyzing the popularity of musicians in social networks, streaming services and radio. We will include the financial results of NBS in our condensed consolidated financial statements as of the date of acquisition starting in the three months ended September 30, 2015.

On July 22, 2015, we amended the operating lease agreement for our office in New York, New York to increase both the leased space and the term of the lease, which previously required monthly lease payments through September 2024. This amendment is expected to result in an additional commitment of approximately \$37.8 million through 2025.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”)

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2014 filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

This Quarterly Report on Form 10-Q contains “forward-looking statements” that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Exchange Act, including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses, plans and objectives of management and economic, competitive and technological trends. In some cases, you can identify forward-looking statements by terms such as “anticipate,” “believe,” “estimate,” “expect,” “intend,” “may,” “might,” “plan,” “project,” “will,” “would,” “should,” “could,” “can,” “predict,” “potential,” “continue,” “objective,” or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled “Risk Factors” included in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2014. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements. We qualify all of our forward-looking statements by these cautionary statements. These and other factors could cause our results to differ materially from those expressed in this Quarterly Report on Form 10-Q.

Some of the industry and market data contained in this Quarterly Report on Form 10-Q are based on independent industry publications, including those generated by Triton Digital Media (“Triton”) or other publicly available information. This information involves a number of assumptions and limitations. Although we believe that each source is reliable as of its respective date, we have not independently verified the accuracy or completeness of this information.

As used herein, “Pandora,” the “Company,” “we,” “our,” and similar terms refer to Pandora Media, Inc., unless the context indicates otherwise.

“Pandora” and other trademarks of ours appearing in this report are our property. This report may contain additional trade names and trademarks of other companies. We do not intend our use or display of other companies’ trade names or trademarks to imply an endorsement or sponsorship of us by such companies, or any relationship with any of these companies.

Overview

Pandora is the leader in internet radio in the United States, offering a personalized experience for each of our listeners wherever and whenever they want to listen to radio on a wide range of smartphones, tablets, computers and car audio systems, as well as a range of other internet-connected devices. The majority of our listener hours occur on mobile devices, with the majority of our revenue generated from advertising on these devices. We have pioneered a new form of radio—one that uses intrinsic qualities of music to initially create stations and then adapts playlists in real-time based on the individual feedback of each listener. We offer local and national advertisers an opportunity to deliver targeted messages to our listeners using a combination of audio, display and video advertisements.

For the three months ended June 30, 2015, we streamed 5.30 billion hours of radio, and as of June 30, 2015, we had 79.4 million active users during the prior 30-day period. Since we launched our free, advertising-supported radio service in 2005 our listeners have created over 8 billion stations.

At the core of our service is our set of proprietary personalization technologies, including the Music Genome Project and our playlist generating algorithms. The Music Genome Project is a database of over 1,000,000 uniquely analyzed songs from over 200,000 artists, spanning over 600 genres and sub-genres, which we develop one song at a time by evaluating and cataloging each song’s particular attributes. When a listener enters a single song, artist, comedian or genre to start a station, the Pandora service instantly generates a station that plays music or comedy we think that listener will enjoy. Based on listener reactions to the recordings we pick, we further tailor the station to match the listener’s preferences. Listeners also have the ability to add variety to and rename stations, which further allows for the personalization of our service.

We currently provide the Pandora service through two models:

- *Free Service.* Our free service is advertising-based and allows listeners access to our music and comedy catalogs and personalized playlist generating system for free across all of our delivery platforms.
- *Pandora One.* Pandora One is a paid subscription service without any advertising. Pandora One also enables listeners to have more daily skips, enjoy higher quality audio on supported devices and enjoy longer timeout-free listening.

A key element of our strategy is to make the Pandora service available everywhere that there is internet connectivity. To this end, we make the Pandora service available through a variety of distribution channels. In addition to streaming our service to computers, we have developed Pandora mobile device applications (“apps”) for smartphones such as iPhone, Android and the Windows Phone and for tablets including the iPad and Android tablets. We distribute those mobile apps free to listeners via app stores. In addition, Pandora is now integrated with more than 1,000 connected devices, including automobiles, automotive aftermarket devices and consumer electronic devices.

Recent Events

In February 2015, we announced a United States licensing agreement to partner with Naxos of America, Inc. (“Naxos”), one of the world’s leading classical music labels representing a collection of classical music works. This partnership is designed to help classical labels and artists increase the audiences they reach. Participating labels and the artists they represent can also take advantage of the marketing capabilities of our connected platform, which capabilities include providing direct access to our metadata to help participating labels make data-driven business decisions. We do not expect this partnership to have a material effect on our financial condition or operating results.

In June 2013, we entered into an agreement to purchase the assets of KXMZ-FM for a total purchase price of \$0.6 million in cash, which is included in the other long-term assets line item of our condensed consolidated balance sheets. This acquisition was done in part to allow us to qualify for certain settlement agreements concerning royalties for the public performance of musical works between the Radio Music Licensing Committee (“RMLC”) and American Society of Composers, Authors and Publishers (“ASCAP”) and Broadcast Music, Inc. (“BMI”). The Federal Communications Commission (“FCC”) approved the transfer of the FCC licenses and the acquisition was completed in June 2015. We have accounted for this acquisition as a business combination in the three months ended June 30, 2015.

In June 2013, BMI filed a petition in the rate court in the U.S. District Court for the Southern District of New York established by the consent decree between BMI and the U.S. Department of Justice for the determination of reasonable fees and terms for a BMI blanket license for the period from January 1, 2013 through December 31, 2016. A trial to determine the royalty rates we will pay BMI concluded in March 2015, and in May 2015, the court issued its opinion establishing a royalty rate of 2.5% of revenue before certain deductions. The district court's opinion did not have a material impact on our consolidated statements of operations in the three and six months ended June 30, 2015. In June 2015, we filed a notice of appeal of the district court's decision with the Second Circuit Court of Appeals. We have been accruing at the RMLC royalty rate of 1.7% of revenue before certain deductions since June 2013, and continue to believe that it is the best estimate of the royalties that we owe for the period in question, rather than the alternative rate of 2.5% of revenue that the district court put forth in May 2015. If our appeal to the Second Circuit is not successful and we are not successful in enforcing our rights to pay the RMLC rate to which we are entitled by virtue of our acquisition of KXMZ, we will need to record royalties at the rate of 2.5% of revenue for the period beginning in June 2013, which would require a significant one-time adjustment to increase cost of revenue-content acquisition costs within our condensed consolidated financial statements. Please refer to our discussion of these matters in “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2014 for further information.

Factors Affecting our Business Model

A majority of our listener hours occur on mobile devices and as such, we face new challenges in optimizing our advertising products for delivery on mobile and other connected device platforms and monetizing inventory, or opportunities to sell advertisements, generated by listeners using these platforms. The mobile digital advertising industry is at an early stage of development, with lower overall spending levels than traditional online advertising markets, and faces technical challenges due to fragmented platforms and a lack of standard audience measurement protocols. As a greater share of our listener hours is consumed on mobile devices, our ability to monetize increased mobile streaming may not achieve the levels of monetization of streaming we have achieved on computers.

In addition, our monetization strategy includes increasing the number of ad campaigns for computer, mobile and other connected device platforms sold to local advertisers, placing us in more direct competition with broadcast radio for advertiser spending, especially for audio advertisements. By contrast, historically our advertisers have been predominantly national brands. To successfully monetize our growing listener hours, a key strategy is to convince a substantial base of local advertisers of the benefits of advertising on the Pandora service, including demonstrating the effectiveness and relevance of our advertising products, in particular audio advertising products, across the range of our delivery platforms.

Growth in our active users and distribution platforms has fueled a corresponding growth in listener hours. Our total number of listener hours is a key driver for both revenue generation opportunities and content acquisition costs, which are the largest component of our expenses.

- *Revenue.* Listener hours define the number of opportunities we have to sell advertisements, which we refer to as inventory. Our ability to attract advertisers depends in large part on our ability to offer sufficient inventory within desired demographics. In turn, our ability to generate revenue depends on the extent to which we are able to sell the inventory we have.
- *Cost of Revenue—Content Acquisition Costs.* The number of sound recordings we transmit to users of the Pandora service, as generally reflected by listener hours, drives substantially all of our content acquisition costs, although certain of our licensing agreements require us to pay fees for public performances of musical works based on a percentage of revenue.

We pay content acquisition costs, or royalties, to the copyright owners, or their agents, of each sound recording that we stream and to the copyright owners, or their agents, for the sound recordings that we perform, as well as the musical works embodied in each of those sound recordings, subject to certain exclusions. Royalties for sound recordings are negotiated with and paid to record labels, rights organizations or to SoundExchange, Inc. ("SoundExchange") and Merlin Networks B.V. ("Merlin"). Royalties for musical works are most often negotiated with and paid to performing rights organizations ("PROs") such as ASCAP, BMI and SESAC, Inc. ("SESAC") or directly to publishing companies. Royalties are calculated based on the number of sound recordings streamed, revenue earned or other usage measures.

We stream spoken word comedy content pursuant to a federal statutory license, for which the underlying literary works are not currently entitled to eligibility for licensing by any PRO for the United States. Rather, pursuant to industry-wide custom and practice, this content is performed absent a specific license from any such PRO or the copyright owner of such content. However, we pay royalties to SoundExchange at rates negotiated between representatives of online music services and SoundExchange for the right to stream this spoken word comedy content.

Given the current royalty structures in effect through the end of 2015 with respect to the public performance of sound recordings in the United States, our content acquisition costs increase with each additional listener hour, regardless of whether we are able to generate more revenue. As such, our ability to achieve and sustain profitability and operating leverage depends on our ability to increase our revenue per hour of streaming through increased advertising revenue across all of our delivery platforms. We are presently involved in proceedings to set the royalties we pay to SoundExchange for streaming performances of musical works for the period from 2016 through 2020. Depending on the outcome of those proceedings, our royalty costs could change significantly. Please refer to our discussion of these matters in "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2014 for further information.

We expect to invest heavily in our operations to support anticipated future growth. One of our key objectives is furthering our industry leadership in internet radio, which we believe will strengthen our brand and help us to convince advertisers to allocate spending towards our ad products. As such, a central focus is adding, retaining and engaging listeners to build market share and grow our listener hours. As our business matures, we expect that our revenue growth will exceed the growth in our listener hours. However, we expect to incur annual net losses on a U.S. GAAP basis in the near term because our current strategy is to leverage improvements in gross profit by investing in broadening distribution channels, developing innovative and scalable advertising products, increasing utilization of advertising inventory and building our sales force. These investments are intended to drive further growth in our business through both increased listener hours and monetization of those hours, and as a result we are targeting gradual improvements in gross profit over time. Our planned reinvestment of the resulting incremental gross profit will continue to depress the growth of our bottom line profitability.

Key Metrics

Listener Hours

We track listener hours because it is a key indicator of the growth of our business. We calculate listener hours based on the total bytes served for each track that is requested and served from our servers, as measured by our internal analytics systems, whether or not a listener listens to the entire track. To the extent that third-party measurements of listener hours are not calculated using a similar server-based approach, the third-party measurements may differ from our measurements.

The table below sets forth our total listener hours for the three and six months ended June 30, 2014 and 2015.

| | Three months ended June 30, | | Six months ended June 30, | |
|----------------|--------------------------------|------|------------------------------|-------|
| | 2014 | 2015 | 2014 | 2015 |
| | (in billions) | | (in billions) | |
| Listener hours | 5.04 | 5.30 | 9.84 | 10.60 |

Active Users

We track the number of active users as an additional indicator of the breadth of audience we are reaching at a given time. We define active users as the number of distinct registered users, including subscribers that have requested audio from our servers within the trailing 30 days to the end of the final calendar month of the period. The number of active users may overstate the number of unique individuals who actively use our service within a month as one individual may register for, and use, multiple accounts.

The table below sets forth our total active users as of June 30, 2014 and 2015.

| | As of June 30, | |
|--------------|----------------|------|
| | 2014 | 2015 |
| | (in millions) | |
| Active users | 76.4 | 79.4 |

We define advertising-based active users (“ad-based active users”) as the number of users, excluding subscribers, that have requested audio from our servers within the trailing 30 days to the end of the final calendar month of the period. We define subscribers as the number of distinct users at the end of the period that have subscribed to our service. Inactive subscribers are included as they contribute towards revenue per thousand listener hours (“RPMs”), which are described in further detail below.

The table below sets forth our users on an advertising and subscription basis as of June 30, 2014 and 2015.

| User type | As of June 30, | |
|-----------------------|---------------------|------|
| | 2014 | 2015 |
| | Users (in millions) | |
| Ad-based active users | 73.5 | 76.0 |
| Subscribers* | 3.4 | 3.9 |
| Total | 76.9 | 79.9 |

* Includes subscribers that have not used our service within the trailing 30 days to the end of the final calendar month of the period.

The table below sets forth our listener hours on an advertising and subscription basis for the three and six months ended June 30, 2014 and 2015.

| User type | Three months ended June 30, | | Six months ended June 30, | |
|-----------------------|--------------------------------|------|------------------------------|-------|
| | 2014 | 2015 | 2014 | 2015 |
| | Listener hours (in billions) | | Listener hours (in billions) | |
| Ad-based active users | 4.42 | 4.63 | 8.63 | 9.30 |
| Subscribers | 0.62 | 0.67 | 1.21 | 1.30 |
| Total | 5.04 | 5.30 | 9.84 | 10.60 |

Advertising Revenue per Thousand Listener Hours (“ad RPMs”)

We track ad RPMs for our free, advertising-supported service because it is a key indicator of our ability to monetize advertising inventory created by our listener hours. We focus on ad RPMs across all of our delivery platforms. We believe ad RPMs to be the central top-line indicator for evaluating the results of our monetization efforts. Ad RPMs are calculated by dividing advertising revenue by the number of thousands of listener hours of our advertising-based service.

Subscription and Other Revenue per Thousand Listener Hours (“subscription RPMs”)

We track subscription RPMs because it is a key indicator of the performance of our subscription service. We focus on subscription RPMs across all of our delivery platforms. Subscription RPMs are calculated by dividing subscription and other revenue by the number of thousands of listener hours of our subscription service.

Total Revenue per Thousand Listener Hours (“total RPMs”)

We track total RPMs for our service, which includes ad and subscription RPMs, because it is a key indicator of our ability to monetize our listener hours. Total RPMs compare advertising and subscription and other revenue in a given period to total listener hours in the period. We calculate total RPMs by dividing the total revenue by the number of thousands of listener hours.

Licensing Costs per Thousand Listener Hours (“LPMs”)

We track LPMs and analyze them in combination with our analysis of RPMs as they provide a key indicator of our profitability. LPMs are relatively fixed licensing costs with scheduled annual rate increases that drive period-over-period changes in LPMs. As such, the margin on our business varies principally with variances in ad RPMs and subscription RPMs.

Estimated RPMs and LPMs by Platform

We also provide estimates of disaggregated ad RPMs, subscription RPMs, total RPMs and related LPMs for our computer platform as well as our mobile and other connected devices platforms, which we calculate by dividing the estimated revenue and costs generated through the respective platforms by the number of thousands of listener hours of our services delivered through such platforms. While we believe that such disaggregated data provides directional insight for evaluating our efforts to monetize our service, we do not validate such disaggregated data to the level of financial statement reporting. Such data should be seen as indicative only and as management's best estimate.

Period-to-period results should not be regarded as precise nor can they be relied upon as indicative of results for future periods. In addition, as our business matures and in response to technological evolutions, we anticipate that the relevant indicators we monitor for evaluating our business may change.

The table below sets forth our RPMs and LPMs, including total, computer and mobile and other connected devices, on an ad, subscription and total basis for the three months ended June 30, 2014 and 2015.

| | Three months ended June 30, | | | | | | | |
|--|-----------------------------|-------|------|-------|------|-------|------|-------|
| | 2014 | | | | 2015 | | | |
| | RPM | | LPM* | | RPM | | LPM* | |
| Advertising | | | | | | | | |
| Computer | \$ | 62.43 | \$ | 20.51 | \$ | 74.35 | \$ | 20.70 |
| Mobile and other connected devices | | 36.00 | | 20.16 | | 46.15 | | 22.82 |
| Total advertising | \$ | 40.11 | \$ | 20.21 | \$ | 49.94 | \$ | 22.54 |
| Subscription | | | | | | | | |
| Computer | \$ | 54.75 | \$ | 33.12 | \$ | 69.53 | \$ | 36.61 |
| Mobile and other connected devices | | 71.06 | | 36.42 | | 84.13 | | 38.98 |
| Total subscription | \$ | 66.97 | \$ | 35.60 | \$ | 81.15 | \$ | 38.49 |
| Total | | | | | | | | |
| Total computer | \$ | 61.01 | \$ | 22.83 | \$ | 73.48 | \$ | 23.58 |
| Total mobile and other connected devices | | 39.88 | | 21.96 | | 50.63 | | 24.73 |
| Total | \$ | 43.41 | \$ | 22.10 | \$ | 53.91 | \$ | 24.57 |

*Under the Pureplay Settlement agreement, we pay per-performance rates for the streaming of sound recordings for our Pandora One subscription service that are higher than the per-performance rates for our free, advertising-supported service.

The table below sets forth our RPMs and LPMs, including total, computer and mobile and other connected devices, on an ad, subscription and total basis for the six months ended June 30, 2014 and 2015.

| | Six months ended June 30, | | | | | | | |
|--|---------------------------|-------|------|-------|------|-------|------|-------|
| | 2014 | | | | 2015 | | | |
| | RPM | | LPM* | | RPM | | LPM* | |
| Advertising | | | | | | | | |
| Computer | \$ | 57.50 | \$ | 20.84 | \$ | 65.82 | \$ | 20.16 |
| Mobile and other connected devices | | 32.84 | | 20.09 | | 40.54 | | 22.45 |
| Total advertising | \$ | 36.83 | \$ | 20.21 | \$ | 44.09 | \$ | 22.13 |
| Subscription | | | | | | | | |
| Computer | \$ | 58.36 | \$ | 33.54 | \$ | 69.84 | \$ | 36.51 |
| Mobile and other connected devices | | 86.14 | | 38.88 | | 84.81 | | 39.27 |
| Total subscription | \$ | 78.93 | \$ | 37.49 | \$ | 81.60 | \$ | 38.68 |
| Total | | | | | | | | |
| Total computer | \$ | 57.66 | \$ | 23.17 | \$ | 66.53 | \$ | 23.05 |
| Total mobile and other connected devices | | 38.70 | | 22.16 | | 45.58 | | 24.37 |
| Total | \$ | 42.00 | \$ | 22.30 | \$ | 48.72 | \$ | 24.17 |

*Under the Pureplay Settlement agreement, we pay per-performance rates for the streaming of sound recordings for our Pandora One subscription service that are higher than the per-performance rates for our free, advertising-supported service.

Total ad RPMs

For the three and six months ended June 30, 2015 compared to 2014, total ad RPMs increased primarily due to an increase in ad RPMs on the mobile and other connected devices platform. Ad RPMs on the mobile and other connected devices platform increased as advertising revenue growth outpaced the growth in advertising listener hours as a result of an increase in the average price per ad sold and an increase in the number of ads sold on that platform.

[Table of Contents](#)

Total subscription RPMs

For the three months ended June 30, 2015 compared to 2014, total subscription RPMs increased primarily due to an increase in subscription RPMs on the computer platform. Subscription RPMs on the computer platform increased as subscription revenue growth outpaced the growth in listener hours as a result of an increase in the average price per subscription and an increase in the number of subscribers.

For the six months ended June 30, 2015 compared to 2014, total subscription RPMs increased primarily due to an increase in subscription RPMs on the computer platform. Subscription RPMs on the computer platform increased as subscription revenue growth outpaced the growth in listener hours as a result of an increase in the average price per subscription and an increase in the number of subscribers. This was offset by a decrease in subscription RPMs on the mobile and other connected devices platform as a result of the one-time recognition of the accumulation of deferred revenue related to certain subscriptions purchased through mobile app stores of \$14.2 million in the three months ended March 31, 2014.

Total ad LPMs

For the three and six months ended June 30, 2015 compared to 2014, total ad LPMs increased primarily due to an increase in ad LPMs on the mobile and other connected devices platform. Ad LPMs on the mobile and other connected devices platform increased as a result of scheduled rate increases for sound recording royalties paid to SoundExchange.

Total subscription LPMs

For the three and six months ended June 30, 2015 compared to 2014, total subscription LPMs increased primarily due to an increase in subscription LPMs on the computer platform. Subscription LPMs on the computer platform increased primarily as a result of a decrease in computer subscription listener hours.

Basis of Presentation and Results of Operations

The following table presents our results of operations for the periods indicated as a percentage of total revenue. The period-to-period comparisons of results are not necessarily indicative of results for future periods.

| | Three months ended June 30, | | Six months ended June 30, | |
|---|--------------------------------|------|------------------------------|-------|
| | 2014 | 2015 | 2014 | 2015 |
| Revenue | | | | |
| Advertising | 81 % | 81 % | 77 % | 79 % |
| Subscription and other | 19 | 19 | 23 | 21 |
| Total revenue (2) | 100 | 100 | 100 | 100 |
| Cost of revenue | | | | |
| Cost of revenue — Content acquisition costs | 51 | 46 | 53 | 50 |
| Cost of revenue — Other(1) | 6 | 7 | 7 | 7 |
| Total cost of revenue (2) | 57 | 53 | 60 | 57 |
| Gross profit (2) | 43 | 47 | 40 | 43 |
| Operating expenses | | | | |
| Product development(1) | 6 | 7 | 6 | 7 |
| Sales and marketing(1) | 30 | 33 | 31 | 35 |
| General and administrative(1) | 12 | 14 | 13 | 15 |
| Total operating expenses (2) | 48 | 53 | 50 | 56 |
| Loss from operations (2) | (5) | (6) | (10) | (13) |
| Other income, net | — | — | — | — |
| Loss before provision for income taxes (2) | (5) | (6) | (10) | (12) |
| Provision for income taxes | — | — | — | — |
| Net Loss (2) | (5)% | (6)% | (10)% | (12)% |

[Table of Contents](#)

| (1) Includes stock-based compensation as follows: | | | | |
|---|------|------|------|------|
| Cost of revenue - Other | 0.5% | 0.5% | 0.5% | 0.5% |
| Product development | 2.0 | 1.9 | 1.9 | 1.9 |
| Sales and marketing | 4.5 | 4.7 | 4.4 | 4.8 |
| General and administrative | 2.4 | 2.6 | 2.4 | 2.6 |

(2) Note: Amounts may not recalculate due to rounding

Revenue

| | Three months ended June 30, | | | Six months ended June 30, | | |
|------------------------|--------------------------------|------------|-----------|------------------------------|------------|------------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Revenue | | | | | | |
| Advertising | \$ 177,324 | \$ 230,921 | \$ 53,597 | \$ 317,958 | \$ 409,660 | \$ 91,702 |
| Subscription and other | 41,570 | 54,639 | 13,069 | 95,251 | 106,664 | 11,413 |
| Total revenue | \$ 218,894 | \$ 285,560 | \$ 66,666 | \$ 413,209 | \$ 516,324 | \$ 103,115 |

Advertising revenue

We generate advertising revenue primarily from audio, display and video advertising, which is typically sold on a cost-per-thousand impressions, or CPM, basis. Advertising campaigns typically range from one to twelve months, and advertisers generally pay us based on the number of delivered impressions or the satisfaction of other criteria, such as click-throughs. We also have arrangements with advertising agencies under which these agencies sell advertising inventory on our service directly to advertisers. We report revenue under these arrangements net of amounts due to agencies. For the three months ended June 30, 2014 and 2015 and the six months ended June 30, 2014 and 2015, advertising revenue accounted for 81%, 81%, 77% and 79%, of our total revenue, respectively. We expect that advertising will comprise a substantial majority of our revenue for the foreseeable future.

For the three months ended June 30, 2015 compared to 2014, advertising revenue increased \$53.6 million or 30%, primarily due to an approximate 20% increase in the average price per ad due in part to our increase in relative volume of local ad sales and our focus on monetizing mobile inventory and an approximate 10% increase in the number of ads sold as a result of an increase in advertising listener hours.

For the six months ended June 30, 2015 compared to 2014, advertising revenue increased \$91.7 million or 29%, primarily due to an approximate 15% increase in the average price per ad due in part to our increase in relative volume of local ad sales and our focus on monetizing mobile inventory and an approximate 10% increase in the number of ads sold as a result of an increase in advertising listener hours.

Subscription and other revenue

Subscription and other revenue is generated primarily through the sale of Pandora One, a premium version of the Pandora service, which currently includes advertisement-free access and higher audio quality on the devices that support it. Subscription revenue is recognized on a straight-line basis over the duration of the subscription period. For the three months ended June 30, 2014 and 2015 and the six months ended June 30, 2014 and 2015, subscription and other revenue accounted for 19%, 19%, 23% and 21% of our total revenue, respectively.

For the three months ended June 30, 2015 compared to 2014, subscription revenue increased \$13.1 million or 31%, primarily due to an approximate 15% increase in average price per subscription and an approximate 15% increase in the number of subscribers.

[Table of Contents](#)

For the six months ended June 30, 2015 compared to 2014, subscription revenue increased \$11.4 million or 12%, primarily due to an approximate 15% increase in the average price per subscription and an approximate 15% increase in the number of subscribers. This was offset by a decrease in subscription revenue as a result of the one-time recognition of the accumulation of deferred revenue related to certain subscriptions purchased through mobile app stores of \$14.2 million in the three months ended March 31, 2014.

Deferred revenue

Our deferred revenue consists principally of both prepaid but unrecognized subscription revenue and advertising fees received or billed in advance of the delivery or completion of the delivery of services. Deferred revenue is recognized as revenue when the services are provided and all other revenue recognition criteria have been met.

In addition, subscription revenue derived from sales through certain mobile devices may be subject to refund or cancellation terms which may affect the timing or amount of the subscription revenue recognition. When refund rights exist, we recognize revenue when services have been provided and the rights lapse or when we have developed sufficient transaction history to estimate a return reserve.

Costs and Expenses

Cost of revenue consists of cost of revenue—content acquisition costs and cost of revenue—other. Our operating expenses consist of product development, sales and marketing and general and administrative costs. Cost of revenue—content acquisition costs are the most significant component of our costs and expenses, followed by employee-related costs, which include stock-based compensation expenses. We expect to continue to hire additional employees in order to support our anticipated growth and our product development initiatives. In any particular period, the timing of additional hires could materially affect our cost of revenue and operating expenses, both in absolute dollars and as a percentage of revenue. We anticipate that our costs and expenses will increase in the future.

Cost of revenue - Content acquisition costs

| | Three months ended June 30, | | | Six months ended June 30, | | |
|---|--------------------------------|------------|-----------|------------------------------|------------|-----------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Cost of revenue - Content acquisition costs | \$ 111,461 | \$ 130,134 | \$ 18,673 | \$ 219,736 | \$ 256,157 | \$ 36,421 |

Content acquisition costs as a percentage of advertising revenue by platform

| | Three months ended June 30, | | Six months ended June 30, | |
|------------------------------------|--------------------------------|------|------------------------------|------|
| | 2014 | 2015 | 2014 | 2015 |
| Computer | 34% | 32% | 37% | 35% |
| Mobile and other connected devices | 56% | 49% | 61% | 55% |

Cost of revenue—content acquisition costs principally consist of royalties paid for streaming music or other content to our listeners. Royalties are currently calculated using negotiated rates documented in agreements. The majority of our royalties are payable based on a fee per public performance of a sound recording, while in other cases our royalties are payable based on a percentage of our revenue or a formula that involves a combination of per performance and revenue metrics. For royalty arrangements under negotiation, we accrue for estimated royalties based on the available facts and circumstances and adjust these estimates as more information becomes available. The results of any finalized negotiation may be materially different from our estimates.

We estimate our advertising-based content acquisition costs attributable to specific platforms by allocating costs from royalties payable based on a fee per track to the platform for which the track is served and by allocating costs from royalties based on a percentage of our revenue in accordance with the overall percentage of our revenue estimated to be attributable to such platforms. While we believe that comparing disaggregated content acquisition costs and revenues across our delivery platforms may provide directional insight for evaluating our efforts to monetize the rapid adoption of our service on mobile and other connected devices, we do not validate such disaggregated metrics to the level of financial statement reporting. We

[Table of Contents](#)

continue to refine our systems and methodologies used to categorize such metrics across our delivery platforms and the period-to-period comparisons of results are not necessarily indicative of results for future periods.

For the three months ended June 30, 2015 compared to 2014, content acquisition costs increased \$18.7 million or 17%, primarily due to scheduled royalty rate increases of 8% and an approximate 5% increase in listener hours. Content acquisition costs as a percentage of total revenue decreased from 51% to 46%, primarily due to an increase in advertising sales, partially offset by scheduled royalty rate increases. Estimated content acquisition costs as a percentage of the advertising revenue attributable to our computer platform decreased from 34% to 32%, primarily due to increases in advertising sales on that platform that outpaced the growth in advertising content acquisition costs on that platform as a result of an increase in the average price per ad, partially offset by scheduled royalty rate increases. Estimated content acquisition costs as a percentage of the advertising revenue attributable to our mobile and other connected devices platforms decreased from 56% to 49%, primarily due to an increase in advertising sales on those platforms that outpaced the growth in advertising content acquisition costs on those platforms as a result of an increase in the average price per ad, partially offset by scheduled royalty rate increases.

For the six months ended June 30, 2015 compared to 2014, content acquisition costs increased \$36.4 million or 17%, primarily due to an approximate 10% increase in listener hours and scheduled royalty rate increases of 8%. Content acquisition costs as a percentage of total revenue decreased from 53% to 50%, primarily due to an increase in advertising sales, partially offset by scheduled royalty rate increases. Estimated content acquisition costs as a percentage of the advertising revenue attributable to our computer platform decreased from 37% to 35%, primarily due to increases in advertising sales on that platform that outpaced the growth in advertising content acquisition costs on that platform as a result of an increase in the average price per ad, partially offset by scheduled royalty rate increases. Estimated content acquisition costs as a percentage of the advertising revenue attributable to our mobile and other connected devices platform decreased from 61% to 55%, primarily due to an increase in advertising sales on those platforms that outpaced the growth in advertising content acquisition costs on those platforms as a result of an increase in the average price per ad, partially offset by scheduled royalty rate increases.

Cost of revenue—Other

| | Three months ended June 30, | | | Six months ended June 30, | | |
|-------------------------|--------------------------------|-----------|-----------|------------------------------|-----------|-----------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Cost of revenue — Other | \$ 13,989 | \$ 20,043 | \$ 6,054 | \$ 28,968 | \$ 36,276 | \$ 7,308 |

Cost of revenue—other consists primarily of hosting and ad serving costs, employee-related costs and other costs of ad sales. Hosting and ad serving costs consist of content streaming, maintaining our internet radio service and creating and serving advertisements through third-party ad servers. We make payments to third-party ad servers for the period the advertising impressions are delivered or click-through actions occur, and accordingly, we record this as a cost of revenue in the related period. Employee-related costs include salaries and benefits associated with supporting hosting and ad serving functions. Other costs of ad sales include costs related to music events that are sold as part of advertising arrangements.

For the three months ended June 30, 2015 compared to 2014, cost of revenue—other increased \$6.1 million or 43%, primarily due to a \$2.6 million increase in hosting and ad serving costs driven by an increase in listener hours, a \$1.6 million increase in employee-related costs driven by an approximate 35% increase in headcount and a \$1.3 million increase in costs related to music events that are sold as part of advertising arrangements.

For the six months ended June 30, 2015 compared to 2014, cost of revenue—other increased \$7.3 million or 25%, primarily due to a \$4.2 million increase in hosting and ad serving costs driven by an increase in listener hours and a \$2.9 million increase in employee-related costs driven by an approximate 35% increase in headcount.

Gross profit

| | Three months ended June 30, | | | Six months ended June 30, | | |
|-----------------------|--------------------------------|------------|-----------|------------------------------|------------|------------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Gross profit | | | | | | |
| Total revenue | \$ 218,894 | \$ 285,560 | \$ 66,666 | \$ 413,209 | \$ 516,324 | \$ 103,115 |
| Total cost of revenue | 125,450 | 150,177 | 24,727 | 248,704 | 292,433 | 43,729 |
| Gross profit | \$ 93,444 | \$ 135,383 | \$ 41,939 | \$ 164,505 | \$ 223,891 | \$ 59,386 |
| Gross margin | 43% | 47% | | 40% | 43% | |

For the three months ended June 30, 2015 compared to 2014, gross profit increased by \$41.9 million or 45% and gross margin increased from 43% to 47% as the growth in revenue outpaced the growth in content acquisition costs, primarily due to an increase in advertising revenue as a result of an increase in the average price per ad and an increase in the number of ads sold.

For the six months ended June 30, 2015 compared to 2014, gross profit increased by \$59.4 million or 36% and gross margin increased from 40% to 43% as the growth in revenue outpaced the growth in content acquisition costs, primarily due to an increase in advertising revenue as a result of an increase in the average price per ad and an increase in the number of ads sold.

Product development

| | Three months ended June 30, | | | Six months ended June 30, | | |
|---------------------|--------------------------------|-----------|-----------|------------------------------|-----------|-----------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Product development | \$ 13,076 | \$ 18,742 | \$ 5,666 | \$ 24,907 | \$ 34,617 | \$ 9,710 |

Product development consists primarily of employee-related costs, including salaries and benefits related to employees in software engineering, music analysis and product management departments, facilities and equipment expenses, information technology and costs associated with supporting consumer connected-device manufacturers in implementing our service in their products. We incur product development expenses primarily for improvements to our website and the Pandora app, development of new advertising products and development and enhancement of our personalized station generating system. We have generally expensed product development as incurred. Certain website development and internal use software development costs are capitalized when specific criteria are met. In such cases, the capitalized amounts are amortized over the useful life of the related application once the application is placed in service. We intend to continue making significant investments in developing new products and enhancing the functionality of our existing products.

For the three months ended June 30, 2015 compared to 2014, product development expenses increased \$5.7 million or 43%, primarily due to a \$5.1 million increase in employee-related costs driven by an approximate 45% increase in headcount.

For the six months ended June 30, 2015 compared to 2014, product development expenses increased \$9.7 million or 39%, primarily due to a \$9.0 million increase in employee-related costs driven by an approximate 45% increase in headcount.

Sales and marketing

| | Three months ended June 30, | | | Six months ended June 30, | | |
|---------------------|--------------------------------|-----------|-----------|------------------------------|------------|-----------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| Sales and marketing | \$ 66,232 | \$ 94,035 | \$ 27,803 | \$ 128,096 | \$ 178,309 | \$ 50,213 |

Sales and marketing consists primarily of employee-related costs, including salaries, commissions and benefits related to employees in sales, sales support, marketing and music industry group departments. In addition, sales and marketing expenses include transaction processing commissions on subscription purchases through mobile app stores, external sales and marketing

[Table of Contents](#)

expenses such as brand marketing, direct response and search engine marketing costs, public relations expenses, costs related to music events, agency platform and media measurement expenses, facilities and equipment expenses and infrastructure costs. We expect sales and marketing expenses to increase as we hire additional personnel to build out our sales and sales support teams, particularly as we continue to build out our local market sales team. While we have historically relied on the success of viral marketing to expand consumer awareness of our service, in 2014 we began to launch marketing campaigns to increase consumer awareness and expand our listener base. We anticipate that we will continue to utilize these types of marketing campaigns in the future.

For the three months ended June 30, 2015 compared to 2014, sales and marketing expenses increased \$27.8 million or 42%, primarily due to a \$12.9 million increase in employee-related costs and a \$1.9 million increase in facilities and equipment expense, both of which were driven by an approximate 30% increase in headcount, a \$7.5 million increase in brand marketing, direct response and search engine marketing costs and a \$3.2 million increase in transaction processing commissions on subscription purchases through mobile app stores.

For the six months ended June 30, 2015 compared to 2014, sales and marketing expenses increased \$50.2 million or 39%, primarily due to a \$24.9 million increase in employee-related costs and a \$2.2 million increase in facilities and equipment expense, both of which were driven by an approximate 30% increase in headcount, a \$13.1 million increase in brand marketing, direct response and search engine marketing costs, a \$6.2 million increase in transaction processing commissions on subscription purchases through mobile app stores and a \$2.1 million increase in costs related to music events.

General and administrative

| | Three months ended June 30, | | | Six months ended June 30, | | |
|----------------------------|--------------------------------|-----------|-----------|------------------------------|-----------|-----------|
| | 2014 | 2015 | \$ Change | 2014 | 2015 | \$ Change |
| | (in thousands) | | | (in thousands) | | |
| General and administrative | \$ 25,865 | \$ 38,812 | \$ 12,947 | \$ 52,226 | \$ 75,566 | \$ 23,340 |

General and administrative consists primarily of employee-related costs, including salaries and benefits for finance, accounting, legal, internal information technology and other administrative personnel. In addition, general and administrative expenses include professional services costs for outside legal and accounting services, facilities and equipment expenses, infrastructure costs and credit card fees. We expect general and administrative expenses to increase in future periods as we continue to invest in corporate infrastructure, including adding personnel and systems to our administrative functions.

For the three months ended June 30, 2015 compared to 2014, general and administrative expenses increased \$12.9 million or 50%, primarily due to a \$5.7 million increase in professional service costs related to royalty-related legal matters and a \$5.1 million increase in employee-related costs driven by an approximate 25% increase in headcount.

For the six months ended June 30, 2015 compared to 2014, general and administrative expenses increased \$23.3 million or 45%, primarily due to a \$9.7 million increase in professional service costs related to royalty-related legal matters, a \$8.9 million increase in employee-related costs and a \$1.6 million increase in facilities and equipment expense, both of which were driven by an approximate 25% increase in headcount, and a \$1.3 million increase in credit card fees.

Provision for (benefit from) income taxes

We have historically been subject to income taxes only in the United States. As we expand our operations outside the United States, we become subject to taxation based on the foreign statutory rates and our effective tax rate could fluctuate accordingly.

Our provision for (benefit from) income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted statutory income tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce net deferred tax assets to the amount expected to be realized.

Off-Balance Sheet Arrangements

[Table of Contents](#)

Our liquidity is not dependent on the use of off-balance sheet financing arrangements and as of June 30, 2015 we had no such arrangements.

Contractual Obligations

There has been no material change in our contractual obligations other than in the ordinary course of business since the year ended December 31, 2014.

Quarterly Trends

Our operating results fluctuate from quarter to quarter as a result of a variety of factors. We expect our operating results to continue to fluctuate in future quarters.

Our results reflect the effects of seasonal trends in listener and advertising behavior. We expect to experience both higher advertising sales due to greater advertiser demand during the holiday season and increased usage due to the popularity of holiday music during the last three months of each calendar year. In addition, we expect to experience lower advertising sales in the first three months of each calendar year due to reduced advertiser demand and increased usage due to increased use of media-streaming devices received as gifts during the holiday season. We believe these seasonal trends have affected, and will continue to affect our operating results, particularly as increases in content acquisition costs from increased usage are not offset by increases in advertising sales in the first calendar quarter.

In addition, expenditures by advertisers tend to be cyclical and discretionary in nature, reflecting overall economic conditions, the economic prospects of specific advertisers or industries, budgeting constraints and buying patterns and a variety of other factors, many of which are outside our control. As a result of these and other factors, the results of any prior quarterly or annual periods should not be relied upon as indications of our future operating performance.

Liquidity and Capital Resources

As of June 30, 2015, we had cash, cash equivalents and investments totaling \$461.5 million, which primarily consisted of cash and money market funds held at major financial institutions, commercial paper and investment-grade corporate debt securities.

Our principal uses of cash during the three and six months ended June 30, 2015 were funding our operations, as described below, and capital expenditures.

Sources of Funds

We believe, based on our current operating plan, that our existing cash and cash equivalents and available borrowings under our credit facility will be sufficient to meet our anticipated cash needs for at least the next twelve months.

From time to time, we may explore additional financing sources and means to lower our cost of capital, which could include equity, equity-linked and debt financing. In addition, in connection with any future acquisitions, we may require additional funding which may be provided in the form of additional debt, equity or equity-linked financing or a combination thereof. There can be no assurance that any additional financing will be available to us on acceptable terms.

Our Indebtedness

We are party to a \$60.0 million credit facility with a syndicate of financial institutions, which expires on September 12, 2018. As of June 30, 2015, we had no borrowings outstanding, \$1.1 million in letters of credit outstanding and \$58.9 million of available borrowing capacity under the credit facility.

Capital Expenditures

Consistent with previous periods, future capital expenditures will primarily focus on acquiring additional hosting and general corporate infrastructure. Our access to capital is adequate to meet our anticipated capital expenditures for our current plans.

Historical Trends

The following table summarizes our cash flow data for the six months ended June 30, 2014 and 2015.

| | Six months ended June 30, | |
|---|------------------------------|-----------|
| | 2014 | 2015 |
| | (in thousands) | |
| Net cash provided by (used in) operating activities | \$ (9,252) | \$ 17,059 |
| Net cash provided by (used in) investing activities | (93,715) | 6,093 |
| Net cash provided by financing activities | 15,044 | 5,230 |

Operating activities

In the six months ended June 30, 2015, net cash provided by operating activities was \$17.1 million and included a \$12.7 million increase in deferred revenue primarily due to the reinstatement of the annual subscription option in December 2014. Net cash provided by operating activities also included non-cash charges of \$62.2 million, primarily related to \$50.7 million in stock-based compensation charges and \$9.4 million in depreciation and amortization expense, offset by our net loss of \$64.3 million. Net cash provided by operating activities improved by \$26.3 million from the six months ended June 30, 2014, primarily due to a \$32.6 million increase in deferred revenue primarily due to the reinstatement of the annual subscription option in December 2014.

Investing activities

In the six months ended June 30, 2015, net cash provided by investing activities was \$6.1 million and included \$135.8 million in proceeds from sales and maturities of investments, offset by \$111.5 million in purchases of investments and \$17.9 million of capital expenditures for leasehold improvements and server equipment. Net cash provided by investing activities improved by \$99.8 million from the six months ended June 30, 2014, primarily due to a decrease in purchases of investments of \$82.6 million and an increase in proceeds from sales and maturities of investments of \$19.0 million.

Financing activities

In the six months ended June 30, 2015, net cash provided by financing activities was \$5.2 million and included \$3.3 million in proceeds from our employee stock purchase plan and \$2.9 million in proceeds from the exercise of stock options. Net cash provided by financing activities decreased \$9.8 million from the six months ended June 30, 2014, primarily due to a decrease in proceeds from the exercise of stock options of \$9.7 million.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses and the related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. Our estimates form the basis for our judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

An accounting policy is considered to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used, or changes in the accounting estimate that are reasonably likely to occur, could materially impact the condensed consolidated financial statements. We believe that our critical accounting policies reflect the more significant estimates and assumptions used in the preparation of the condensed consolidated financial statements.

Other than those discussed below, there have been no material changes to our critical accounting policies and estimates as compared to those described in our Annual Report on Form 10-K for the year ended December 31, 2014 under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies and Estimates.”

Stock-Based Compensation — Market Stock Units ("MSUs")

We implemented a market stock unit program in March 2015 for certain key executives. Specifically, MSUs measure Pandora's total stockholder return ("TSR") performance against that of the Russell 2000 Index across three performance periods.

We have determined the grant-date fair value of the MSUs using a Monte Carlo simulation performed by a third-party valuation firm. The Monte Carlo simulation model utilizes multiple input variables to estimate the probability that market conditions will be achieved. These variables include our expected stock price volatility over the expected term of the award, actual and projected employee stock option exercise behaviors and the risk-free interest rate for the expected term of the award. The variables used in these models are reviewed on an annual basis and adjusted, as needed. We recognize stock-based compensation for the MSUs over the requisite service period using the accelerated attribution method.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Interest Rate Fluctuation Risk

There have been no material changes in our primary market risk exposures or how those exposures are managed from the information disclosed in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2014. For further discussion of quantitative and qualitative disclosures about market risk, reference is made to our Annual Report on Form 10-K.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain “disclosure controls and procedures,” as such term is defined in Rule 13a-15(e) under the Exchange Act, that are designed to ensure that information required to be disclosed by us 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 Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. Based on their evaluation at the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of June 30, 2015.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The material set forth in Note 5 in the Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q is incorporated herein by reference.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. Before deciding to invest in our common stock, you should carefully consider each of the risk factors described in “Part I - Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2014 and all information set forth in this Quarterly Report on Form 10-Q. Those risks and the risks described in this Quarterly Report on Form 10-Q, including in the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” could materially harm our business, financial condition, operating results, cash flow and prospects. If that occurs, the trading price of our common stock could decline, and you may lose all or part of your investment.

There have been no material changes to the Risk Factors described under “Part I - Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2014, other than as set forth below. The risk factors below, all of which originally appear in our Annual Report on Form 10-K, have been updated to reflect additional information regarding programmatic buying on mobile and platforms for deploying and monitoring ads, among other things.

Advertising spending is increasingly being placed through new data-driven channels, such as the programmatic buying ecosystem, where mobile offerings are not as mature as their web-based equivalents. Because the majority of our listener hours occur on mobile devices, our growth prospects and revenue may be adversely impacted if the advertising ecosystem is slow to adopt data-driven mobile advertising offerings.

As new advertising channels, such as programmatic buying, develop around data-driven technologies and advertising products, an increasing percentage of advertising spend is likely to shift to such channels and products. These data-driven advertising products and programmatic buying channels allow publishers to use data to target advertising toward specific groups of consumers who are more likely to be interested in the advertising message delivered. These advertising products and programmatic channels are currently more developed in terms of ad technology and industry adoption on the web than they are on mobile. Due to the fact that the majority of our listener hours occur on mobile devices, our ability to attract advertising spend, and ultimately our ad revenue, may be negatively impacted by this shift. We have no reliable way to predict how significantly or how quickly advertisers will shift buying to programmatic channels and data-driven advertising products on the web.

We have developed a data-driven, programmatic advertising capability for mobile in an effort to take advantage of this trend. However, we only released this capability to the market in the second quarter of 2015, and we have no reliable way to predict how significantly or how quickly advertisers will shift buying toward such data-driven ad products and programmatic channels on mobile. If advertising spend continues to be reallocated to web-based programmatic channels and mobile programmatic adoption lags, our ability to grow revenue may be impacted and our business could be materially and adversely affected.

We rely upon an agreement with DoubleClick, which is owned by Google, for delivering and monitoring most of our ads. Failure to renew the agreement on favorable terms, or termination of the agreement, could adversely affect our business.

We use DoubleClick’s ad-serving platform to deliver and monitor most of the ads for our service. There can be no assurance that our agreement with DoubleClick, which is owned by Google, will be extended or renewed upon expiration, that we will be able to extend or renew our agreement with DoubleClick on terms and conditions favorable to us or that we could identify another alternative vendor to take its place. Our agreement with DoubleClick also allows DoubleClick to terminate our relationship before the expiration of the agreement on the occurrence of certain events, including material breach of the agreement by us, and to suspend provision of the services if DoubleClick determines that our use of its service violates certain security, technology or content standards.

Item 6. Exhibits

| Exhibit No. | Exhibit Description | Incorporated by Reference | | | | | Filed Herewith |
|-------------|---|---------------------------|----------|---------|-------------|----------|----------------|
| | | Form | File No. | Exhibit | Filing Date | Filed By | |
| 10.10.L | First Lease Modification and Term Extension and Additional Space Agreement between 125 Park Owner LLC and Pandora Media, Inc., dated July 22, 2015 | | | | | | X |
| 31.01 | Certification of the Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act | | | | | | X |
| 31.02 | Certification of the Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act | | | | | | X |
| 32.01 | Certification of the Principal Executive Officer and Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act | | | | | | X |
| 101 | Interactive Data Files Pursuant to Rule 405 of Regulation S-T: (i) Condensed Balance Sheets as of June 30, 2015 and December 31, 2014, (ii) Condensed Statements of Operations for the three and six months ended June 30, 2015 and 2014, (iii) Condensed Statements of Comprehensive Loss for the three and six months ended June 30, 2015 and 2014, (iv) Condensed Statements of Cash Flows for the six months ended June 30, 2015 and 2014 and (v) Notes to Condensed Financial Statements | | | | | | X |

† Indicates management contract or compensatory plan.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, Pandora Media, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PANDORA MEDIA, INC.

Date: July 24, 2015

By: /s/ Michael S. Herring
Michael S. Herring
Executive Vice President and Chief Financial Officer
(Duly Authorized Officer and Principal Financial and Accounting Officer)

FIRST LEASE MODIFICATION AND TERM EXTENSION AND
ADDITIONAL SPACE AGREEMENT

FIRST LEASE MODIFICATION AND TERM EXTENSION AND ADDITIONAL SPACE AGREEMENT (this “ Agreement”) dated as of the 22nd day of July, 2015 between 125 PARK OWNER LLC, having an office c/o SL Green Realty Corp., 420 Lexington Avenue, New York, New York (hereinafter referred to as “ Landlord”) and PANDORA MEDIA, INC., a Delaware corporation, having an office at 2101 Webster Street, Suite 1650, Oakland, California 94612 (hereinafter referred to as “ Tenant”).

WITNESSETH:

WHEREAS, Landlord and Tenant entered into that certain Lease dated as of June 13, 2013 (the “ Original Lease”), covering the entire rentable portion of the nineteenth (19th) and twentieth (20th) floors (hereinafter referred to as the “ Original Premises”), in the building known as 125 Park Avenue, New York, New York (the “ Building”) under the terms and conditions contained therein for a term scheduled to expire on September 30, 2024 (the “ Expiration Date”);

WHEREAS, Tenant wishes to extend the term of the Lease to the date (the “ New Expiration Date”) which is the last day of the month in which occurs the day immediately preceding the tenth (10th) anniversary of the Additional Space Rent Commencement Date (as hereinafter defined), unless the Lease is sooner terminated or expires pursuant to the terms of the Lease or pursuant to law;

WHEREAS, Tenant wishes to add to the Original Premises (i) the entire rentable portion of the 21st floor of the Building (the “ 21st Floor Premises”), and (ii) the entire rentable portion of the 22nd floor of the Building (the “ 22nd Floor Premises”), each approximately as shown hatched on the floor plans annexed hereto and made a part hereof as Exhibit A, for a term to commence on the Additional Space Commencement Date (as hereinafter defined) and to expire on the New Expiration Date (as hereinafter defined). For purposes hereof, the 21st Floor Premises and the 22nd Floor Premises are collectively referred to as, the “ Additional Space”. The Additional Space is deemed by Landlord and Tenant to consist of 51,065 rentable square feet for purposes of the Lease (i.e., 26,256 rentable square feet with respect to the 21st Floor Premises and 24,809 rentable square feet with respect to the 22nd Floor Premises);

WHEREAS, Landlord has agreed to extend the term of the Lease to the New Expiration Date and to permit Tenant to add the Additional Space to the Premises for a term as herein provided and, in all cases, otherwise subject to the terms, covenants and conditions of the Lease;

WHEREAS, Landlord and Tenant desire to modify the Lease in accordance with the above and in certain other respects, all as more particularly set forth herein.

N-

NOW, THEREFORE, in consideration of the agreements herein contained and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

Article 1

TERMS

Section 1.1. Except as otherwise defined herein, all capitalized terms used in this Agreement shall have the meanings given to such terms in the Original Lease. The Original Lease, as amended and modified by this Agreement, is referred to in this Agreement as the "Lease". The Original Premises, together with the Additional Space, is referred to in this Agreement as the "Premises".

ARTICLE 2

EXTENSION OF LEASE

Section 2.1. The term of the Original Lease shall be extended (the "Extended Term") under the same terms, covenants and conditions contained in the Original Lease, except to the extent specifically modified by this Agreement, so that the term of the Lease shall expire on the New Expiration Date, or upon such earlier date upon which the term of the Lease shall expire, be canceled or terminated pursuant to any of the conditions or covenants of the Lease or pursuant to law. Effective as of the date hereof, any reference in the Original Lease to the "Expiration Date" shall be deemed to be a reference to the New Expiration Date, unless the Lease is sooner terminated or expires pursuant to the terms of the Lease or pursuant to law.

ARTICLE 3

ADDITIONAL SPACE; CONDITION OF ADDITIONAL SPACE

Section 3.1. Additional Space.

(a) The Additional Space shall be added to the Premises under all the applicable terms and conditions of the Original Lease, except as modified herein, for a term (the "Additional Space Term") commencing on the date (the "Additional Space Commencement Date") which is the earlier to occur of (i) the date Tenant (or anyone claiming by, through or under Tenant) first occupies the Additional Space for either the performance of Alterations or for the ordinary conduct of Tenant's business, and (ii) the date Landlord's Pre-Commencement Additional Space Work (as hereinafter defined) has been substantially completed, and shall end on the New Expiration Date. Unless the context otherwise requires and, effective as of the Additional Space Commencement Date, references in the Original Lease to the Premises shall be deemed to include the Additional Space.

(b) The parties acknowledge that Tenant has inspected the Additional Space and the Building and is fully familiar with the physical condition thereof and Tenant agrees to accept the Additional Space at the commencement of the Additional Space Term in its then “as is” condition, subject to the performance by Landlord of Landlord’s Additional Space Work in the 21st Floor Premises. Except for the performance of Landlord’s Additional Space Work, Tenant acknowledges and agrees that Landlord shall have no obligation to do any work in or to the Additional Space in order to make it suitable and ready for occupancy and use by Tenant. For purposes of clarification, Tenant expressly acknowledges and agrees that Landlord’s Additional Space Work shall only be performed with respect to the 21st Floor Premises and no such Landlord’s Additional Space Work is required to be performed in the 22nd Floor Premises. Notwithstanding the foregoing to the contrary, if during the performance of Tenant’s Initial Additional Space Work, it shall be determined that the restrooms located in the 22nd Floor Premises are not in compliance with the Americans with Disabilities Act of 1990 (as defined on the date hereof), then upon notice from Tenant to Landlord thereof, Landlord shall perform such work as shall be reasonably necessary to cause the restrooms in the 22nd Floor Premises to be in compliance with the Americans with Disabilities Act of 1990 (as defined on the date hereof). Nothing contained herein shall be or be deemed to relieve Landlord of any ongoing maintenance and repair obligations set forth in the Original Lease with respect to the Building systems serving the Additional Space (including, without limitation, any fire and life safety systems that Landlord is required to repair and maintain pursuant to the terms of the Original Lease).

(c) (i) Following the date hereof, Landlord shall, at its sole cost and expense, perform the work detailed on Exhibit B-1 annexed hereto (the “Landlord’s Pre-Commencement Additional Space Work”) in the 21st Floor Premises pursuant to the terms and conditions detailed therein. Following the Additional Space Commencement Date, Landlord shall, at its sole cost and expense, perform the work detailed on Exhibit B-2 annexed hereto (the “Landlord’s Post-Commencement Additional Space Work”); and collectively with the Landlord’s Pre-Commencement Additional Space Work, referred to as the “Landlord’s Additional Space Work”) in the 21st Floor Premises pursuant to the terms and conditions detailed therein. Landlord’s Pre-Commencement Additional Space Work shall be deemed to be “substantially completed” notwithstanding that minor or non-material details of construction, mechanical adjustment or decoration which do not interfere with the performance of Tenant’s Additional Space Work (as hereinafter defined) or the ordinary conduct of Tenant’s business in the 21st Floor Premises (in either case, other than to a de minimis extent) remain to be performed (the “Additional Space Punch List Items”). Landlord and Tenant hereby acknowledge and agree that the Additional Space Punch List Items, Landlord’s Post-Commencement Additional Space Work and Tenant’s Additional Space Initial Work shall be performed simultaneously and the parties shall reasonably cooperate with each other with respect to scheduling each portion of said work.

(ii) If any approvals and/or final signoffs required pursuant to Applicable Laws with respect to Landlord’s Pre-Commencement Work have not been obtained as of the Commencement Date, Landlord shall be required to thereafter pursue and obtain all such approvals and final signoffs if and to the extent that failure to do so

would prevent or delay Tenant from obtaining a building permit or a final sign-off with respect to Tenant's Initial Additional Space Work or would otherwise adversely affect Tenant's ability to use the Additional Space for any of the uses permitted under the Lease.

(d) (i) If Landlord shall be unable to give possession of the Additional Space by a certain date because of the retention of possession of any occupant thereof, alteration or construction work, or for any other reason, Landlord shall not be subject to any liability for such failure (except as provided in Section 3.1(d)(ii), (iii) and (iv) below). In such event, the Original Lease, as modified by this Amendment, shall stay in full force and effect with respect to the Additional Space without further extension of the term of the Lease. The provisions of this Section 3.1(d) are intended to constitute an "express provision to the contrary" within the meaning of Section 223-a of the New York Real Property Law.

(ii) Anything to the contrary herein notwithstanding, if the Additional Space Commencement Date has not occurred (or has not been deemed to have occurred) on or before the date that is two hundred forty (240) days following the date of this Agreement (as such date shall be extended due to casualty, condemnation, Unavoidable Delays and/or Tenant Delays, the "Additional Space Outside Date"), then the Additional Space Rent Commencement Date (as hereinafter defined) shall be extended by one day for each day beyond the Additional Space Outside Date that the Additional Space Commencement Date shall occur (or shall be deemed to have occurred).

(iii) Anything to the contrary herein notwithstanding, if Landlord's Post-Commencement Additional Space Work has not been substantially completed (or has not been deemed to have been substantially completed) on or before the date that is fifteen (15) days following the date Tenant shall have completed Tenant's Initial Additional Space Work (as hereinafter defined) and commenced business operations in the Additional Space and notice thereof shall have been given to Landlord at least thirty (30) days prior to such commencement of such business operations (as such date shall be extended due to casualty, condemnation, Unavoidable Delays and/or Tenant Delays, the "Additional Space Post-Commencement Work Outside Date"), then Tenant shall receive a credit in the amount of \$1,000.00 for each day beyond the Additional Space Post-Commencement Work Outside Date that Landlord's Post-Commencement Additional Space Work shall have been substantially completed (or shall have been deemed to have been substantially completed), which credit shall be applied to the initial Fixed Annual Rent payment(s) due under the Lease with respect to the Additional Space).

(iv) Anything to the contrary herein notwithstanding, if the Additional Space Commencement Date has not occurred on or before the date that is three hundred (300) days following the date of this Agreement (as such date shall be extended by one (1) day for each day of delay due to casualty, condemnation, Unavoidable Delay and/or Tenant Delay, the "Additional Space Outside Termination Date"), then within ten (10) days following the Additional Space Outside

Termination Date, time being of the essence, Tenant may give to Landlord notice of Tenant's intent to terminate this Lease upon thirty (30) days' notice to Landlord, which notice of termination must be given on or before the occurrence (or deemed occurrence) of the Additional Space Commencement Date. If Tenant gives a termination notice pursuant to the preceding sentence and Landlord fails, on or before the expiration of such thirty (30) day period to deliver possession of the Additional Space to Tenant in the condition required hereunder, then the Lease shall terminate in respect of the Additional Space only, on the expiration of such thirty (30) day period, and neither Landlord nor Tenant shall have any further obligation or liability to the other under the Lease with respect to the Additional Space only except under any provision of the Lease that expressly survives the expiration or earlier termination of the Lease.

(e) Following the Additional Space Commencement Date and Tenant's submission of plans and specifications for Tenant's Initial Additional Space Work, Landlord shall deliver to Tenant a form ACP-5 covering the Additional Space.

ARTICLE 4

CONDITION OF ORIGINAL PREMISES

Section 4.1. Landlord and Tenant each hereby acknowledge and agree that Tenant is currently in occupancy of the Original Premises, has inspected the same and the Building and is fully familiar with the physical condition thereof and Tenant agrees to accept the Original Premises on the date hereof in their current "as is" condition and Landlord shall not be required to perform any work, to pay any work allowance or any other amount or to render any services to make the Original Premises ready for Tenant's continued use thereof.

ARTICLE 5

FIXED RENTAL

Section 5.1. Original Premises.

(a) From and after the date hereof and through and including the Expiration Date (i.e., September 30, 2024), Tenant shall continue to pay the Fixed Annual Rent that is due and payable under the Original Lease with respect to the Original Premises without modification or amendment thereof.

(b) With respect to the Original Premises, from and after October 1, 2024 through and including the New Expiration Date, Tenant shall pay Fixed Annual Rent (payable at the times and in the manner set forth in the Original Lease) at the rate of \$3,671,500.00 per annum (\$305,958.33 per month).

Section 5.2. Additional Space.

(a) From and after the Additional Space Commencement Date, Tenant shall pay Fixed Annual Rent for the Additional Space as follows:

(i) \$3,319,225.00 per annum (\$276,602.08 per month) for the period commencing on the Additional Space Commencement Date and ending on the last day of the month in which occurs the day immediately preceding the fifth (5th) anniversary of the Additional Space Rent Commencement Date (the "1st Additional Space Rent Period"); and

(ii) \$3,574,550.00 per annum (\$297,879.17 per month) for the period commencing on the day immediately following the expiration of the 1st Additional Space Rent Period and ending on the New Expiration Date.

(b) Subject to the provisions hereof, if and so long as Tenant is not then in monetary or material non-monetary default under the Lease beyond any applicable cure or grace period, the Fixed Annual Rent payable pursuant to Section 5.2(a) above with respect to the Additional Space only shall be abated for the period commencing on the Additional Space Commencement Date and ending on the date (the "Additional Space Rent Commencement Date") that is three hundred thirty (330) days following the Additional Space Commencement Date. If, however, during the period (the "Additional Space Rent Abatement Period") referenced in the immediately preceding sentence during which Fixed Annual Rent is to be abated, Tenant shall default in the payment of a sum of money or any other of its obligations under the Lease after notice and the expiration of any applicable cure periods, if any, then, notwithstanding the foregoing, the Rent Abatement Period shall be deemed to have ended on the date such default occurred; provided, however, if Tenant cures such default prior to any termination of the Lease by Landlord due to such default pursuant to the terms hereof, then Tenant shall then be entitled to any remaining abatement of Fixed Annual Rent remaining with respect to such initial period that was not previously received by Tenant pursuant to this Section 5.2(b).

ARTICLE 6

ADDITIONAL RENT AND ESCALATION RENT

Section 6.1. Original Premises.

(c) From and after the date hereof and through and including the Expiration Date (i.e., September 30, 2024), Tenant shall continue to pay the Additional Rent that is due and payable under the Original Lease (including, without limitation, pursuant to Articles 32 and 49) with respect to the Original Premises without modification or amendment thereof.

(d) With respect to the Original Premises only, in addition to the payment of Fixed Annual Rent as hereinabove provided, from and after October 1, 2024 and through and including the New Expiration Date, Tenant shall pay all Additional Rent accruing under the Lease (including, without limitation, pursuant to Articles 32 and 49 of the Original Lease), provided however, that, solely with respect to the Original Premises:

(i) The term “Base Tax Year”, as defined in Section 32.01(a)(iii) of the Original Lease, shall mean the New York City fiscal tax year commencing on July 1, 2015 and ending on June 30, 2016; and

(ii) The term “Base Year”, as defined in Section 49.02(iii) of the Original Lease, shall mean the calendar year 2015”.

Section 6.2. Additional Space.

(a) With respect to the Additional Space only, in addition to the payment of Fixed Annual Rent as hereinabove provided, from and after the Additional Space Commencement Date and through and including the New Expiration Date, Tenant shall continue pay all Additional Rent accruing under the Lease (including, without limitation, pursuant to Articles 32 and 49 of the Original Lease), with respect to the Additional Space, provided however, that, solely with respect to the Additional Space:

(i) The term “Tenant’s Share”, as defined in Section 32.01(a)(i) of the Original Lease, shall mean 8.9%;

(ii) The term “Base Tax Year”, as defined in Section 32.01(a)(iii) of the Original Lease, shall mean the New York City fiscal tax year commencing on July 1, 2015 and ending on June 30, 2016;

(iii) The term “Base Year”, as defined in Section 49.02(iii) of the Original Lease, shall mean the calendar year 2015; and

(iv) The term “Percentage”, as defined in Section 49.02(v) of the Original Lease, shall mean 8.4%.

ARTICLE 7

LANDLORD’S ADDITIONAL SPACE CONTRIBUTION

Section 7.1. Provided that no monetary or material non-monetary default by Tenant after notice and the expiration of any applicable cure period has occurred and is continuing, Landlord, subject to and in accordance with the provisions of this Article 45 of the Original Lease (as amended by this Amendment), shall contribute up to the sum of \$3,319,225.00 (“Landlord’s Additional Space Contribution”) towards the cost (the “Additional Space Work Cost”) of Tenant’s Initial Additional Space Work (as hereinafter defined). For purposes hereof, “Tenant’s Initial Additional Space Work”) shall mean Alterations to be performed in the Additional Space in order to prepare the same for Tenant’s initial occupancy thereof immediately following the Additional Space Commencement Date and the conduct of business therein. Without limitation, for purposes of this Article, Tenant’s Initial Additional Space Work shall be deemed not to include, and Landlord’s Additional Space Contribution shall not be applied to (except as otherwise expressly permitted

hereunder), the cost of interest, late charges, or any personal property whatsoever, or to the cost of labor, materials or services used to furnish or provide the personal property.

Section 7.2. Landlord's Additional Space Contribution shall be payable by Landlord to Tenant in accordance with, and pursuant to, the terms and conditions of Sections 45.03 and 45.04 of the Original Lease except that the references therein to: (i) "Work Cost" shall mean the Additional Space Work Cost, (ii) the "Premises" shall mean the "Additional Space", (iii) "Landlord's Contribution" shall mean Landlord's Additional Space Contribution, and (iv) "Tenant's Initial Alteration Work" shall mean Tenant's Initial Additional Space Work.

Section 7.3. It is expressly understood and agreed that if the amount of Landlord's Additional Space Contribution with respect to the Additional Space is less than the cost of Tenant's Initial Additional Space Work with respect thereto, Tenant shall remain solely responsible for the payment and completion of, and in all events shall complete, at its sole cost and expense, Tenant's Initial Additional Space Work. Further, if Tenant fails to submit a requisition for any portion of the Landlord's Additional Space Contribution by the date which is the two (2) year anniversary of the Additional Space Commencement Date, then Tenant shall have no further right to utilize any such portion of the Landlord's Additional Space Contribution so not requisitioned and Landlord shall have no obligation to reimburse Tenant for same. The provisions of Section 45.05(b) shall not be applicable to the Landlord's Additional Space Contribution.

Section 7.4. The Landlord's Additional Space Contribution is being given for the benefit of the Named Tenant (as such term is defined in the Original Lease) only. No third party shall be permitted to make any claims against Landlord or Tenant with respect to any portion of the Landlord's Additional Space Contribution.

ARTICLE 8

RENEWAL OPTION

Section 8.1. Landlord and Tenant acknowledge and agree that Tenant's Extension Right described in Article 48 of the Original Lease shall remain in full force and effect and all references therein to the "Expiration Date" shall mean the Extended Expiration Date and all references therein to the "Premises" shall mean the entire Premises then being leased by Tenant (including, without limitation, the Original Premises and the Additional Space, if then applicable).

ARTICLE 9

RIGHT OF FIRST OFFER

Section 9.1 Subject to the provisions of this Article 9, provided and on the condition that (i) the Tenant under this Lease at the time in question is the Named Tenant (as such term is defined in the Original Lease), (ii) no monetary or material non-monetary default after notice and the expiration of any applicable cure period has

occurred and is continuing at the time of the giving of the Option Response Notice or the ROFO Space Commencement Date, (iii) as of the date Tenant gives the Option Response Notice and as of the ROFO Space Commencement Date, the Named Tenant (as such term is defined in the Original Lease) shall be in actual occupancy of at least ninety (90%) percent of the Premises then leased to Tenant under the Lease, and (iv) there remain at least five (5) years in the Term of the Lease determined as of the Scheduled ROFO Space Commencement Date (or, if less than five (5) years remain in the Term of the Lease (but at least fifteen (15) months remain)), Tenant, simultaneously with the giving of an Option Response Notice, irrevocably exercises any unexpired or unexercised Tenant's Extension Right so long as Tenant has such right under the Lease), Landlord shall not enter into a lease for the entire ROFO Space (as hereinafter defined) with any party other than Tenant (subject to Section 9.04(a) below) at any time during the Term of the Lease, without first instituting the procedure described in, and subject to the limitations set forth in, this Article 9. For purposes hereof, "ROFO Space" shall mean the entire rentable area of the twenty-third (23rd) floor of the Building.

Section 9.2 Landlord shall institute the procedure described in this Article 9 by giving notice thereof (the "Option Notice") to Tenant, which Option Notice shall set forth the date that Landlord reasonably expects that the ROFO Space will be vacant and available for Tenant's occupancy (such date designated by Landlord being referred to herein as the "Scheduled ROFO Space Commencement Date"). Landlord shall have the right to give an Option Notice with respect to the ROFO Space at any time if the ROFO Space shall become available for lease or if Landlord reasonably anticipates that the ROFO Space shall become available for lease; provided, however, that Landlord shall not give an Option Notice more than eighteen (18) months prior to the Schedule ROFO Space Commencement Date.

Section 9.3 Tenant shall have the one-time option with respect to the ROFO Space (the "ROFO Option") to lease the entire ROFO Space for a term (the "Option Term") commencing on the ROFO Space Commencement Date and expiring on the New Expiration Date by giving notice thereof (the "Option Response Notice") to Landlord not later than the twentieth (20th) day after the date that Landlord gives the Option Notice to Tenant. Time shall be of the essence as to the date by which Tenant must give the Option Response Notice to Landlord. Tenant may only exercise the ROFO Option with respect to all of the ROFO Space and not merely a portion thereof. If Tenant does not give the Option Response Notice to Landlord on or prior to the twentieth (20th) day after the date that Landlord gives the Option Notice to Tenant, then, Landlord shall thereafter have the right to lease the applicable ROFO Space (or any part thereof) to any other party on terms acceptable to Landlord in Landlord's sole discretion without being required to make any other offer to Tenant regarding the ROFO Space under this Article 9 and this Article 9 there thereafter become void and of no further force and effect.

Section 9.4 Tenant shall not have the right to exercise the ROFO Option (and Landlord shall not be required to give an Option Notice) in respect of any ROFO Space prior to Landlord's leasing such ROFO Space to (i) any party having a renewal right contained

in such party's lease with respect to such ROFO Space, (ii) any party whose lease is renewed voluntarily by Landlord (irrespective if such renewal right is contained in such party's lease), (iii) any then occupant of all or any portion of the ROFO Space (irrespective of whether such occupant shall have any right in its occupancy agreement or otherwise to lease such space) or (iv) any party to which Landlord has granted an expansion right, first offer right or other similar right with respect to such ROFO Space as of the date of this Agreement. Landlord represents that as of the date of this Agreement, Landlord has not granted any expansion right, first offer right or other similar right with respect to the ROFO Space to any party. Accordingly, (A) Landlord shall have no obligation to give an Option Notice to Tenant with respect to the ROFO Space (or any portion thereof), and (B) Landlord shall have the right to lease the ROFO Space (or any portion thereof) to any such party described in this Section 9.4 without first offering such ROFO Space (or the applicable portion thereof) to Tenant as contemplated by this Article 9.

Section 9.5 (a) If Tenant timely and properly exercises the ROFO Option in accordance with the terms of this Article 9, then the ROFO Space shall be included within the Premises on the date (the "ROFO Space Commencement Date") which is the later to occur of (a) the Scheduled ROFO Space Commencement Date and (b) the date on which Landlord delivers to Tenant vacant, broom-clean possession of the applicable ROFO Space, upon the following terms and conditions and all other applicable terms and conditions of the Lease (as extended pursuant to Section 9.9), all of which shall take effect as of the ROFO Space Commencement Date:

(i) The Fixed Annual Rent for the ROFO Space shall be payable from and after the ROFO Space Commencement Date in an amount equal to the ROFO Space FMRV (as hereinafter defined). "ROFO Space FMRV" shall mean 100% of the fair market rental value of the ROFO Space that an unaffiliated third party would be willing to pay to Landlord as of the ROFO Space Commencement Date, which ROFO Space FMRV shall be determined in accordance with the provisions of Section 9.7 below taking into account all then relevant factors, whether favorable to Landlord or Tenant;

(ii) "Tenant's Share", as defined in Article 32 of the Original Lease, and the "Percentage", as defined in Article 49 of the Original Lease, shall be increased to include the rentable square footage of the ROFO Space (as reasonably determined by Landlord); and

(iii) Landlord shall not be obligated to perform any work or make any installations in the ROFO Space to prepare same for Tenant's occupancy, grant Tenant any work allowance or rent concession therefor, and Tenant shall accept the ROFO Space in its "as is" condition on the ROFO Space Commencement Date (unless otherwise expressly provided by Landlord to the contrary, in Landlord's sole discretion, as part of an Option Notice).

Section 9.6 Landlord shall deliver vacant and exclusive possession of the ROFO Space to Tenant on the Scheduled ROFO Space Commencement Date; provided,

that (x) if a party remains in occupancy of the ROFO Space (or any portion thereof) on the Scheduled ROFO Space Commencement Date, then Landlord shall use commercially reasonable efforts to cause vacant and exclusive possession of the ROFO Space to be delivered to Tenant as promptly as reasonably practicable thereafter, and (y) Landlord shall have no liability to Tenant, and Tenant shall have no right to terminate or rescind the Lease or Tenant's exercise of the ROFO Option or reduce the Rent, in each case deriving from Landlord's failure to deliver vacant and exclusive possession of the ROFO Space to Tenant on the Scheduled ROFO Space Commencement Date.

Section 9.7 (a) In the event that Tenant properly and timely exercises the ROFO Option, then within thirty (30) days following the date upon which Tenant gives to Landlord the Option Response Notice, Landlord and Tenant shall commence negotiations in good faith to attempt to agree upon the ROFO Space FMRV for the ROFO Space. If Landlord and Tenant cannot reach agreement within twenty (20) days thereafter (the "Negotiation Period"), then the ROFO Space FMRV for the ROFO Space shall be determined in accordance with the process and provisions set forth in Section 48.02 of the Original Lease except that (i) Landlord shall select Landlord's Broker and Tenant shall select Tenant's Broker no later than ten (10) business days following the expiration of the Negotiation Period, (ii) Landlord's Broker and Tenant's Broker shall proceed with the selection of the Independent Broker if they are not able to agree upon the ROFO Space FMRV within fifteen (15) business days after both of them shall have been appointed, (iii) any reference therein to "Renewal FMRV" shall be deemed to be referring to the ROFO Space FMRV, and (iv) any other references therein that shall not be applicable to the determination of the ROFO Space FMRV shall be deemed inapplicable.

(b) If the final determination of the ROFO Space FMRV is not made on or before the ROFO Space Commencement Date in accordance with the provisions of this Article 9, then, pending such final determination, the ROFO Space FMRV shall be deemed to be the average of the determination of Landlord's Broker and the determination of Tenant's Broker. If, based upon the final determination hereunder of the ROFO Space FMRV, the payments made by Tenant on account of the Rent for the period prior to the final determination of the ROFO Space FMRV were less than the Rent payable for such period, then Tenant, not later than the thirtieth (30th) day after Landlord's demand therefor, shall pay to Landlord the amount of such deficiency. If, based upon the final determination of the ROFO Space FMRV, the payments made by Tenant on account of the Rent for the period prior to the final determination of the ROFO Space FMRV were more than the Rent due hereunder for such period, then Landlord, not later than the thirtieth (30th) day after Tenant's demand therefor, shall pay or credit such excess to Tenant.

(c) Promptly after the occurrence of the ROFO Space Commencement Date, Landlord and Tenant shall confirm the occurrence thereof, the inclusion of the ROFO Space in the Premises, by executing an instrument reasonably satisfactory to Landlord and Tenant; provided, that failure by Landlord or Tenant to execute such instrument shall not affect the inclusion of such ROFO Space in the Premises in accordance with this Article 9.

Section 9.8 Anything to the contrary herein notwithstanding, Landlord shall have the right (hereinafter called "Landlord's Acceleration Right") to accelerate the exercise of the ROFO Option in advance of the Scheduled ROFO Space Commencement Date by written notice thereof to Tenant ("Landlord's Acceleration Notice"), and to cause the ROFO Space Commencement Date to occur earlier than the Scheduled Option Commencement Date in the event that the same will become available for delivery to Tenant earlier than the Scheduled Option Commencement Date (the "Acceleration Date"); it being agreed, however, that the Acceleration Date shall not occur on a date that is less than forty-five (45) days following the giving of a Landlord's Acceleration Notice. Notwithstanding the foregoing, for purposes of this Article 9, the applicable ROFO Space shall not be deemed to "become available" for Tenant earlier than the Scheduled ROFO Space Commencement Date except in the event that the existing lease(s) for such space shall be terminated by reason of a ROFO Space Termination Event (as such term is hereinafter defined). As used herein, the term "ROFO Space Termination Event" shall mean one or more of the following: (i) a default by the existing tenant or occupant of such space (hereinafter called the "Existing Tenant") under the Existing Tenant's lease (hereinafter called the "Existing Lease") after the expiration of any applicable notice and cure periods provided for in the Existing Lease; (ii) a voluntary surrender or early termination of the Existing Lease (or a portion thereof); or (iii) a rejection of the Existing Lease in bankruptcy or the filing of a bankruptcy or insolvency proceeding by or against the Existing Tenant. In the event that Landlord shall exercise Landlord's Acceleration Right, Tenant shall notify Landlord that it is electing to exercise the ROFO Option by providing an Option Response Notice no later than twenty (20) days following the giving of such Landlord's Acceleration Notice (time shall be of the essence with respect to such date), and if Tenant exercises the ROFO Option the Scheduled ROFO Space Commencement Date shall be deemed to be the Acceleration Date. If Tenant does not give the Option Response Notice to Landlord on or prior to the expiration of such 20-day period, then, Landlord shall thereafter have the right to lease the applicable ROFO Space (or any part thereof) to any other party on terms acceptable to Landlord in Landlord's sole discretion and Tenant shall no longer have any rights under this Article 9 and this Article 9 there thereafter become void and of no further force and effect.

Section 9.10 Notwithstanding anything to the contrary contained in this Article, Landlord shall have the right, in its sole discretion, to waive the conditions which limit or restrict the effectiveness of any exercise by Tenant of the ROFO Option hereunder, without thereby waiving a default, if any, by Tenant, in which event (i) the ROFO Space shall be added to the Premises without execution or delivery of any other or further document in accordance with the provisions of this Article 9 with the same force and effect as if such default did not occur or such conditions had been complied with, and (ii) Landlord shall be entitled to all of the remedies provided by this Lease and at law with respect to any such default.

Section 9.11 Notwithstanding anything to the contrary contained herein, if Tenant does not exercise a ROFO Option in a timely manner as set forth in Section 9.3 hereof, then Landlord shall be under no further obligation with respect to the ROFO Space under this Article 9, and Landlord shall at any and all times thereafter be entitled to lease

all or any portion of the ROFO Space to others at such rentals and upon such terms and conditions as Landlord in its sole discretion may desire.

ARTICLE 10

MISCELLANEOUS LEASE MODIFICATIONS

Section 10.1. The provisions of Section 15.05 of the Original Lease shall be applicable to this Amendment. In addition, Landlord, at Landlord's sole cost and expense (but subject to reimbursement, if any, in accordance with Article 49 below), shall comply with all Applicable Laws applicable to Landlord's Additional Space Work, including, without limitation, the removal of noted Building violations and liens resulting from Landlord's performance of Landlord's Additional Space Work that would delay Tenant from obtaining a building permit or a final sign-off on its Alterations or would otherwise adversely affect the use of the Additional Space for any of the uses permitted hereunder in accordance with the certificate of occupancy for the Building, subject, however, to Landlord's right to contest diligently and in good faith the applicability or legality thereof

Section 10.2. Effective as of the date hereof, Article 51 of the Original Lease is hereby deleted in its entirety.

Section 10.3. Effective as of the date hereof, Section 30.03 of the Original Lease is hereby modified to provide that no after hours charge shall be imposed by Landlord with respect to the first one hundred (100) hours of after hours freight elevator usage by Tenant (in the aggregate) in connection with Tenant's initial move-in to the Additional Space and/or Tenant's Initial Additional Space Work.

Section 10.4. Effective as of the date hereof, (i) Section 35.03 of the Original Lease is hereby modified to provide that any portion of the Supplemental Condenser Water allocated to the Original Premises and not yet utilized by Tenant for purposes thereof may, pursuant to the terms of Section 35.03, be utilized by Tenant in connection with the operation by Tenant of supplemental air-conditioning equipment in the Additional Space, and (ii) the CW Outside Date described in Section 35.03 shall mean the date this is five hundred forty (540) days after the Additional Space Commencement Date.

Section 10.5. Landlord and Tenant agree that electricity with respect to the Additional Space shall be provided pursuant to Article 41 of the Original Lease except that with respect to the Additional Space only, the second sentence of Section 41.01 shall be deleted and replaced with the following:

“Landlord shall make electricity available during the Term at the combined electrical closets servicing the Additional Space for all purposes (exclusive of electricity required for the operation of the Existing HVAC Equipment serving the Additional Space), with an average capacity of not

less than six (6) watts connected load per usable square foot of the Additional Space which shall be distributed by Tenant at its sole cost and expense.”

Section 10.6. Landlord and Tenant acknowledge and agree that notwithstanding anything to the contrary contained in (i) Section 30.01 of the Original Lease, the current rate for non HVAC Period heating service is \$243.00 per hour (which rate shall be increased from time to time by Landlord in accordance with the provisions of Section 30.01), and (ii) Section 35.01 of the Original Lease, the current rate for non HVAC Period air conditioning service is \$230.00 per hour (which rate shall be increased from time to time by Landlord in accordance with the provisions of Section 35.01).

Section 10.7. (a) Landlord and Tenant acknowledge and agree that the amount of the Required Security under the Lease is currently \$3,199,450.00, which amount, notwithstanding anything to the contrary contained in the Original Lease, is currently in the form of cash security (and not a Security Letter), which amount shall be held and utilized by Landlord in accordance with the terms of Article 31 of the Original Lease.

(a) As of the date hereof, Article 31 of the Original Lease is hereby amended as follows:

(i) Section 31.01(a) of the Original Lease is amended by increasing the “Required Amount” to \$5,975,452.09. Upon the execution and delivery of this Agreement, Tenant shall deliver to Landlord additional cash security so that the total cash security being held by Landlord is in the amount of the increased Required Amount (i.e., Tenant shall deliver to Landlord additional cash security in the amount of \$2,776,002.09).

(ii) Section 31.07 of the Original Lease is hereby deleted and replaced with the following:

“Notwithstanding anything to the contrary herein, provided and on the condition that, as of the date Tenant elects to reduce the amount of security required hereunder, Tenant shall not be in default under this Lease after notice and the expiration of any applicable cure and grace periods, then in such case, (i) on or after the third (3rd) anniversary of the Additional Space Rent Commencement Date, the security required under this Article 31 shall be reduced to \$4,345,783.34, and (ii) on or after the fifth (5th) anniversary of the Additional Space Rent Commencement Date, the security required under this Article 31 shall be reduced to \$3,259,337.50, in any such case, by Tenant delivering to Landlord notice requesting the return of the amount by which the Required Amount is being reduced pursuant to this Section 31.07 (provided that the Required Amount is then in the form of cash security).”

ARTICLE 11

BROKERAGE

Section 11.1. Tenant covenants, represents and warrants that Tenant has had no dealings or negotiations with any broker or agent in connection with the consummation of this Amendment other than SL Green Leasing LLC and CBRE, Inc. (collectively, the “Brokers”) and Tenant covenants and agrees to defend, hold harmless and indemnify Landlord from and against any and all cost, expense (including reasonable attorneys’ fees) or liability for any compensation, commissions or charges claimed by any broker or agent with respect to this Amendment or the negotiation thereof. Landlord covenants, represents and warrants that Landlord has had no dealings or negotiations with any broker or agent in connection with the consummation of this Amendment other than the Brokers and Landlord covenants and agrees to defend, hold harmless and indemnify Tenant from and against any and all cost, expense (including reasonable attorneys’ fees) or liability for any compensation, commissions or charges claimed by any broker or agent (including the Brokers) with respect to this Amendment or the negotiation thereof, based on claims that such broker or agent represented or acted on behalf of Landlord. Landlord shall pay to the Brokers a commission to be agreed upon between Landlord and the Brokers pursuant to separate agreements.

ARTICLE 12

MISCELLANEOUS

Section 12.1. Except as modified, amended and supplemented by this Agreement, the terms and provisions of the Lease shall continue in full force and effect and are hereby ratified and confirmed.

Section 12.2. This Agreement shall not be binding upon Landlord and Tenant unless and until it is signed by both parties hereto and a signed copy thereof is delivered by Landlord to Tenant.

Section 12.3. This Agreement constitutes the entire agreement among the parties hereto with respect to the matters stated herein and may not be amended or modified unless such amendment or modification shall be in writing and signed by the party against whom enforcement is sought.

Section 12.4. The terms, provisions and conditions contained in this Agreement shall bind and inure to the benefit of the parties hereto and their respective successors and assigns.

Section 12.5. This Agreement shall be governed in all respects by the laws of the State of New York.

Section 12.6. This Agreement may be executed in counterparts, each of which shall constitute an original and all of which taken together shall constitute one and the same agreement, and an executed counterpart delivered by “.pdf”, facsimile or email shall be binding upon the parties.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, Landlord and Tenant have duly executed this Agreement as of the day and year first above written.

125 PARK OWNER LLC

By: /s/ Steven M. Durels

Name: Steven M. Durels

Title: Executive Vice President, Director of Leasing and Real Property

PANDORA MEDIA, INC.

By: /s/ Mike Herring

Name: Mike Herring

Title: Chief Financial Officer

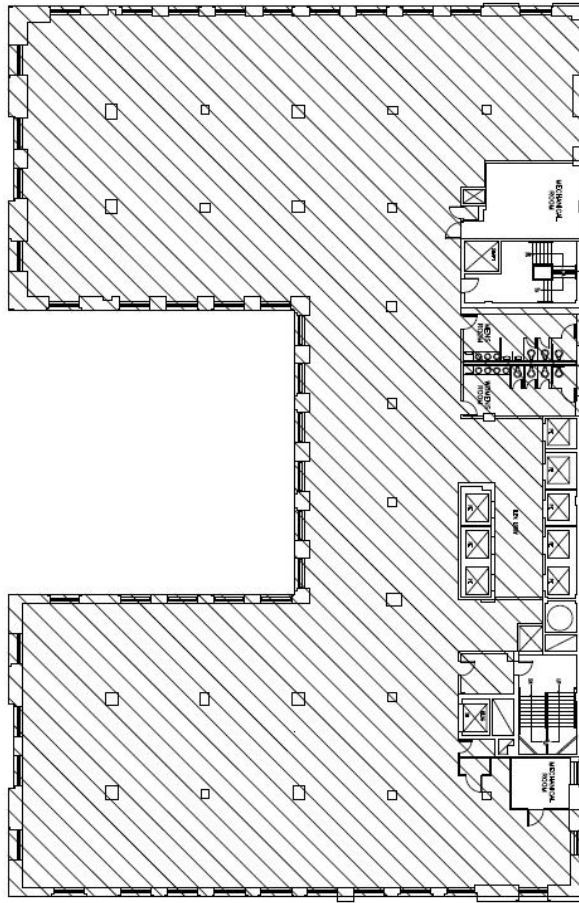
EXHIBIT A

Additional Space

[see attached]

N-

EAST 42ND STREET



EAST 41ST STREET

PARK AVENUE

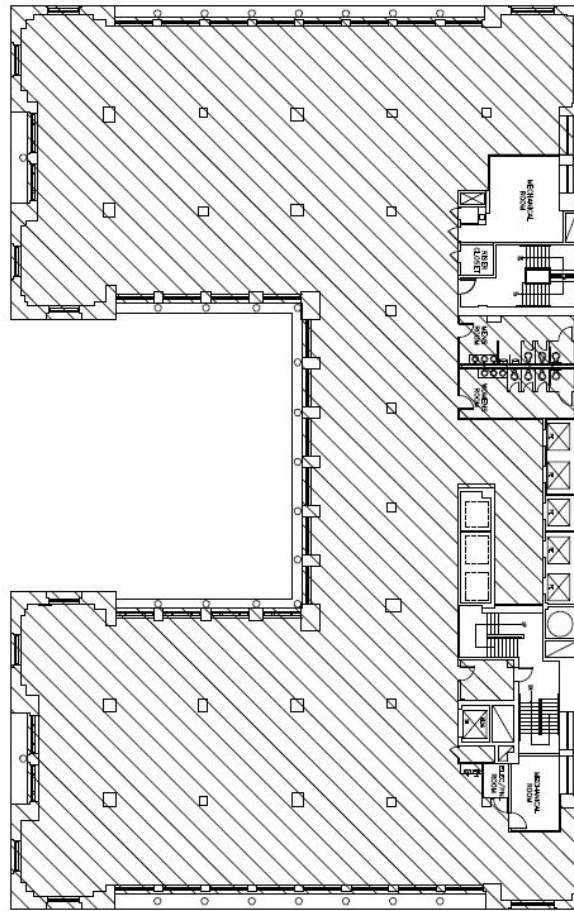
125 PARK AVENUE
21ST FLOOR

SCALE:
1" = 34'



ALL DIMENSIONS ARE APPROXIMATE AND ARE
SHOWN IN GENERAL IN THIS RESPONSE.

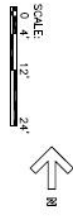
EAST 42ND STREET



EAST 41ST STREET

PARK AVENUE

125 PARK AVENUE
22ND FLOOR



ALL DIMENSIONS ARE APPROXIMATE AND ARE
BASED UPON 12/3/13 SURVEY DATA.



EXHIBIT B-1

Landlord's Pre-Commencement Additional Space Work

Landlord shall perform the following work in the 21st Floor Premises only in a Building-standard manner utilizing Building-standard materials, finishes and fixtures and in compliance with all Applicable Laws applicable to demolished space (except any signoffs or approvals in connection with Landlord's Pre-Commencement Additional Space Work shall be obtained by Landlord following substantial completion of Landlord's Pre-Commencement Additional Space Work, and not as a condition to the substantial completion thereof).

1. Demolish any existing installations in the 21st Floor Premises. The 21st Floor Premises shall be delivered in broom clean condition.
2. Deliver the main HVAC trunk on the 21st floor complete with smoke and fire dampers at the core.
3. Delivery fully operational sprinkler infrastructure with the heads turned up, including combination standpipe/sprinkler risers, pumps and valve connections.
4. All Building Systems serving the 21st Floor Premises and which are expressly required of Landlord to be provided under the Lease shall be in good working order and ready for Tenant's connection thereto; provided that distribution within the 21st Floor Premises shall be at Tenant's sole cost and expense.
5. Fireproofing on the core columns as required by code for demolished space. Landlord will ensure that all shafts and pipe penetrations within the Additional Space are firestopped.
6. Demolish the existing flooring, (demolishing includes scraping of glue or other adhesives from the installation of all flooring) and patch all holes, core drills and other similar perforations patched (as necessary) No leveling.
7. All perimeter and core walls shall be finished, taped and spackled to a reasonable condition.

N-

EXHIBIT B-2

Landlord's Post-Commencement Additional Space Work

Landlord shall perform the following work in the 21st Floor Premises in a Building-standard manner utilizing Building-standard materials, finishes and fixtures and in compliance with all Applicable Laws applicable to demolished space (except any signoffs or approvals in connection with Landlord's Post-Commencement Additional Space Work shall be obtained by Landlord following substantial completion of Landlord's Post-Commencement Additional Space Work, and not as a condition to the substantial completion thereof).

1. Provide reasonably sufficient points, for typical office use, for Tenant's connection to Building Class "E" system; provided that tie-ins to such system shall be at Tenant's sole cost and expense.
2. Renovate the core bathrooms on the 21st Floor Premises (in a manner so that such bathrooms shall be substantially consistent with the finishes and fixtures in the core bathrooms located on the 22nd Floor Premises).
3. Existing electrical panels shall be left in place. The existing meters and transformers shall be removed. Landlord shall install new electrical submeters.

**Certification of Principal Executive Officer
Pursuant to Section 302 of Sarbanes-Oxley Act of 2002**

I, Brian McAndrews, certify that:

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

July 24, 2015

/s/ Brian McAndrews

Name: Brian McAndrews
Title: *Chief Executive Officer, President and Chairman of the Board (Principal Executive Officer)*

**Certification of Principal Financial Officer
Pursuant to Section 302 of Sarbanes-Oxley Act of 2002**

I, Michael S. Herring, certify that:

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

July 24, 2015

/s/ Michael S. Herring

Name: Michael S. Herring

Title: *Executive Vice President and Chief Financial Officer (Principal Financial Officer)*

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF SARBANES-OXLEY ACT OF 2002**

The certification set forth below is being submitted in connection with this Quarterly Report on Form 10-Q for the quarter ended June 30, 2015 (the "Report") for the purpose of complying with Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Section 1350 of Chapter 63 of Title 18 of the United States Code.

Each of the undersigned certifies that, to his knowledge:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Pandora Media, Inc.

July 24, 2015

/s/ Brian McAndrews

Name: Brian McAndrews
Title: *Chief Executive Officer, President and Chairman of the Board (Principal Executive Officer)*

/s/ Michael S. Herring

Name: Michael S. Herring
Title: *Executive Vice President and Chief Financial Officer (Principal Financial Officer)*

This certification accompanying the Report is not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities such Section, and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before, on or after the date of the Report), irrespective of any general incorporation language contained in such filing.