

IZEA, Inc.  
Form 10-Q  
November 13, 2014  
Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2014

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No.: 333-167960

IZEA, INC.  
(Exact name of registrant as specified in its charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

37-1530765  
(I.R.S. Employer  
Identification No.)

480 N. Orlando Avenue, Suite 200  
Winter Park, FL  
(Address of principal executive offices)

32789  
(Zip Code)

Registrant's telephone number, including area code: (407) 674-6911

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 on 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

Edgar Filing: IZEA, Inc. - Form 10-Q

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

Accelerated filer

Non-accelerated filer

(Do not check if a smaller reporting company)

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

As of November 11, 2014, there were 57,497,631 shares of our common stock outstanding.

---

Table of Contents

Quarterly Report on Form 10-Q for the period ended September 30, 2014

Table of Contents

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Balance Sheets as of September 30, 2014 (unaudited) and December 31, 2013</u>	<u>1</u>
<u>Unaudited Consolidated Statements of Operations for the three and nine months ended September 30, 2014 and 2013</u>	<u>2</u>
<u>Unaudited Consolidated Statement of Stockholders' Equity (Deficit) for the nine months ended September 30, 2014</u>	<u>3</u>
<u>Unaudited Consolidated Statements of Cash Flows for the nine months ended September 30, 2014 and 2013</u>	<u>4</u>
<u>Notes to the Unaudited Consolidated Financial Statements</u>	<u>5</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>19</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>28</u>
<u>Item 4. Controls and Procedures</u>	<u>28</u>
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	<u>30</u>
<u>Item 1A. Risk Factors</u>	<u>30</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>31</u>
<u>Item 3. Defaults Upon Senior Securities</u>	<u>32</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>32</u>
<u>Item 5. Other Information</u>	<u>32</u>
<u>Item 6. Exhibits</u>	<u>33</u>
<u>Signatures</u>	<u>35</u>

Table of Contents

## PART I - FINANCIAL INFORMATION

## ITEM 1 - FINANCIAL STATEMENTS

## IZEA, Inc.

## Consolidated Balance Sheets

	September 30, 2014 (Unaudited)	December 31, 2013
Assets		
Current:		
Cash and cash equivalents	\$7,879,918	\$530,052
Accounts receivable	1,475,834	1,659,802
Prepaid expenses	485,176	109,960
Other current assets	150,892	83,486
Total current assets	9,991,820	2,383,300
Property and equipment, net of accumulated depreciation of \$220,319 and \$205,070	275,920	156,482
Software development costs, net of accumulated amortization of \$94,812 and \$0	474,063	362,346
Security deposits	57,641	46,574
Total assets	\$10,799,444	\$2,948,702
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities:		
Accounts payable	\$642,671	\$817,057
Accrued expenses	452,030	365,454
Unearned revenue	1,136,072	1,292,228
Current portion of capital lease obligations	60,001	43,852
Total current liabilities	2,290,774	2,518,591
Capital lease obligations, less current portion	15,601	34,013
Deferred rent	74,687	14,179
Warrant liability	5,423,124	1,832,945
Total liabilities	7,804,186	4,399,728
Stockholders' equity (deficit):		
Series A convertible preferred stock; \$.0001 par value; 240 shares authorized; no shares issued and outstanding	—	—
Common stock, \$.0001 par value; 200,000,000 shares authorized; 57,497,631 and 22,560,653 issued and outstanding	5,750	2,256
Additional paid-in capital	26,969,728	24,672,132
Accumulated deficit	(23,980,220 )	(26,125,414 )
Total stockholders' equity (deficit)	2,995,258	(1,451,026 )
Total liabilities and stockholders' equity (deficit)	\$10,799,444	\$2,948,702

See accompanying notes to the unaudited consolidated financial statements.



Table of Contents

IZEA, Inc.  
Consolidated Statements of Operations  
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenue	\$1,931,671	\$1,565,851	\$5,857,946	\$4,666,399
Cost of sales	692,217	499,127	1,998,406	1,846,130
Gross profit	1,239,454	1,066,724	3,859,540	2,820,269
Operating expenses:				
General and administrative	2,320,142	1,655,727	6,340,796	4,594,888
Sales and marketing	482,045	63,436	986,195	272,695
Total operating expenses	2,802,187	1,719,163	7,326,991	4,867,583
Loss from operations	(1,562,733 )	(652,439 )	(3,467,451 )	(2,047,314 )
Other income (expense):				
Interest expense	(5,519 )	(14,439 )	(20,587 )	(52,435 )
Loss on exchange of warrants and debt	—	(93,482 )	—	(94,214 )
Change in fair value of derivatives and notes payable carried at fair value, net	2,250,344	(215,092 )	5,625,555	(558,869 )
Other income (expense), net	3,278	150	7,677	230
Total other income (expense)	2,248,103	(322,863 )	5,612,645	(705,288 )
Net income (loss)	\$685,370	\$(975,302 )	\$2,145,194	\$(2,752,602 )
Weighted average common shares outstanding – basic	57,350,743	12,996,717	50,584,635	9,034,361
Basic income (loss) per common share	\$0.01	\$(0.08 )	\$0.04	\$(0.30 )
Weighted average common shares outstanding – diluted	69,428,993	12,996,717	63,663,192	9,034,361
Diluted income (loss) per common share	\$0.01	\$(0.08 )	\$0.03	\$(0.30 )

See accompanying notes to the unaudited consolidated financial statements.

2

---

Table of Contents

IZEA, Inc.

Consolidated Statement of Stockholders' Equity (Deficit)  
(Unaudited)

	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In Capital	Deficit	Stockholders' Equity (Deficit)
Balance, December 31, 2013	22,560,653	\$2,256	\$24,672,132	\$(26,125,414 )	\$(1,451,026 )
Sale of common stock, net of offering costs	34,285,728	3,429	10,928,759	—	10,932,188
Fair value of warrants issued	—	—	(12,382,216 )	—	(12,382,216 )
Fair value of 2013 PPM warrants reclassified from liability to equity	—	—	3,166,482	—	3,166,482
Exercise of stock options & warrants	451,250	45	112,755	—	112,800
Stock purchase plan subscriptions	—	—	724	—	724
Stock issued for payment of services	200,000	20	82,090	—	82,110
Stock-based compensation	—	—	389,002	—	389,002
Net income	—	—	—	2,145,194	2,145,194
Balance, September 30, 2014	57,497,631	\$5,750	\$26,969,728	\$(23,980,220 )	\$2,995,258



See accompanying notes to the unaudited consolidated financial statements.

3

---

Table of Contents

IZEA, Inc.

Consolidated Statements of Cash Flows  
(Unaudited)

	Nine Months Ended September 30,	
	2014	2013
Cash flows from operating activities:		
Net income (loss)	\$2,145,194	\$(2,752,602 )
Adjustments to reconcile net income (loss) to net cash used for operating activities:		
Depreciation	65,683	36,377
Amortization of software development costs and other assets	103,529	33,636
Loss on sale of furniture and equipment	16,192	—
Bad debt expense	—	24,018
Stock-based compensation	389,002	359,251
Stock issued or to be issued for payment of services	147,860	416,768
Loss on exchange of warrants and debt	—	94,214
Change in fair value of derivatives and notes payable carried at fair value, net	(5,625,555 )	558,869
Cash provided by (used for):		
Accounts receivable	183,968	(760,864 )
Prepaid expenses and other current assets	(454,839 )	17,716
Accounts payable	(174,386 )	(421,790 )
Accrued expenses	30,326	273,061
Unearned revenue	(156,156 )	120,779
Deferred rent	60,508	—
Net cash used for operating activities	(3,268,674 )	(2,000,567 )
Cash flows from investing activities:		
Purchase of equipment	(159,974 )	(15,064 )
Increase in software development costs	(206,529 )	(244,878 )
Security deposits	(11,067 )	1,097
Net cash used for investing activities	(377,570 )	(258,845 )
Cash flows from financing activities:		
Proceeds from issuance of notes payable, net	—	1,439,798
Proceeds from issuance of common stock and warrants, net	10,932,912	2,032,145
Proceeds from exercise of stock options & warrants	112,800	—
Payments on notes payable and capital leases	(49,602 )	(206,789 )
Net cash provided by financing activities	10,996,110	3,265,154
Net increase in cash and cash equivalents	7,349,866	1,005,742
Cash and cash equivalents, beginning of year	530,052	657,946
Cash and cash equivalents, end of period	\$7,879,918	\$1,663,688
Supplemental cash flow information:		
Cash paid during period for interest	\$11,870	\$9,902
Non-cash financing and investing activities:		

Edgar Filing: IZEA, Inc. - Form 10-Q

Fair value of 2013 PPM warrants reclassified from liability to equity	\$3,166,482	\$—
Fair value of warrants issued	\$12,382,216	\$2,352,108
Conversion of notes payable into common stock	\$—	\$1,501,229
Acquisition of assets through capital lease	\$41,339	\$55,369
See accompanying notes to the unaudited consolidated financial statements.		

4

---

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

## NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Unaudited Interim Financial Information

The accompanying consolidated balance sheet as of September 30, 2014, the consolidated statements of operations for the three and nine months ended September 30, 2014 and 2013, the consolidated statement of stockholders' equity (deficit) for the nine months ended September 30, 2014 and the consolidated statements of cash flows for the nine months ended September 30, 2014 and 2013 are unaudited but include all adjustments that are, in the opinion of management, necessary for a fair presentation of our financial position at such dates and our results of operations and cash flows for the periods then ended in conformity with U.S. generally accepted accounting principles ("U.S. GAAP"). The consolidated balance sheet as of December 31, 2013 has been derived from the audited consolidated financial statements at that date but, in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC"), does not include all of the information and notes required by U.S. GAAP for complete financial statements. Operating results for the nine months ended September 30, 2014 are not necessarily indicative of results that may be expected for the entire fiscal year. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended December 31, 2013 included in the Company's Annual Report on Form 10-K filed with the SEC on March 25, 2014.

### Nature of Business

IZEA, Inc. (the "Company") was founded in February 2006 under the name PayPerPost, Inc. and became a public company incorporated in the state of Nevada in May 2011. The Company is headquartered in Winter Park, Florida with offices in Chicago and Los Angeles and a sales presence in New York, London and Detroit.

The Company is a leader and pioneer in the social sponsorship space, creating the first social sponsorship marketplace in 2006 with the launch of PayPerPost.com. Social sponsorship is when a company compensates a social media publisher or influencer such as a blogger or tweeter ("creators") to share sponsored content with their social network audience. This sponsored content is shared within the body of a content stream, a practice known as "native advertising." The Company generates its revenue primarily through the sale of sponsorship campaigns to its advertisers. The Company fulfills these campaigns through its platforms by utilizing its network of creators to complete sponsorship opportunities for its advertisers. The Company also generates revenue from the posting of targeted display advertising and from various service fees.

The Company currently operates multiple online properties including SocialSpark.com and SponsoredTweets.com. In March 2014, the Company launched The IZEA Exchange (IZEAx), a social sponsorship platform designed to replace its older platforms with current technology and provide the infrastructure necessary to support a larger and more diverse social sponsorship ecosystem. IZEAx is designed to provide a unified ecosystem that enables the creation of multiple types of content including blog posts, status updates, videos and photos through a wide variety of social channels including blogs, Twitter, Facebook, Instagram, Tumblr and LinkedIn, among others. The Company is in the process of sunsetting all of its older platforms by the end of 2014 and moving all of its transactions to IZEAx.

### Principles of Consolidation

The consolidated financial statements include the accounts of IZEA, Inc. and its wholly-owned subsidiary, IZEA Innovations, Inc. (together, the "Company"). All significant intercompany balances and transactions have been eliminated in consolidation.

### Cash and Cash Equivalents

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

#### Accounts Receivable and Concentration of Credit Risk

Accounts receivable are customer obligations due under normal trade terms. Uncollectibility of accounts receivable is not significant since most customers are bound by contract and are required to fund the Company for all the costs of an “opportunity,” defined as an order created by an advertiser for a creator to write about the advertiser’s product. If a portion of the account balance is deemed uncollectible, the Company will either write-off the amount owed or provide a reserve based on the uncollectible portion of the account. Management determines the collectibility of accounts by regularly evaluating individual customer receivables and considering a customer’s financial condition, credit history and current economic conditions. The Company does not have a reserve for doubtful accounts as of September 30, 2014 and December 31, 2013. Management believes that this estimate is reasonable, but there can be no assurance that the estimate will not change as a result of a change in economic conditions or business conditions within the industry, the individual customers or the Company. Any adjustments to this account are reflected in the consolidated statements of operations as a general and administrative expense. Bad debt expense was less than 1% of revenue for the nine months ended September 30, 2014 and 2013.

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

Concentrations of credit risk with respect to accounts receivable are typically limited because a large number of geographically diverse customers make up the Company's customer base, thus spreading the trade credit risk. The Company also controls credit risk through credit approvals, credit limits and monitoring procedures. The Company performs credit evaluations of its customers but generally does not require collateral to support accounts receivable. At September 30, 2014, there were no customers that accounted for more than 10% of the Company's accounts receivable in the aggregate. At December 31, 2013, the Company had two customers which accounted for 23% of total accounts receivable in the aggregate. The Company had no customers that accounted for more than 10% of the Company's revenue during the three months ended September 30, 2014 and two customers that accounted for 33% of its revenue during the three months ended September 30, 2013. The Company had one customer that accounted for 10% of its revenue during the nine months ended September 30, 2014 and one customer that accounted for 13% of its revenue during the nine months ended September 30, 2013.

Property and Equipment

Depreciation and amortization is computed using the straight-line method and half-year convention over the estimated useful lives of the assets as follows:

Computer Equipment	3 years
Software Development Costs	3 years
Office Equipment	3 - 10 years
Furniture and Fixtures	5 - 10 years
Leasehold Improvements	5 years

Major additions and improvements are capitalized, while replacements, maintenance and repairs, which do not improve or extend the life of the respective assets, are expensed as incurred. When assets are retired or otherwise disposed of, related costs and accumulated depreciation and amortization are removed and any gain or loss is recognized in net income or loss.

Software Development Costs

Throughout 2013 and 2014, the Company developed a new web-based advertising exchange platform called the IZEA Exchange (IZEAx). IZEAx is designed to provide a unified ecosystem that enables the creation of multiple types of content including blog posts, status updates, videos and photos through a wide variety of social channels including blogs, Twitter, Facebook, Instagram, Tumblr and LinkedIn, among others. This platform will be utilized both internally and externally to facilitate native advertising campaigns on a greater scale. In accordance with ASC 350-40, Internal Use Software and ASC 985-730, Computer Software Research and Development, research phase costs should be expensed as incurred and development phase costs including direct materials and services, payroll and benefits and interest costs may be capitalized. The Company capitalized \$568,875 in direct materials, payroll and benefit costs to software development costs in the consolidated balance sheet as of September 30, 2014. The Company determined that on April 15, 2013, the project became technologically feasible and the development phase began. On March 17, 2014, the Company launched a public beta of IZEA.com powered by IZEAx and began amortizing the costs over three years.

Revenue Recognition

The Company derives its revenue from three sources: revenue from an advertiser for the use of the Company's network of social media content creators to fulfill advertiser sponsor requests for a blog post, tweet, click or action ("Sponsored Revenue"), revenue from the posting of targeted display advertising ("Media Revenue") and revenue derived from various service fees charged to advertisers and creators ("Service Fee Revenue"). Sponsored revenue is recognized and considered earned after an advertiser's opportunity is posted on the Company's online platform and their request was completed and content listed, as applicable, by the Company's creators for a requisite period of time.

The requisite period ranges from 3 days for an action or tweet to 30 days for a blog. Advertisers may prepay for services by placing a deposit in their account with the Company. The deposits are typically paid by the advertiser via check, wire transfer or credit card. Deposits are recorded as unearned revenue until earned as described above. Media Revenue is recognized and considered earned when the Company's creators place targeted display advertising in blogs. Service fees charged to advertisers are primarily related to inactivity fees for dormant accounts and fees for additional services outside of sponsored revenue. Service fees charged to creators include upgrade account fees for obtaining greater visibility to advertisers in advertiser searches in our platforms, early cash-out fees if a creator wishes to take proceeds earned for services from their account when the account balance is below certain minimum balance thresholds and inactivity fees for dormant accounts. Service fees are recognized immediately when the maintenance or enhancement service is performed for an advertiser or creator. All of the Company's revenue is generated through the rendering of services and is recognized under the general guidelines of SAB Topic 13 A.1 which states that revenue will be recognized when it is realized or realizable and earned. The Company considers its revenue as generally realized or realizable and earned once (i) persuasive evidence of an arrangement exists, (ii) services have

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

been rendered, (iii) the price to the advertiser or customer is fixed (required to be paid at a set amount that is not subject to refund or adjustment) and determinable, and (iv) collectibility is reasonably assured. The Company records revenue on the gross amount earned since it generally is the primary obligor in the arrangement, establishes the pricing and determines the service specifications.

#### Advertising Costs

Advertising costs are charged to expense as they are incurred, including payments to contact creators to promote the Company. Advertising expense charged to operations for the three months ended September 30, 2014 and 2013 were approximately \$347,000 and \$12,000, respectively. Advertising expense charged to operations for the nine months ended September 30, 2014 and 2013 were approximately \$635,000 and \$56,000, respectively. Advertising costs are included in sales and marketing expense in the accompanying consolidated statements of operations.

#### Deferred Rent

The Company's operating lease for its office facilities contains predetermined fixed increases of the base rental rate during the lease term which was recognized as rental expense on a straight-line basis over the lease term which ends in April 2019, but is renewable for one additional year until April 2020. The Company records the difference between the amounts charged to operations and amounts payable under the lease as deferred rent in the accompanying consolidated balance sheets.

#### Income Taxes

The Company has not recorded current income tax expense due to the generation of net operating losses. Deferred income taxes are accounted for using the balance sheet approach which requires recognition of deferred tax assets and liabilities for the expected future consequences of temporary differences between the financial reporting basis and the tax basis of assets and liabilities. A valuation allowance is provided when it is more likely than not that a deferred tax asset will not be realized.

The Company identifies and evaluates uncertain tax positions, if any, and recognizes the impact of uncertain tax positions for which there is a less than more-likely-than-not probability of the position being upheld when reviewed by the relevant taxing authority. Such positions are deemed to be unrecognized tax benefits and a corresponding liability is established on the balance sheet. The Company has not recognized a liability for uncertain tax positions. If there were an unrecognized tax benefit, the Company would recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. The Company's tax years, subject to examination by the Internal Revenue Service, generally remain open for three years from the date of filing.

#### Derivative Financial Instruments

Derivative financial instruments are defined as financial instruments or other contracts that contain a notional amount and one or more underlying factor (e.g., interest rate, security price or other variable), require no initial net investment and permit net settlement. Derivative financial instruments may be free-standing or embedded in other financial instruments. Further, derivative financial instruments are initially, and subsequently, measured at fair value and recorded as liabilities or, in rare instances, assets. The Company accounts for derivative instruments in accordance with ASC 815, Derivatives and Hedging ("ASC 815"), which requires additional disclosures about the Company's objectives and strategies for using derivative instruments, how the derivative instruments and related hedged items are accounted for, and how the derivative instruments and related hedging items affect the financial statements. The Company does not use derivative instruments to hedge exposures to cash flow, market or foreign currency risk. Terms of convertible debt and equity instruments are reviewed to determine whether or not they contain embedded derivative instruments that are required under ASC 815 to be accounted for separately from the host contract, and recorded on the balance sheet at fair value. The fair value of derivative liabilities, if any, is required to be revalued at each reporting date, with corresponding changes in fair value recorded in current period operating results. Pursuant to ASC



815, an evaluation of specifically identified conditions is made to determine whether the fair value of warrants issued is required to be classified as equity or as a derivative liability.

The Company records a beneficial conversion feature (“BCF”) related to the issuance of convertible debt and equity instruments that have conversion features at fixed rates that are in-the-money when issued, and the fair value of warrants issued in connection with those instruments. The BCF for the convertible instruments is recognized and measured by allocating a portion of the proceeds to warrants, based on their relative fair value, and as a reduction to the carrying amount of the convertible instrument equal to the intrinsic value of the conversion feature. The discounts recorded in connection with the BCF and warrant valuation are recognized (a) for convertible debt as interest expense over the term of the debt, using the effective interest method or (b) for preferred stock as dividends at the time the stock first becomes convertible.

#### Fair Value of Financial Instruments

The Company’s financial instruments are recorded at fair value. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

an orderly transaction between market participants on the measurement date. The valuation techniques are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect certain market assumptions. There are three levels of inputs that may be used to measure fair value:

Level 1 – Valuation based on quoted market prices in active markets for identical assets and liabilities.

Level 2 – Valuation based on quoted market prices for similar assets and liabilities in active markets.

Level 3 – Valuation based on unobservable inputs that are supported by little or no market activity, therefore requiring management's best estimate of what market participants would use as fair value.

Fair value estimates discussed herein are based upon certain market assumptions and pertinent information available to management. The Company does not have any Level 1 or 2 financial assets or liabilities. The Company's Level 3 financial liabilities measured at fair value consisted of a warrant liability as of September 30, 2014 (see Note 3).

Significant unobservable inputs used in the fair value measurement of the warrants include the estimated term.

Significant increases (decreases) in the estimated remaining period to exercise would result in a significantly higher (lower) fair value measurement. In developing our credit risk assumption used in the fair value of warrants, consideration was made of publicly available bond rates and US Treasury Yields. However, since the Company does not have a formal credit-standing, management estimated its standing among various reported levels and grades for use in the model. During all periods, management estimated that the Company's standing was in the speculative to high-risk grades (BB- to CCC in the Standard and Poor's Rating). A significant increase (decrease) in the risk-adjusted interest rate could result in a significantly lower (higher) fair value measurement.

The respective carrying value of certain on-balance-sheet financial instruments approximated their fair values due to the short-term nature of these instruments. These financial instruments include cash and cash equivalents, accounts receivable, accounts payable, unearned revenue and accrued expenses. Unless otherwise disclosed, the fair value of the Company's capital lease obligations approximate their carrying value based upon current rates available to the Company.

#### Stock-Based Compensation

Stock-based compensation cost related to stock options granted under the May 2011 Equity Incentive Plan and August 2011 B Equity Incentive Plan (together, the "2011 Equity Incentive Plans") (see Note 4) is measured at grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period. The Company estimates the fair value of each option award on the date of grant using a Black-Scholes option-pricing model that uses the assumptions noted in the table below. The Company estimates the fair value of its common stock using the closing stock price of its common stock as quoted in the OTCQB marketplace on the date of the agreement. The Company estimates the volatility of its common stock at the date of grant based on the volatility of comparable peer companies that are publicly traded and have had a longer trading history than itself. The Company determines the expected life based on historical experience with similar awards, giving consideration to the contractual terms, vesting schedules and post-vesting forfeitures. The Company uses the risk-free interest rate on the implied yield currently available on U.S. Treasury issues with an equivalent remaining term approximately equal to the expected life of the award. The Company has never paid any cash dividends on its common stock and does not anticipate paying any cash dividends in the foreseeable future. The Company used the following assumptions for options granted under the 2011 Equity Incentive Plans during the three and nine months ended September 30, 2014 and 2013:

2011 Equity Incentive Plans Assumptions	Three Months Ended		Nine Months Ended	
	September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013
Expected term	5 years	10 years	5 years	9 years
Weighted average volatility	40.37%	51.72%	40.83%	52.02%

Edgar Filing: IZEA, Inc. - Form 10-Q

Weighted average risk free interest rate	1.75%	2.74%	1.71%	2.27%
Expected dividends	—	—	—	—

The Company estimates forfeitures when recognizing compensation expense and this estimate of forfeitures is adjusted over the requisite service period based on the extent to which actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures are recognized through a cumulative catch-up adjustment, which is recognized in the period of change, and also impact the amount of unamortized compensation expense to be recognized in future periods. Average expected forfeiture rates were 3.79% and 50.21% during the three months ended September 30, 2014 and 2013, respectively. Average expected forfeiture rates were 7.29% and 50.21% during the nine months ended September 30, 2014 and 2013, respectively.

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

#### Non-Employee Stock-Based Compensation

The Company's accounting policy for equity instruments issued to consultants and vendors in exchange for goods and services follows the provisions of ASC 505, "Equity-Based Payments to Non-Employees." The measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant or vendor's performance is complete. The fair value of equity instruments issued to consultants that vest immediately is expensed when issued. The fair value of equity instruments issued to consultants that have future vesting and are subject to forfeiture if performance does not occur is recognized as expense over the vesting period. Fair values for the unvested portion of issued instruments are adjusted each reporting period. The change in fair value is recorded to additional paid-in capital. Stock-based compensation related to non-employees is accounted for based on the fair value of the related stock or the fair value of the services, whichever is more readily determinable.

#### Segment Information

The Company does not identify separate operating segments for management reporting purposes. The results of operations are the basis on which management evaluates operations and makes business decisions.

#### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### Recent Accounting Pronouncements

There are several new accounting pronouncements issued by the Financial Accounting Standards Board ("FASB") which are not yet effective. Management does not believe any of these accounting pronouncements will have a material impact on the Company's financial position or operating results.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP.

The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). The Company is currently evaluating the impact of the adoption of ASU 2014-09 on its consolidated financial statements and has not yet determined the method by which it will adopt the standard in 2017.

#### Reclassifications

Certain items have been reclassified in the 2013 financial statements to conform to the 2014 presentation.

#### NOTE 2. NOTES PAYABLE

##### Convertible Notes Payable

**\$550,000 Note Payable:**

On February 3, 2012, the Company issued a senior secured promissory note in the principal amount of \$550,000 less an original issuance discount (OID) of \$50,000. The holders were permitted to convert the outstanding principal amount of the note at a conversion price of 90% of the closing price of the Company's common stock. Upon initial recording of the note, the Company determined that the embedded conversion option (ECO) required bifurcation from the host instrument and classification as a liability at fair value. The initial fair value of the ECO of \$12,151 was subsequently remeasured at fair value each reporting period. The OID was subject to amortization, through charges to interest expense, over the term to maturity or conversion using the effective interest method.

From October 2012 through December 2012, the holders of this promissory note converted \$437,850 of note value into 2,069,439 shares of common stock at an average conversion rate of \$.21 per share. On February 4, 2013, the Company satisfied all of its

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

remaining obligations under this note when the noteholders converted the final balance owed of \$112,150 into 773,983 shares of common stock at an average conversion rate of \$.145 per share.

**\$75,000 Notes Payable:**

On May 4, 2012, the Company issued an unsecured 30-day promissory note to two of its existing shareholders in the principal amount of \$75,000. In June 2012, the note was extended until December 4, 2012 and the parties agreed that the noteholders could convert the note at any time on or before the maturity date into shares of common stock at a conversion price equal to the lower of (i) \$5.00 per share or (ii) 90% of the then market price based on a volume weighted average price per share of the Company's common stock for the ten trading days prior to the conversion date. Upon initial recording of the note, the Company determined that the embedded conversion option (ECO) required bifurcation from the host instrument and classification as a liability at fair value. The initial fair value of the ECO of \$15,625 was subsequently remeasured at fair value each reporting period. The note bore interest at a rate of 8% per annum. The noteholders did not elect to convert this note and the Company was not able to pay the balance owed upon its maturity on December 4, 2012. Therefore, the conversion feature expired and the note was in default bearing interest at the default rate of 18% per annum. On August 15, 2013, the Company satisfied all of its remaining obligations under this note when the noteholders converted the \$75,000 in principal, plus \$12,366 of accrued interest, into 349,464 shares of common stock and a like number of warrants on the same terms and conditions as other investors in its 2013 Private Placement discussed in Note 4.

**Bridge Bank Credit Agreement**

On March 1, 2013, the Company entered into a secured credit facility agreement with Bridge Bank, N.A. of San Jose, California. Pursuant to this agreement, the Company may submit requests for funding up to 80% of its eligible accounts receivable up to a maximum total outstanding advanced amount of \$1.5 million. This agreement is secured by the Company's accounts receivable and substantially all of the Company's other assets. The agreement renews annually and requires the Company to pay an annual facility fee of \$5,000 (0.5% of the credit facility) and an annual due diligence fee of \$1,000. Interest accrues on the advances at the prime rate plus 2% per annum. The default rate of interest is prime plus 7%. As of September 30, 2014, the Company had no advances outstanding under this agreement. The Company incurred \$37,301 in costs related to this loan acquisition including the fair value of warrants issued of \$7,209. These costs have been capitalized in the Company's consolidated balance sheet as deferred finance costs and are being amortized to interest expense over one year.

**Brian Brady Promissory Notes**

On April 11, 2013 and May 22, 2013, the Company entered into unsecured loan agreements with Brian W. Brady, a director of the Company. Pursuant to these agreements, the Company received short-term loans totaling \$750,000 due on May 31, 2013. The notes bore interest at 7% per annum with a default rate of interest at 12% based on a 360-day year. On May 31, 2013, the Company signed an extension and conversion agreement that extended the maturity date to August 31, 2013. Additionally, the parties agreed to allow these notes and all accrued interest thereon to be converted into equity upon closing of the next private placement on the same terms and conditions that will be applicable to other investors in the private placement. In consideration for the extension and conversion agreement, the Company issued Mr. Brady a warrant to purchase 1,000,000 shares of the Company's common stock at \$0.25 per share for a period of 5 years. The Company also agreed that upon the first closing of its next private placement it would issue Mr. Brady an additional warrant to purchase 3,187,500 shares of the Company's common stock at \$0.25 per share for a period of five years and 1,687,500 restricted stock to be issued upon the earlier of two years after the closing or completion of a transaction resulting in a change of control of the Company. The Company accounted for the extension and conversion agreement associated with these loans as a substantial modification on May 31, 2013 (see Note 3 under Convertible Notes-Carried at Fair Value).

On June 7, June 14, July 25 and August 12, 2013, the Company entered into additional unsecured loan agreements with Mr. Brady. Pursuant to these agreements, the Company received short-term loans totaling \$520,000 due on August 31, 2013. The notes bore interest at 7% per annum with a default rate of interest at 12% based on a 360-day year.

On August 15, 2013, Mr. Brady converted the \$1,270,000.00 of total principal, plus \$19,252 of accrued interest, into 5,157,008 shares of common stock on the same terms and conditions as were applicable to the other investors in the 2013 Private Placement discussed in Note 4. There were no further amounts owed to Mr. Brady after the conversion.

During the three and nine months ended September 30, 2013, interest expense on all the notes amounted to \$3,998 and \$22,397, respectively. Direct finance costs allocated to the embedded derivatives were expensed in full upon issuance of the notes. Direct finance costs allocated to the notes are subject to amortization, through charges to interest expense, using the effective interest method. During the three months ended September 30, 2014 and 2013, interest expense related to the amortization of finance costs amounted to \$1,500 and \$7,826, respectively. During the nine months ended September 30, 2014 and 2013, interest expense related to the amortization of finance costs amounted to \$8,717 and \$20,137, respectively.

IZEA, Inc.  
Notes to the Unaudited Consolidated Financial Statements

NOTE 3. DERIVATIVE FINANCIAL INSTRUMENTS

The Company evaluates its convertible debt, warrants or other contracts to determine if those contracts or embedded components of those contracts qualify as derivatives to be separately accounted for in accordance with paragraph 810-10-05-4 of the FASB Accounting Standards Codification and paragraph 815-40-25 of the FASB Accounting Standards Codification. The result of this accounting treatment is that the fair value of the embedded derivative is marked-to-market each balance sheet date and recorded as a liability. In the event that the fair value is recorded as a liability, the change in fair value is recorded in the Statement of Operations as other income or expense. Upon registration, conversion or exercise, as applicable, of a derivative instrument, the instrument is marked to fair value at the conversion date and then that fair value is reclassified to equity.

The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is re-assessed at the end of each reporting period. Equity instruments that are initially classified as equity that become subject to reclassification are reclassified to liability at the fair value of the instrument on the reclassification date. Derivative instrument liabilities will be classified in the balance sheet as current or non-current based on whether or not net-cash settlement of the derivative instrument is expected within 12 months after the balance sheet date.

Warrant Liability

2014 Activity:

On February 21, 2014, the Company issued five-year warrants to purchase 17,142,864 shares of the Company's common stock at an exercise price of \$0.35 per share and five-year warrants to purchase 17,142,864 shares of the Company's common stock at an exercise price of \$0.50 per share pursuant to the terms of the Securities Purchase Agreements entered into in connection with its 2014 Private Placement (see Note 4 for further details). As part of the transaction, the Company also issued a five-year warrant to purchase up to 750,511 shares of the Company's common stock at an exercise price of \$0.35 per share and a five-year warrant to purchase up to 750,511 shares of the Company's common stock at an exercise price of \$0.50 per share to the placement agent.

The Company determined that these warrants require classification as a liability due to certain registration rights and listing requirements that required the Company to file a registration statement with the SEC for purposes of registering the resale of the shares underlying these warrants. The warrants also require classification as a liability due to provisions for potential exercise price adjustments. The Company determined that the fair value of these warrants on their issuance date on February 21, 2014 was \$12,382,216. The fair value and outstanding derivative warrant liability related to these warrant shares as of September 30, 2014 was \$5,421,694. The Company filed a registration statement on Form S-1 related to these shares on April 7, 2014, which was declared effective by the SEC on May 14, 2014. Although the warrants are currently registered, they still require liability classification due to the provisions for potential exercise price adjustments.

2013 Activity:

In February 2013, pursuant to a private transaction with a warrant holder, the Company redeemed a warrant to purchase 5,001 shares of common stock for the same number of shares without the Company receiving any further cash consideration. The redemption was treated as an exchange wherein the difference between the fair value of the newly issued common stock and the carrying value of the warrant received in the exchange was recognized as a loss on exchange of warrants in the amount of \$732 during the nine months ended September 30, 2013.

On May 4, 2012, the Company issued an unsecured 30-day promissory note to two of its existing shareholders in the principal amount of \$75,000 (See Note 2). On August 15, 2013, the Company satisfied all of its remaining obligations under this note when the noteholders converted the \$75,000 in principal, plus \$12,366 of accrued interest, into 349,464 shares of common stock and a like number of warrants on the same terms and conditions as other investors in



its 2013 Private Placement discussed in Note 4. Since there was no conversion provision in effect on the note at the time, the conversion was treated as an exchange wherein the difference between the fair value of the newly issued common stock and the carrying value of the note received in the exchange was recognized as a loss on exchange of debt in the amount of \$93,482 during the three and nine months ended September 30, 2013.

From August 15, 2013 through September 23, 2013, the Company issued five-year warrants to purchase 7,118,236 shares of its common stock at an exercise price of \$0.25 per share and five-year warrants to purchase 7,118,236 shares of its common stock at an exercise price of \$0.50 per share pursuant to the terms of the Securities Purchase Agreements entered into in connection with its 2013 Private Placement (see Note 4 for further details). The Company determined that these warrants require classification as a liability due to certain registration rights in the agreements that required the Company to file a registration statement with the SEC for purposes of registering the resale of the shares underlying these warrants. The Company determined that the fair value of these warrants on their issuance date was \$2,344,899. The Company filed a registration statement on Form S-1 on October 16,

IZEA, Inc.

## Notes to the Unaudited Consolidated Financial Statements

2013, which was declared effective by the SEC on November 8, 2013 for the registration of 174,732 of these warrant shares. The Company filed a registration statement on Form S-1 related to the remaining warrant shares on July 17, 2014, which was declared effective by the SEC on July 29, 2014. The fair value and outstanding derivative warrant liability related to these warrant shares as of July 29, 2014 was \$3,166,482. As a result of the registration, the warrants no longer require liability classification and the fair value was reclassified to equity in July 2014.

## 2012 Activity:

The Company determined that 110,000 warrant shares issued in its September 2012 public offering still require classification as a liability due to certain registration rights and listing requirements in the agreements. The fair value and outstanding derivative warrant liability related to these warrant shares as of September 30, 2014 was \$1,430.

## 2011 Activity:

The Company determined that 13,554 warrant shares remaining from its May 2011 Offering and 250 warrant shares issued in July 2011 for a customer list acquisition still require classification as a liability due to certain registration rights and listing requirements in the agreements. The fair value and outstanding derivative warrant liability related to these warrant shares as of September 30, 2014 was \$0.

During the three months ended September 30, 2014 and 2013, the Company recorded a gain of \$2,250,344 and of \$207,462, respectively, due to the change in the fair value of its warrant liability. During the nine months ended September 30, 2014 and 2013, the Company recorded a gain of \$5,625,555 and of \$207,682, respectively, due to the change in the fair value of its warrant liability.

The following table summarizes the Company's activity and fair value calculations of its derivative warrants for the nine months ended September 30, 2014 and for the year ended December 31, 2013:

	Linked Common Shares to Derivative Warrants	Warrant Liability	
Balance, December 31, 2012	128,350	\$2,750	
Issuance of warrants to investors in 2013 Private Placement	14,236,472	2,344,899	
Exchange of warrants for common stock	(4,546	)—	
Change in fair value of derivatives	—	(514,704	)
Balance, December 31, 2013	14,360,276	\$1,832,945	
Issuance of warrants to investors in 2014 Private Placement	35,786,750	12,382,216	
Reclassification of fair value of 2013 Private Placement warrants to equity	(14,236,472	)(3,166,482	)
Change in fair value of derivatives	—	(5,625,555	)
Balance, September 30, 2014	35,910,554	\$5,423,124	

The Company's warrants were valued on the applicable dates using a Binomial Lattice Option Valuation Technique ("Binomial"). Significant inputs into this technique as of August 15, 2013 - September 23, 2013, December 31, 2013, February 21, 2014, July 29, 2014 and September 30, 2014 are as follows:

Binomial Assumptions	August 15, 2013 - September 23, 2013	December 31, 2013	February 21, 2014	July 29, 2014	September 30, 2014
Fair market value of asset <sup>(1)</sup>	\$0.28-\$0.37	\$0.30	\$0.58	\$0.45	\$0.37
Exercise price	\$0.25-\$0.50	\$0.25-\$1.25	\$0.35-\$0.50	\$0.25-\$0.50	\$0.35-\$1.25
Term <sup>(2)</sup>	5.0 years	3.7 - 4.7 years	5.0 years	4.1 - 4.2 years	2.9 - 4.4 years
Implied expected life <sup>(3)</sup>	5.0 years	3.7 - 4.7 years	5.0 years	4.1 - 4.2 years	2.9 - 4.4 years
Volatility range of inputs <sup>(4)</sup>	48.46%--81.72%	40.63%--78.73%	60%	40%--76%	41%--74%

Edgar Filing: IZEA, Inc. - Form 10-Q

Equivalent volatility <sup>(3)</sup>	56.57%--57.55%	55%--56%	60%	53%	45%--53%
Risk-free interest rate range of inputs <sup>(5)</sup>	0.04%--1.72%	0.38%--1.75%	1.56%	1.35%	1.07%--1.78%
Equivalent risk-free interest rate <sup>(3)</sup>	0.56%--0.69%	0.78%--1.75%	1.56%	1.35%	1.07%--1.78%

12

---

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

- (1) The fair market value of the asset was determined by using the Company's closing stock price as reflected in the over-the-counter market.
- (2) The term is the contractual remaining term, allocated among twelve equal intervals for purposes of calculating other inputs, such as volatility and risk-free rate.
- (3) The implied expected life, and equivalent volatility and risk-free interest rate amounts are derived from the binomial.
- (4) The Company does not have a market trading history upon which to base its forward-looking volatility. Accordingly, the Company selected peer companies that provided a reasonable basis upon which to calculate volatility for each of the intervals described in (2), above.
- (5) The risk-free rates used for inputs represent the yields on zero coupon U.S. Government Securities with periods to maturity consistent with the intervals described in (2), above.

Convertible Notes-Carried At Fair value

On May 31, 2013, the Company signed a loan extension and conversion agreement with Brian W. Brady, a director of the Company, that extended the due date on its \$750,000 notes payable to August 31, 2013 and added a conversion feature in which the notes and all accrued interest thereon will be converted into equity upon the closing of the next private placement on the same terms and conditions that will be applicable to other investors in the future financing. In consideration for the extension and conversion agreement, the Company issued Mr. Brady a warrant to purchase 1,000,000 shares of the Company's common stock at \$0.25 per share for a period of five years. The Company also agreed that upon the first closing of its next private placement it would issue Mr. Brady an additional warrant to purchase 3,187,500 shares of the Company's common stock at \$0.25 per share for a period of five years and 1,687,500 restricted stock units which vest upon the earlier of two years after issuance or completion of a transaction resulting in a change of control of the Company.

The Company concluded that since the modification resulted in the addition of a conversion feature, the notes no longer met the definition of being indexed to the Company's own stock as provided in ASC 815 Derivatives and Hedging. Accordingly, the modification of these loans on May 31, 2013 resulted in a change that required either bifurcation of the embedded conversion feature or the Company could choose to record the entire fair value of the convertible notes at fair value. According to the terms of the modification, the convertible notes are required to be converted on the date the Company finalizes a future contemplated financing. Rather than choosing to value the notes based on the present value of their cash flows, it was assumed a market participant would likely consider the common stock equivalent value to be more indicative of the fair value of the notes since they will be converted and not paid in cash. Therefore, management chose to record the promissory notes at their fair value using a common stock equivalent approach, with changes in fair value being reported as "Change in the fair value of derivatives and notes payable carried at fair value, net" in the accompanying consolidated statements of operations. On August 15, 2013, Mr. Brady converted the total principal and accrued interest on the above notes into shares of common stock on the same terms and conditions as were applicable to the other investors in the 2013 Private Placement discussed in Note 4. The \$750,000 convertible notes payable was valued at \$820,202 on May 31, 2013 and \$1,586,109 on the note conversion date of August 15, 2013. This change in fair value resulted in an expense of \$422,554 and \$765,907 during the three and nine months ended September 30, 2013, respectively.

Compound Embedded Derivative

The Company concluded that the compound embedded derivative in its \$550,000 senior secured promissory note issued on February 3, 2012 required bifurcation and liability classification as derivative financial instruments because it was not considered indexed to the Company's own stock as defined in ASC 815, Derivatives and Hedging. On February 4, 2013, the Company satisfied all of its remaining obligations under its \$550,000 senior secured promissory note when the noteholders converted the final balance owed of \$112,150 into 773,983 shares of common stock at an average conversion rate of \$.145 per share. The value of the compound embedded derivative on December 31, 2012 was \$11,817 and its value on the conversion date of February 4, 2013 was \$12,461. The Company recorded the value

of the compound embedded derivative on the conversion date as a charge to additional paid-in capital. As of February 4, 2013, all convertible notes in which the conversion feature had been bifurcated and recorded at fair value, had been converted in full. The Company recorded an expense of \$644 resulting from the change in the fair value of the compound embedded derivatives during the nine months ended September 30, 2013.

NOTE 4. STOCKHOLDERS' EQUITY (DEFICIT)

Authorized Shares

13

---

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

On April 17, 2014, the Company filed a certificate of amendment to its articles of incorporation to increase the number of authorized shares of its common stock from 100,000,000 shares to 200,000,000 shares. The amendment was adopted by stockholders holding a majority of the Company's outstanding shares of common stock by written consent on April 16, 2014.

The Company also has authorized 10,000,000 shares of preferred stock with a par value of \$0.0001 per share, of which no shares are outstanding as of September 30, 2014.

#### 2014 Private Placement

On February 21, 2014, the Company completed a private placement pursuant to a Purchase Agreement dated as of February 12, 2014, for the issuance and sale of 34,285,728 shares of its common stock, at a purchase price of \$0.35 per share, for gross proceeds of approximately \$12,000,000 ("2014 Private Placement"). As part of the private placement, the investors received warrants to purchase up to 17,142,864 shares of the Company's common stock at an exercise price of \$0.35 per share and warrants to purchase up to another 17,142,864 shares of the Company's common stock at an exercise price of \$0.50 per share. The warrants expire on February 21, 2019.

The net proceeds of \$10,932,188 from the private placement, following the payment of \$1,067,812 in offering-related expenses, are being used by the Company to focus on revenue growth through the acceleration of its sales and client relations activities and marketing initiatives, establishment of strategic partnerships and continuation of technology and engineering enhancements to its platforms, as well as to fund its working capital and capital expenditure requirements. At the closing of the private placement, the Company paid Craig-Hallum Capital Partners LLC, the exclusive placement agent for the private placement, cash compensation of \$814,850 and two five-year warrants, one warrant to purchase up to 750,511 shares of the Company's common stock at an exercise price of \$0.35 per share and another warrant to purchase up to 750,511 shares of the Company's common stock at an exercise price of \$0.50 per share.

The Company agreed, pursuant to the terms of a registration rights agreement with the investors, to (i) file a shelf registration statement with respect to the resale of the shares of its common stock sold to the investors and shares of its common stock issuable upon exercise of the warrants with the SEC within the sooner of 60 days after the closing date or 10 business days after the Company filed its Annual Report on Form 10-K for the year ended December 31, 2013; (ii) use its commercially reasonable best efforts to have the shelf registration statement declared effective by the SEC as soon as possible after the initial filing, and in any event no later than 90 days after the closing date (or 120 days in the event of a full review of the shelf registration statement by the SEC); and (iii) keep the shelf registration statement effective until all registrable securities may be sold pursuant to Rule 144 under the Securities Act of 1933, without the need for current public information or other restriction. If the Company is unable to comply with any of the above covenants, it will be required to pay liquidated damages to the investors in the amount of 1% of the investors' purchase price per month until such non-compliance is cured, with such liquidated damages payable in cash. The Company filed a registration statement on Form S-1 related to these shares on April 7, 2014, which was declared effective by the SEC on May 14, 2014 (satisfying the terms of (i) and (ii) above, and on February 21, 2015, the terms of (iii) will be satisfied).

#### 2013 Private Placement

In accordance with a Private Placement Memorandum and Securities Purchase Agreement, from August 15, 2013 through September 23, 2013, the Company raised \$2,182,500 in cash through the sale of 8,730,000 shares of its common stock at a price of \$0.25 per share ("2013 Private Placement"). Additionally, the Company converted notes payable and accrued interest thereon totaling \$1,376,618 into 5,506,472 shares of its common stock at an effective price of \$0.25 per share. The Company also issued five-year warrants to purchase 7,118,236 shares of its common stock at an exercise price of \$0.25 per share and five-year warrants to purchase 7,118,236 shares of its common stock at an exercise price of \$0.50 per share. The net proceeds received from the 2013 Private Placement were used for general working capital purposes.

Pursuant to the terms of the Securities Purchase Agreement in the 2013 Private Placement, the Company filed a registration statement on Form S-1 with the SEC on October 16, 2013, which was declared effective by the SEC on November 8, 2013 for the registration of 8,730,000 shares of common stock and 174,732 shares underlying the warrants. The Company filed a registration statement on Form S-1 related to the remaining warrant shares on July 17, 2014, which was declared effective by the SEC on July 29, 2014. In July 2014, 450,000 of the \$0.25 warrants were exercised for total proceeds of \$112,500.

#### Stock Options

In May 2011, the Board of Directors adopted the 2011 Equity Incentive Plan of IZEA, Inc. (the "May 2011 Plan"). The May 2011 Plan allows the Company to grant options as an incentive for its employees and consultants. On April 16, 2014, upon consent from holders of a majority of the Company's outstanding voting capital stock, the Company increased the number of shares of common stock available for issuance under the May 2011 Plan from 11,613,715 to 20,000,000 shares. As of September 30, 2014, the Company had 7,962,980 shares of common stock available for future grants under the May 2011 Plan.

IZEA, Inc.  
Notes to the Unaudited Consolidated Financial Statements

On August 22, 2011, the Company adopted the 2011 B Equity Incentive Plan (the "August 2011 Plan") reserving for issuance an aggregate of 87,500 shares of common stock under the August 2011 Plan. As of September 30, 2014, the Company had no shares of common stock available for future grants under the August 2011 Plan.

Under both the May 2011 Plan and the August 2011 Plan (together, the "2011 Equity Incentive Plans"), the Board of Directors determines the exercise price to be paid for the shares, the period within which each option may be exercised, and the terms and conditions of each option. The exercise price of the incentive and non-qualified stock options may not be less than 100% of the fair market value per share of the Company's common stock on the grant date. If an individual owns stock representing more than 10% of the outstanding shares, the price of each share of an incentive stock option must be equal to or exceed 110% of fair market value. Unless otherwise determined by the Board of Directors at the time of grant, the right to purchase shares covered by any options under the 2011 Equity Incentive Plans typically vest over the requisite service period as follows: 25% of options shall vest one year from the date of grant and the remaining options shall vest monthly, in equal increments over the following three years. The term of the options is up to ten years. The Company issues new shares to the optionee for any stock awards or options exercised pursuant to its equity incentive plans.

A summary of option activity under the 2011 Equity Incentive Plans for the nine months ended September 30, 2014 and the year ended December 31, 2013 is presented below:

Options Outstanding	Common Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (Years)
Outstanding at December 31, 2012	391,977	\$5.87	4.3
Granted	8,620,062	0.26	
Exercised	—	—	
Forfeited	(1,261,561)	) 0.49	
Outstanding at December 31, 2013	7,750,478	\$0.51	8.1
Granted	4,478,947	0.40	
Exercised	(1,250)	) 0.24	
Forfeited	(106,139)	) 1.06	
Outstanding at September 30, 2014	12,122,036	\$0.46	6.5
Exercisable at September 30, 2014	3,589,722	\$0.63	7.6

During the three and nine months ended September 30, 2014, options were exercised into 1,250 shares of common stock for cash proceeds of \$300. The intrinsic value of these options was \$295. During the three and nine months ended September 30, 2013, no options were exercised. The outstanding options have an aggregate intrinsic value of \$0 as of September 30, 2014. There is no aggregate intrinsic value on the exercisable options as of September 30, 2014 since the weighted average exercise price per share exceeded the fair value of \$0.37 on such date.

A summary of the nonvested stock option activity under the 2011 Equity Incentive Plans for the nine months ended September 30, 2014 and the year ended December 31, 2013 is presented below:

Nonvested Options	Common Shares	Weighted Average Grant Date Fair Value	Weighted Average Remaining Years to Vest
Nonvested at December 31, 2012	308,627	\$2.17	2.9
Granted	8,620,062	0.20	



Edgar Filing: IZEA, Inc. - Form 10-Q

Vested	(1,871,201 )	0.36	
Forfeited	(1,248,125 )	0.23	
Nonvested at December 31, 2013	5,809,363	\$0.24	3.3
Granted	4,478,947	0.15	
Vested	(1,683,306 )	0.24	
Forfeited	(72,690 )	0.24	
Nonvested at September 30, 2014	8,532,314	\$0.20	3.2

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

Stock-based compensation cost related to stock options granted under the 2011 Equity Incentive Plans is measured at grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period. The Company estimates the fair value of each option award on the date of grant using a Black-Scholes option-pricing model that uses the assumptions stated in Note 1. Total stock-based compensation expense recognized on awards outstanding during the three months ended September 30, 2014 and 2013 was \$142,252 and \$190,877, respectively. Total stock-based compensation expense recognized on awards outstanding during the nine months ended September 30, 2014 and 2013 was \$389,002 and \$359,251, respectively. Stock-based compensation expense is recorded as a general and administrative expense in the Company's consolidated statements of operations. Future compensation related to nonvested awards expected to vest of \$1,557,021 is estimated to be recognized over the weighted-average vesting period of approximately three years.

#### Employee Stock Purchase Plan

On April 16, 2014, stockholders holding a majority of the Company's outstanding shares of common stock, upon previous recommendation and approval of the Board of Directors, adopted the IZEA, Inc. 2014 Employee Stock Purchase Plan (the "ESPP") and reserved 1,500,000 shares of the Company's common stock for issuance thereunder. Any employee regularly employed by our company for 90 days or more on a full-time or part-time basis (20 hours or more per week on a regular schedule) will be eligible to participate in the ESPP. The ESPP will operate in successive six month offering periods commencing at the beginning of each fiscal year half. Each eligible employee who has elected to participate may purchase up to 10% of their annual compensation in common stock not to exceed \$21,250 annually or 20,000 shares per offering period. The purchase price will be the lower of (i) 85% of the fair market value of a share of common stock on the first trading day of the offering period or (ii) 85% of the fair market value of a share of common stock on the last trading day of the offering period. The ESPP will continue until January 1, 2024, unless otherwise terminated by the Board. As of September 30, 2014, \$724 subscription payments were received to purchase shares at the end of the offering period on December 31, 2014. No shares have been issued under the ESPP as of September 30, 2014.

#### Restricted Stock Issued for Services

On January 3, 2013, the Company issued 60,000 shares of restricted stock valued at \$15,900 pursuant to a twelve-month compensation arrangement with Mitchel J. Laskey for his service as a director and Chairman of the Company's Board of Directors.

On January 3, 2013, the Company issued 20,000 shares of restricted stock valued at \$4,820 in order to pay for a small asset purchase.

Effective January 3, 2013, the Company entered into a twelve-month agreement to pay \$4,000 per month beginning January 2013 to a firm which would provide investor relations services. In accordance with the agreement, the Company issued 100,000 shares of restricted common stock valued at \$26,500 on January 15, 2013 and agreed to issue an additional 100,000 restricted shares on or before July 15, 2013. This agreement was mutually terminated on May 1, 2013 for no further cash consideration with the Company agreeing to issue the final installment of 100,000 shares of restricted common stock valued at \$25,000 upon the termination of the agreement.

On May 16, 2013, the Company issued 30,000 shares of restricted common stock valued at \$6,000 to settle an outstanding balance with a vendor.

On September 30, 2013, the Company entered into an agreement pursuant to which it issued 823,090 shares of restricted common stock, at an effective price of \$0.35 per share, to settle a \$288,081 balance owed for legal services.

Effective October 1, 2013, the Company entered into a six-month agreement to pay \$5,000 per month to a firm which would provide investor relations services. In accordance with the agreement, the Company also issued 50,000 shares of restricted common stock valued at \$19,000 on October 1, 2013, which is being amortized over the six month service period. \$9,500 of this value was recognized as general and administrative expense on the accompanying consolidated statement of operations for the twelve months ended December 31, 2013 and during the nine months ended September 30, 2014.

The Company issued 85,661 shares of restricted common stock valued at \$25,000 to each Brian W. Brady and Dan R. Rua for their service as directors of the Company during the twelve months ended December 31, 2013.

Effective January 1, 2014, the Company entered into a one year agreement to pay \$7,500 per month and 100,000 shares of restricted stock per quarter to a firm to provide investor relations services. In accordance with the agreement, the Company issued 100,000 shares of restricted common stock valued at \$30,110 on January 1, 2014 and 100,000 shares of restricted common stock valued at \$52,000 on April 1, 2014. This agreement was canceled in June 2014 and no further amounts are owed.

IZEA, Inc.

## Notes to the Unaudited Consolidated Financial Statements

The following table contains summarized information about nonvested restricted stock outstanding during the nine months ended September 30, 2014 and the year ended December 31, 2013:

Restricted Stock	Common Shares
Nonvested at December 31, 2012	48,582
Granted	1,354,412
Vested	(1,402,994 )
Forfeited	—
Nonvested at December 31, 2013	—
Granted	326,993
Vested	(326,993 )
Forfeited	—
Nonvested at September 30, 2014	—

Total stock-based compensation expense recognized for vested restricted stock awards during the three months ended September 30, 2013 was \$301,803, of which \$1,222 is included in sales and marketing expense and \$300,581 is included in general and administrative expense. Total stock-based compensation expense recognized for vested restricted stock awards during the nine months ended September 30, 2013 was \$416,768, of which \$14,027 is included in sales and marketing expense and \$402,741 is included in general and administrative expense. Total stock-based compensation expense recognized for vested restricted stock awards during the three and nine months ended September 30, 2014 was \$18,750 and \$147,860, respectively, and is included in general and administrative expense in the consolidated statements of operations. The fair value of the services is based on the value of the Company's common stock over the term of service.

## NOTE 5. EARNINGS PER COMMON SHARE

Basic earnings per share is computed by dividing the net income or loss by the weighted-average number of shares of common stock outstanding during each period presented. Diluted earnings per share is computed by dividing the net income or loss by the weighted-average number of shares of common stock outstanding plus the additional dilutive securities that could be exercised or converted into common shares during each period presented less the amount of shares that could be repurchased using the proceeds from the exercises.

	Three Months Ended		Nine Months Ended	
	September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013
Net Income (Loss)	\$685,370	\$(975,302 )	\$2,145,194	\$(2,752,602 )
Weighted average shares outstanding - basic	57,350,743	12,996,717	50,584,635	9,034,361
Basic income (loss) per share	\$0.01	\$(0.08 )	\$0.04	\$(0.30 )
Net Income (Loss)	\$685,370	\$(975,302 )	\$2,145,194	\$(2,752,602 )
Weighted average shares outstanding - basic	57,350,743	12,996,717	50,584,635	9,034,361
Potential shares from "in-the-money" options	8,156,507	—	7,706,548	—
Potential shares from "in-the-money" warrants	28,953,989	—	25,746,789	—
Potential shares from converted restricted stock units	1,781,503	—	1,742,146	—
Less: Shares assumed repurchased under the Treasury Stock Method	(26,813,749 )	—	(22,116,926 )	—

Edgar Filing: IZEA, Inc. - Form 10-Q

Weighted average shares outstanding - diluted	69,428,993	12,996,717	63,663,192	9,034,361
Diluted income (loss) per share	\$0.01	\$(0.08	) \$0.03	\$(0.30 )

The Company excluded the following items from the above computation of diluted earnings per common share as their effect would be anti-dilutive:

IZEA, Inc.

Notes to the Unaudited Consolidated Financial Statements

	Three Months Ended		Nine Months Ended	
	September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013
Stock options	1,699,021	6,921,026	1,004,445	6,921,026
Warrants	25,135,499	18,605,999	21,727,235	18,605,999
Restricted stock units	—	1,819,400	—	1,819,400
Potential conversion of Series A convertible preferred stock	—	3,788	—	3,788
Total excluded shares	26,834,520	27,350,213	22,731,680	27,350,213

**NOTE 6. RELATED PARTY TRANSACTIONS**

During the nine months ended September 30, 2014, the Company incurred approximately \$75,000 in legal fees payable to Northwest Broadcasting, Inc. where Brian Brady, a director, is the President and Chief Executive Officer. The legal fees are included as part of the offering related expenses in the 2014 Private Placement.

**NOTE 7. COMMITMENTS & CONTINGENCIES**

From time to time, the Company may become involved in various lawsuits and legal proceedings that arise in the ordinary course of business. Litigation is, however, subject to inherent uncertainties, and an adverse result in these or other matters may harm the Company's business. Other than as described below, the Company is currently not aware of any legal proceedings or claims that it believes would or could have, individually or in the aggregate, a material adverse effect on its operations or financial position.

On October 17, 2012, Blue Calypso, Inc. filed a complaint against the Company in the U.S. District Court for the Eastern District of Texas. Blue Calypso's complaint alleges that the Company infringes on their patents related to peer-to-peer advertising between mobile communication devices and seeks unspecified damages. On July 19, 2013, Blue Calypso's case against the Company was consolidated, along with patent infringement cases against Yelp, Inc. and Foursquare Labs, Inc., into Blue Calypso, Inc. v. Groupon, Inc. for all pretrial purposes, including discovery and claim construction.

On December 16, 2013, the Patent Trial and Appeal Board's (PTAB) instituted a Covered Business Method Review (CBMR) for three of the five patents Blue Calypso asserts in its case against IZEA. In its decisions granting the CMBRs, the PTAB explained that several of Blue Calypso's asserted patents are likely invalid. In particular, the PTAB found it more likely than not that each of these three patents was invalid based on two independent grounds of anticipation, and one ground of obviousness. Additionally, the PTAB preliminarily found it more likely than not that many of the claims of one of Blue Calypso's patents were invalid due to a lack of written description. On January 17, 2014, the PTAB expanded its review to all five of Blue Calypso's assert patents. The PTAB's final decision regarding the asserted patents is expected by the end of this year. On January 16, 2014, the court granted a joint motion to stay Blue Calypso's patent infringement case until the PTAB's review of Blue Calypso's asserted patents is complete. At this stage, the Company does not have an estimate of the likelihood or the amount of any potential exposure to it. The Company believes that there is no merit to this suit and continues to vigorously defend itself against Blue Calypso's allegations.

**NOTE 8. SUBSEQUENT EVENTS**

No material events have occurred since September 30, 2014 that require recognition or disclosure in the financial statements.

## Table of Contents

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

#### Special Note Regarding Forward-Looking Information

The following discussion and analysis is provided to increase the understanding of, and should be read in conjunction with, our consolidated financial statements and related notes included elsewhere in this report. Historical results and percentage relationships among any amounts in these financial statements are not necessarily indicative of trends in operating results for any future period. This report contains “forward-looking statements.” The statements, which are not historical facts contained in this report, including this Management’s Discussion and Analysis of Financial Condition and Results of Operations, and notes to our consolidated financial statements, particularly those that utilize terminology such as “may” “will,” “should,” “expects,” “anticipates,” “estimates,” “believes,” or “plans” or comparable terminology are forward-looking statements. Such statements are based on currently available operating, financial and competitive information, and are subject to various risks and uncertainties. Future events and our actual results may differ materially from the results reflected in these forward-looking statements. Factors that might cause such a difference include, but are not limited to, our ability to raise additional funding, our ability to maintain and grow our business, variability of operating results, our ability to maintain and enhance our brand, our development and introduction of new products and services, marketing and other business development initiatives, competition in the industry, general government regulation, economic conditions, dependence on key personnel, the ability to attract, hire and retain personnel who possess the technical skills and experience necessary to meet the service requirements of our clients, our ability to protect our intellectual property, the potential liability with respect to actions taken by our existing and past employees, risks associated with international sales, and other risks described herein and in our other filings with the SEC.

All forward-looking statements in this document are based on information currently available to us as of the date of this report, and we assume no obligation to update any forward-looking statements. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results to differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

#### Company History

IZEA, Inc. was founded in February 2006 under the name PayPerPost, Inc. and became a public company incorporated in the state of Nevada in May 2011. We are headquartered in Winter Park, Florida with offices in Chicago and Los Angeles and a sales presence in New York, London and Detroit.

#### Company Overview

IZEA is a leader and pioneer in the social sponsorship space. We believe that we pioneered the concept of a marketplace for sponsorships on the social web in 2006 with the launch of PayPerPost.com and have focused on scaling our offerings ever since.

Social sponsorship is when a company compensates a social media publisher or influencer such as a blogger or tweeter (“creators”) to share sponsored content with their social network audience. This sponsored content is shared within the body of a content stream, a practice known as “native advertising.” We generate our revenue primarily through the sale of sponsorship campaigns to our advertisers. We fulfill these campaigns through our platforms by utilizing our network of creators to complete sponsorship opportunities for its advertisers. We also generate revenue from the posting of targeted display advertising and from various service fees.

We currently operate multiple online properties including SocialSpark.com and SponsoredTweets.com. In March 2014, we launched The IZEA Exchange (IZEAx), a social sponsorship platform designed to replace our older



platforms with current technology and provide the infrastructure necessary to support a larger and more diverse social sponsorship ecosystem. IZEAx is designed to provide a unified ecosystem that enables the creation of multiple types of content including blog posts, status updates, videos and photos through a wide variety of social channels including blogs, Twitter, Facebook, Instagram, Tumblr and LinkedIn, among others. We are in the process of sunsetting all of our older platforms by the end of 2014 and moving all of our transactions to IZEAx.

Our platforms take the existing concepts of product placement and endorsements commonly found in movies, television and radio and apply them to the social web. We democratize the sponsorship process, allowing everyone from college students and stay at home moms to celebrities the opportunity to monetize their content, creativity and influence in social media. We direct bloggers, tweeters and other types of social media content creators to share information about

Table of Contents

companies, products, websites and events within their social media content streams. Advertisers benefit from buzz, traffic, awareness and sales, and creators earn cash compensation in exchange for their posts.

Results of Operations for the Three Months Ended September 30, 2014 Compared to the Three Months Ended September 30, 2013

	(unaudited)				
	Three Months Ended				
	September 30, 2014	September 30, 2013	\$ Change	% Change	
Revenue	\$1,931,671	\$1,565,851	\$365,820	23.4	%
Cost of sales	692,217	499,127	193,090	38.7	%
Gross profit	1,239,454	1,066,724	172,730	16.2	%
Operating expenses:					
General and administrative	2,320,142	1,655,727	664,415	40.1	%
Sales and marketing	482,045	63,436	418,609	659.9	%
Total operating expenses	2,802,187	1,719,163	1,083,024	63.0	%
Loss from operations	(1,562,733	) (652,439	) (910,294	) (139.5	)%
Other income (expense):					
Interest expense	(5,519	) (14,439	) 8,920	(61.8	)%
Loss on exchange of warrants and debt	—	(93,482	) 93,482	(100.0	)%
Change in fair value of derivatives and notes payable carried at fair value, net	2,250,344	(215,092	) 2,465,436	(1,146.2	)%
Other income (expense), net	3,278	150	3,128	2,085.3	%
Total other income (expense)	2,248,103	(322,863	) 2,570,966	796.3	%
Net income (loss)	\$685,370	\$ (975,302	) \$1,660,672	170.3	%

## Non-GAAP Financial Measures

To supplement our consolidated financial statements presented in accordance with generally accepted accounting principles in the United States ("U.S. GAAP"), we consider certain financial measures that are not prepared in accordance with U.S. GAAP, including Operating EBITDA. These non-GAAP financial measures are not based on any standardized methodology prescribed by GAAP. These non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with GAAP.

We believe that Operating EBITDA provides useful information to investors as it excludes transactions not related to the core cash operating business activities including non-cash transactions. We believe that excluding these transactions allows investors to meaningfully trend and analyze the performance of our core cash operations. All companies do not calculate EBITDA in the same manner, and Operating EBITDA as presented by IZEA may not be comparable to EBITDA presented by other companies. IZEA defines Operating EBITDA as earnings or loss before interest, taxes, depreciation and amortization, non-cash stock related compensation, gain or loss on asset disposals or impairment and all other income and expense items such as loss on exchanges and changes in fair value of derivatives, if applicable.

Table of Contents

Reconciliation of Net Income (Loss) to Operating EBITDA:	(unaudited)	
	Three Months Ended	
	September 30, 2014	September 30, 2013
Net income (loss)	\$ 685,370	\$ (975,302 )
Non-cash stock-based compensation	142,252	190,877
Non-cash stock issued for payment of services	18,750	301,803
Change in the fair value of derivatives	(2,250,344 )	215,092
Loss on exchange of warrants	—	93,482
Loss/(Gain) on disposal of equipment	16,593	—
Interest expense	5,519	14,439
Depreciation	24,903	11,449
Amortization of software development costs and other assets	47,406	4,500
Operating EBITDA	\$ (1,309,551 )	\$ (143,660 )

## Revenues

We derive revenue from three sources: revenue from an advertiser for the use of our network of social media content creators to fulfill advertiser sponsor requests for a blog post, tweet, click or action ("Sponsored Revenue"), revenue from the posting of targeted display advertising ("Media Revenue") and revenue derived from various service fees charged to advertisers and creators for services, maintenance and enhancement of their accounts ("Service Fee Revenue").

Revenues for the three months ended September 30, 2014 increased by \$365,820, or 23.4%, compared to the same period in 2013. The increase was attributable to a \$340,000 increase in our Sponsored Revenue, a \$44,000 decrease from Media Revenue and a \$70,000 increase in Service Fee Revenue. In the three months ended September 30, 2014, Sponsored Revenue was 87%, Media Revenue was 3% and Service Fee Revenue was 10% of total revenue compared to Sponsored Revenue of 86%, Media Revenue of 7% and Service Fee Revenue of 7% of total revenue in the three months ended September 30, 2013. The increase in Sponsored Revenue income was primarily attributable to our concentrated sales efforts toward larger IZEA managed campaigns rather than smaller advertiser self-service campaigns and generating repeat business from existing customers. Service fees increased in the three months ended September 30, 2014 due to more fees received from inactive self-service advertisers and creators. Media Revenue is decreasing due to a tactical shift from display advertising to focus on our Sponsored Revenue.

Our net bookings of \$2.02 million for the three months ended September 30, 2014 were approximately 8% higher than the net bookings of \$1.87 million for the three months ended September 30, 2013. Net bookings is a measure of sales and contracts minus any cancellations or refunds in a given period. Management uses net bookings as a leading indicator of future revenue recognition as revenue is typically recognized within 90 days of booking. We experienced higher bookings as a result of new customers, larger IZEA managed campaigns and an increase in repeat clients. These bookings are expected to translate into higher revenue in 2014 as compared to 2013.

## Cost of Sales and Gross Profit

Our cost of sales is comprised primarily of amounts paid to our social media content creators for fulfilling an advertiser's sponsor request for a blog post, tweet, click or action.

Cost of sales for the three months ended September 30, 2014 increased by \$193,090, or 38.7%, compared to the same period in 2013. The increase in cost of sales was primarily related to the increase in our sales.

Gross profit for the three months ended September 30, 2014 increased by \$172,730, or 16.2%, compared to the same period in 2013. Additionally, our gross profit as a percentage of revenue decreased by four percentage points from 68% for the three months ended September 30, 2013 to 64% for the same period in 2014. The gross profit decrease during the three months ended September 30, 2014 compared to 2013 was primarily attributable to the higher utilization of premium creators in campaigns in 2014 that provide us with lower margins.

## Table of Contents

### Operating Expenses

Operating expenses consist of general and administrative, and sales and marketing expenses. Total operating expenses for the three months ended September 30, 2014 increased by \$1,083,024, or 63.0%, compared to the same period in 2013. The increase was primarily attributable to higher personnel costs, depreciation and amortization expense and advertising and promotional costs.

General and administrative expenses consist primarily of payroll, general operating costs, public company costs, facilities costs, insurance, depreciation, professional fees, and investor relations fees. General and administrative expenses for the three months ended September 30, 2014 increased by \$664,415, or 40.1%, compared to the same period in 2013. The increase was primarily attributable to an increase in personnel costs of approximately \$586,000 as a result of the increase in the number of our personnel by nearly 85% and additional commissions paid to personnel for the increase in customer bookings; and an increase in depreciation and amortization expense of approximately \$73,000 as a result of the amortization of software development costs for IZEA Exchange (IZEAx), our new web-based advertising exchange platform, after its release in March 2014 and depreciation on additional equipment required to support the increase in our personnel.

IZEAx will be utilized both internally and externally to facilitate native advertising campaigns on a greater scale. We have filed a patent application covering important features of this platform which is currently pending approval. On March 17, 2014, we launched a public beta of IZEA.com powered by IZEAx. Personnel costs and all the other variable costs related to an increase in personnel are expected to increase throughout 2014 as we increase our sales efforts and continue to develop and support our IZEAx. Rent expense is expected to increase over our 2013 levels, because our rent for 2013 was lower than standard market rates pursuant to our one-year sublease. Additionally, with our personnel growth, we increased the amount of office space that we are leasing in Winter Park, Florida in the third quarter of 2014.

Sales and marketing expenses consist primarily of compensation for sales and marketing and related support resources, sales commissions and trade show expenses. Sales and marketing expenses for the three months ended September 30, 2014 increased by \$418,609 or 659.9%, compared to the same period in 2013. The increase was primarily attributable to increased planned promotional expenses related to the development of brand recognition for IZEA and additional trade shows in 2014. We contributed only \$63,000 towards promotional costs in 2013 while we were focusing our efforts and awaiting the completion of IZEAx.

### Other Income (Expense)

Other income (expense) consists primarily of interest expense, a loss on exchange of warrants and debt and the change in the fair value of derivatives and notes payable carried at fair value.

Interest expense during the three months ended September 30, 2014 decreased by \$8,920 compared to the same period in 2013 primarily due to lower debt balances in 2014 after all debt was converted into equity in our 2013 Private Placement pursuant to the terms of our various then outstanding notes payable or by separate agreement.

On May 4, 2012, we issued an unsecured 30-day promissory note to two of our existing shareholders in the principal amount of \$75,000. On August 15, 2013, we satisfied all of our remaining obligations under this note when the noteholders converted the \$75,000 in principal, plus \$12,366 of accrued interest, into 349,464 shares of common stock and a like number of warrants on the same terms and conditions as other investors in our 2013 Private Placement as discussed in Note 4 of the Financial Statements. Since there was no conversion provision in effect on the note at the time, the conversion was treated as an exchange wherein the difference between the fair value of the newly issued common stock and the carrying value of the note received in the exchange was recognized as a loss on exchange of

debt in the amount of \$93,482 during the three months ended September 30, 2013.

During the current periods and in prior periods, we entered into financing transactions that gave rise to derivative liabilities. These financial instruments are carried at fair value in our financial statements. Changes in the fair value of derivative financial instruments are required to be recorded in other income (expense) in the period of change. We recorded income of \$2,250,344 and \$207,462, resulting from the increase in the fair value of certain warrants during the three months ended September 30, 2014 and 2013, respectively. Additionally, we recorded expense from the increase in fair value of certain notes payable of during the three months ended September 30, 2013 in the amount of \$422,554. The net effect of these changes in fair values resulted in income of \$2,250,344 and expense of \$215,092 during the three months ended September 30, 2014 and 2013, respectively. We have no control over the amount of change in the fair value of our derivative instruments as this is a factor based on fluctuating interest rates and stock prices and other market conditions outside of our control. We have 35,910,554 warrants that are required to be fair valued each period. When the price of our stock decreases, it causes the fair

Table of Contents

value of our warrant liability in our consolidated balance sheets to decrease causing substantial income from the change in fair value in our consolidated statement of operations. Alternatively, when the price of our stock increases, it causes the fair value of our warrant liability to increase causing a substantial loss from the change in fair value.

## Net Income (Loss)

Net income for the three months ended September 30, 2014 was \$685,370, compared to a net loss of \$975,302 for the same period in 2013. The increase in net income was primarily the result of income recorded for the change in fair value of derivative financial instruments offset by increases in operating expenses as discussed above.

## Results of Operations for the Nine Months Ended September 30, 2014 Compared to the Nine Months Ended September 30, 2013

	(unaudited) Nine Months Ended				
	September 30, 2014	September 30, 2013	\$ Change	% Change	
Revenue	\$5,857,946	\$4,666,399	\$1,191,547	25.5	%
Cost of sales	1,998,406	1,846,130	152,276	8.2	%
Gross profit	3,859,540	2,820,269	1,039,271	36.9	%
Operating expenses:					
General and administrative	6,340,796	4,594,888	1,745,908	38.0	%
Sales and marketing	986,195	272,695	713,500	261.6	%
Total operating expenses	7,326,991	4,867,583	2,459,408	50.5	%
Loss from operations	(3,467,451)	(2,047,314)	(1,420,137)	(69.4)	%)
Other income (expense):					
Interest expense	(20,587)	(52,435)	31,848	(60.7)	%)
Loss on exchange of warrants and debt	—	(94,214)	94,214	(100.0)	%)
Change in fair value of derivatives and notes payable carried at fair value, net	5,625,555	(558,869)	6,184,424	(1,106.6)	%)
Other income (expense), net	7,677	230	7,447	3,237.8	%
Total other income (expense)	5,612,645	(705,288)	6,317,933	895.8	%
Net income (loss)	\$2,145,194	\$(2,752,602)	\$4,897,796	177.9	%

## Reconciliation of Net Income (Loss) to Operating EBITDA:

	(unaudited) Nine Months Ended		
	September 30, 2014	September 30, 2013	
Net income (loss)	\$2,145,194	\$(2,752,602)	)
Non-cash stock-based compensation	389,002	359,251	
Non-cash stock issued for payment of services	147,860	416,768	
Change in the fair value of derivatives	(5,625,555)	558,869	)
Loss on exchange of warrants	—	94,214	
Loss/(Gain) on disposal of equipment	16,192	—	
Interest expense	20,587	52,435	
Depreciation	65,683	36,377	
Amortization of software development costs and other assets	94,812	13,500	
Operating EBITDA	\$(2,746,225)	\$(1,221,188)	)





## Table of Contents

### Revenues

We derive revenue from three sources: revenue from an advertiser for the use of our network of social media content creators to fulfill advertiser sponsor requests for a blog post, tweet, click or action ("Sponsored Revenue"), revenue from the posting of targeted display advertising ("Media Revenue") and revenue derived from various service fees charged to advertisers and creators for services, maintenance and enhancement of their accounts ("Service Fee Revenue").

Revenues for the nine months ended September 30, 2014 increased by \$1,191,547, or 25.5%, compared to the same period in 2013. The increase was attributable to a \$1,141,000 increase in our Sponsored Revenue, a \$76,000 decrease in Media Revenue and a \$127,000 increase in Service Fee Revenue. In the nine months ended September 30, 2014, Sponsored Revenue was 89%, Media Revenue was 4% and Service Fee Revenue was 7% of total revenue compared to Sponsored Revenue of 88%, Media Revenue of 6% and Service Fee Revenue of 6% of total revenue in the nine months ended September 30, 2013. The increase in Sponsored Revenue income was primarily attributable to our concentrated sales efforts toward larger IZEA managed campaigns rather than smaller advertiser self-service campaigns and generating repeat business from existing customers. Service fees increased in the nine months ended September 30, 2014 due to additional fees received from inactive self-service advertisers and creators. Media Revenue is decreasing due to a tactical shift from display advertising to focus on our Sponsored Revenue.

Our net bookings of \$6.3 million for the nine months ended September 30, 2014 were approximately 18% higher than the net bookings of \$5.3 million for the nine months ended September 30, 2013. Net bookings is a measure of sales and contracts minus any cancellations or refunds in a given period. Management uses net bookings as a leading indicator of future revenue recognition as revenue is typically recognized within 90 days of booking. We experienced higher bookings as a result of new customers, larger IZEA managed campaigns and an increase in repeat clients. These bookings are expected to translate into higher revenue in 2014 as compared to 2013.

### Cost of Sales and Gross Profit

Our cost of sales is comprised primarily of amounts paid to our social media content creators for fulfilling an advertiser's sponsor request for a blog post, tweet, click or action.

Cost of sales for the nine months ended September 30, 2014 increased by \$152,276, or 8.2%, compared to the same period in 2013. The increase in cost of sales was primarily related to the increase in our sales.

Gross profit for the nine months ended September 30, 2014 increased by \$1,039,271, or 36.9%, compared to the same period in 2013. Additionally, our gross profit as a percentage of revenue increased by six percentage points from 60% for the nine months ended September 30, 2013 to 66% for the same period in 2014. The gross profit increase during the nine months ended September 30, 2014 compared to 2013 was primarily attributable to an increase in larger advertisers using our managed campaign services, where we manage all aspects of their sponsored social advertising, as compared to smaller or self-service advertisers who manage their own campaigns using our platforms. Additionally, a larger portion of revenue was derived from service fees during the nine months ended September 30, 2014, which have little or no cost associated with them.

### Operating Expenses

Operating expenses consist of general and administrative, and sales and marketing expenses. Total operating expenses for the nine months ended September 30, 2014 increased by \$2,459,408, or 50.5%, compared to the same period in 2013. The increase was primarily attributable to higher personnel and related costs, stock compensation and investor relations expenses, along with higher travel and promotional marketing expenses for our new platform.

General and administrative expenses consist primarily of payroll, general operating costs, public company costs, facilities costs, insurance, depreciation, professional fees, and investor relations fees. General and administrative expenses for the nine months ended September 30, 2014 increased by \$1,745,908, or 38.0%, compared to the same period in 2013. The increase was primarily attributable to an increase in personnel costs of approximately \$1,114,000 as a result of the increase in the number of our personnel by nearly 85% and additional commissions paid to personnel for the increase in customer bookings; an increase in investor relations expenses of approximately \$103,000 due to the retainer of several investor relation firms to help further promote our Company in the current year; a \$94,000 increase in software and subscription costs as a result of increased personnel and additional systems used to manage our growing business; a \$109,000 increase in travel costs related to the launch tour of our new platform and increase in outside personnel; an increase in non-cash stock compensation expense of approximately \$30,000 due to several large option grants in the third quarter of 2013 that are vesting in the current year; a

## Table of Contents

\$127,000 increase in depreciation and amortization expense as a result of the amortization of software development costs for IZEA Exchange (IZEAx); and a \$81,000 increase in rent for our new facilities.

Sales and marketing expenses consist primarily of compensation for sales and marketing and related support resources, sales commissions and trade show expenses. Sales and marketing expenses for the nine months ended September 30, 2014 increased by \$713,500 or 261.6%, compared to the same period in 2013. The increase was primarily attributable to increased planned promotional expenses related to the launch of IZEAx and development of brand recognition for IZEA.

### Other Income (Expense)

Other income (expense) consists primarily of interest expense, a loss on exchange of warrants and debt and the change in the fair value of derivatives and notes payable carried at fair value.

Interest expense during the nine months ended September 30, 2014 decreased by \$31,848 compared to the same period in 2013 primarily due to lower debt balances in 2014 after all debt was converted into equity in our 2013 Private Placement pursuant to the terms of our various then outstanding notes payable or by separate agreement.

During the nine months ended September 30, 2013, we recognized a \$94,214 loss on exchange when we settled the payment of a \$75,000 note payable and accrued interest thereon through an exchange of shares of our common stock and we redeemed certain warrants to purchase an aggregate of 4,546 shares of common stock for the same number of shares of our common stock without receiving any cash consideration for the exchange.

During the current periods and in prior periods, we entered into financing transactions that gave rise to derivative liabilities. These financial instruments are carried at fair value in our financial statements. Changes in the fair value of derivative financial instruments are required to be recorded in other income (expense) in the period of change. We recorded income of \$5,625,555 and \$207,682, resulting from the increase in the fair value of certain warrants during the nine months ended September 30, 2014 and 2013, respectively. Additionally, we recorded a \$765,907 expense from the increase in fair value of certain notes payable and a \$644 expense from the increase in fair value of compound embedded derivatives during the nine months ended September 30, 2013. The net effect of these changes in fair values resulted in income of \$5,625,555 and expense of \$558,869 during the nine months ended September 30, 2014 and 2013, respectively. We have no control over the amount of change in the fair value of our derivative instruments as this is a factor based on fluctuating interest rates and stock prices and other market conditions outside of our control. We have 35,910,554 warrants that are required to be fair valued each period. When the price of our stock decreases, it causes the fair value of our warrant liability in our consolidated balance sheets to decrease causing substantial income from the change in fair value in our consolidated statement of operations. Alternatively, when the price of our stock increases, it causes the fair value of our warrant liability to increase causing a substantial loss from the change in fair value.

### Net Income (Loss)

Net income for the nine months ended September 30, 2014 was \$2,145,194, which increased from a net loss of \$2,752,602 for the same period in 2013. The increase in net income was primarily the result of income recorded for the change in fair value of derivative financial instruments offset by increases in operating expenses as discussed above.

### Liquidity and Capital Resources

Our cash position was \$7,879,918 as of September 30, 2014 as compared to \$530,052 as of December 31, 2013, an increase of \$7,349,866 primarily as a result of proceeds received in our 2014 Private Placement described below. We have incurred significant net losses and negative cash flow from operations since our inception which has resulted in a total accumulated deficit of \$23,980,220 as of September 30, 2014.

Cash used for operating activities was \$3,268,674 during the nine months ended September 30, 2014 and was primarily a result of our loss from operations during the period of \$3,467,451. Cash used for investing activities was \$377,570 during the nine months ended September 30, 2014 due primarily to the capitalization of software development costs for IZEAx that launched in March 2014 and increases in computer equipment purchases. Cash provided by financing activities was \$10,996,110 during the nine months ended September 30, 2014 and was primarily a result of net proceeds of \$10,932,912 from the sale of our common stock, as discussed below. Financing activities were reduced by loan costs and principal payments on our capital leases of \$49,602. In July 2014, 450,000 of our \$0.25 warrants issued in our 2013 Private Placement were exercised

## Table of Contents

for total proceeds of \$112,500 and employee stock options were exercised into 1,250 shares of common stock for cash proceeds of \$300.

To date, we have financed our operations through internally generated revenue from operations and the sale of our equity securities.

On February 21, 2014, we completed a private placement pursuant to a Purchase Agreement dated as of February 12, 2014, for the issuance and sale of 34,285,728 shares of our common stock, at a purchase price of \$0.35 per share for gross proceeds of \$12,000,000. As part of the private placement, the investors received warrants to purchase up to 17,142,864 shares of our common stock at an exercise price of \$0.35 per share and warrants to purchase up to another 17,142,864 shares of our common stock at an exercise price of \$0.50 per share. The warrants expire on February 21, 2019, five years after the date on which they were issued. The net proceeds from the private placement, following the payment of offering-related expenses, are being used by us to focus on revenue growth through the acceleration of our sales and client relations activities and marketing initiatives, establishment of strategic partnerships and continuation of technology and engineering enhancements to our platforms, as well as to fund our working capital and capital expenditure requirements.

The effect of the above transactions has provided us with a positive working capital balance and sufficient cash reserves for the foreseeable future.

## Off-Balance Sheet Arrangements

We do not engage in any activities involving variable interest entities or off-balance sheet arrangements.

## Critical Accounting Policies and Use of Estimates

The preparation of the accompanying financial statements and related disclosures in conformity with U.S. GAAP requires us to make judgments, assumptions and estimates that affect the amounts reported in the accompanying financial statements and the accompanying notes. The preparation of these financial statements requires managements to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. When making these estimates and assumptions, we consider our historical experience, our knowledge of economic and market factors and various other factors that we believe to be reasonable under the circumstances. Actual results could differ from these estimates. The following critical accounting policies are significantly affected by judgments, assumptions and estimates used in the preparation of the financial statements.

Accounts receivable are customer obligations due under normal trade terms. Uncollectibility of accounts receivable is not significant since most customers are bound by contract and are required to fund us for all the costs of an “opportunity,” defined as an order created by an advertiser for a creator to write about the advertiser’s product. If a portion of the account balance is deemed uncollectible, we will either write-off the amount owed or provide a reserve based on the uncollectible portion of the account. Management determines the collectibility of accounts by regularly evaluating individual customer receivables and considering a customer’s financial condition, credit history and current economic conditions. We do not have a reserve for doubtful accounts as of September 30, 2014. We believe that this estimate is reasonable, but there can be no assurance that the estimate will not change as a result of a change in economic conditions or business conditions within the industry, the individual customers or our company. Any adjustments to this account are reflected in the consolidated statements of operations as a general and administrative expense. Bad debt expense was less than 1% of revenue for the nine months ended September 30, 2014 and 2013.

We derive revenue from three sources: revenue from an advertiser for the use of the our network of social media content creators to fulfill advertiser sponsor requests for a blog post, tweet, click or action ("Sponsored Revenue"), revenue from the posting of targeted display advertising ("Media Revenue") and revenue derived from various service fees charged to advertisers and creators ("Service Fee Revenue"). Sponsored revenue is recognized and considered earned after an advertiser's opportunity is posted on our online platform and their request was completed and content listed, as applicable, by our creators for a requisite period of time. The requisite period ranges from 3 days for an action or tweet to 30 days for a blog. Advertisers may prepay for services by placing a deposit in their account with us. The deposits are typically paid by the advertiser via check, wire transfer or credit card. Deposits are recorded as unearned revenue until earned as described above. Media Revenue is recognized and considered earned when our creators place targeted display advertising in blogs. Service fees are recognized immediately when the maintenance, enhancement or other service is performed for an advertiser or creator. Service fees charged to advertisers are primarily related to inactivity fees for dormant accounts and fees for additional services

Table of Contents

outside of sponsored revenue. Service fees charged to creators include upgrade account fees for obtaining greater visibility to advertisers in advertiser searches in our platforms, early cash-out fees if a creator wishes to take proceeds earned for services from their account when the account balance is below certain minimum balance thresholds and inactivity fees for dormant accounts. All of our revenue is generated through the rendering of services and is recognized under the general guidelines of SAB Topic 13 A.1 which states that revenue will be recognized when it is realized or realizable and earned. We consider our revenue as generally realized or realizable and earned once (i) persuasive evidence of an arrangement exists, (ii) services have been rendered, (iii) our price to the advertiser or customer is fixed (required to be paid at a set amount that is not subject to refund or adjustment) and determinable, and (iv) collectibility is reasonably assured. We record revenue on the gross amount earned since we generally are the primary obligor in the arrangement, establish the pricing and determine the service specifications.

Stock-based compensation is measured at grant date, based on the fair value of the award, and is recognized as an expense over the employee's requisite service period. We estimate the fair value of each stock option as of the date of grant using the Black-Scholes pricing model. Options typically vest ratably over four years with one-fourth of options vesting one year from the date of grant and the remaining options vesting monthly, in equal increments over the remaining three-year period and generally have five or ten-year contract lives. We estimate the fair value of our common stock using the closing stock price of our common stock as quoted in the OTCQB marketplace on the date of the agreement. We estimate the volatility of our common stock at the date of grant based on the volatility of comparable peer companies that are publicly traded and have had a longer trading history than us. We determine the expected life based on historical experience with similar awards, giving consideration to the contractual terms, vesting schedules and post-vesting forfeitures. We use the risk-free interest rate on the implied yield currently available on U.S. Treasury issues with an equivalent remaining term approximately equal to the expected life of the award. We have never paid any cash dividends on our common stock and do not anticipate paying any cash dividends in the foreseeable future. We estimate forfeitures when recognizing compensation expense and this estimate of forfeitures is adjusted over the requisite service period based on the extent to which actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures are recognized through a cumulative catch-up adjustment, which is recognized in the period of change. Changes also impact the amount of unamortized compensation expense to be recognized in future periods.

The following table shows the number of options granted under our May 2011 and August 2011 Equity Incentive Plans and the assumptions used to determine the fair value of those options during the quarterly periods in 2013 and through September 30, 2014:

## 2011 Equity Incentive Plans - Options Granted

Period Ended	Total Options Granted	Weighted Average Fair Value of Common Stock	Weighted Average Expected Term	Weighted Average Volatility	Weighted Average Risk Free Interest Rate	Weighted Average Fair Value of Options Granted
March 31, 2013	2,170,834	\$0.25	10 years	52.72%	1.91%	\$0.16
June 30, 2013	975,250	\$0.25	6 years	51.84%	0.91%	\$0.12
September 30, 2013	4,493,978	\$0.35	10 years	51.72%	2.74%	\$0.24
December 31, 2013	980,000	\$0.34	5 years	47.55%	1.37%	\$0.14
March 31, 2014	330,000	\$0.48	5 years	43.32%	1.60%	\$0.19
June 30, 2014	1,066,680	\$0.46	5 years	41.38%	1.66%	\$0.18
September 30, 2014	3,082,267	\$0.37	5 years	40.37%	1.75%	\$0.14

There were 12,122,036 total options outstanding with a weighted average exercise price of \$0.46 per share and 3,589,722 exercisable options outstanding with a weighted average exercise price of \$0.63 per share as of September 30, 2014. There is no aggregate intrinsic value on the exercisable, outstanding options as of September 30, 2014 since the weighted average exercise price per share exceeded the market price of \$0.37 of our common stock on such date.

We account for derivative instruments in accordance with ASC 815, Derivatives and Hedging , which requires additional disclosures about the our objectives and strategies for using derivative instruments, how the derivative instruments and related hedged items are accounted for, and how the derivative instruments and related hedging items affect the financial statements. We do not use derivative instruments to hedge exposures to cash flow, market or foreign currency risk. Terms of convertible debt and equity instruments are reviewed to determine whether or not they contain embedded derivative instruments that are required under ASC 815 to be accounted for separately from the host contract, and recorded on the balance



## Table of Contents

sheet at fair value. The fair value of derivative liabilities, if any, is required to be revalued at each reporting date, with corresponding changes in fair value recorded in current period operating results. Pursuant to ASC 815, an evaluation of specifically identified conditions is made to determine whether the fair value of warrants issued is required to be classified as equity or as a derivative liability.

We record a beneficial conversion feature (“BCF”) related to the issuance of convertible debt and equity instruments that have conversion features at fixed rates that are in-the-money when issued, and the fair value of warrants issued in connection with those instruments. The BCF for the convertible instruments is recognized and measured by allocating a portion of the proceeds to warrants, based on their relative fair value, and as a reduction to the carrying amount of the convertible instrument equal to the intrinsic value of the conversion feature. The discounts recorded in connection with the BCF and warrant valuation are recognized (a) for convertible debt as interest expense over the term of the debt, using the effective interest method or (b) for preferred stock as dividends at the time the stock first becomes convertible.

### Recent Accounting Pronouncements

There are several new accounting pronouncements issued by the Financial Accounting Standards Board (“FASB”) which are not yet effective. Management does not believe any of these accounting pronouncements will have a material impact on our financial position or operating results.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP.

The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). We are currently evaluating the impact of the adoption of ASU 2014-09 on our consolidated financial statements and have not yet determined the method by which we will adopt the standard in 2017.

### ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable to smaller reporting companies.

### ITEM 4 – CONTROLS AND PROCEDURES

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is

accumulated and communicated to our management, including our principal executive and financial officer, as appropriate to allow timely decisions regarding required disclosures.

In designing and evaluating the disclosure controls and procedures, our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Furthermore, controls and procedures could be circumvented by the individual acts of some persons, by collusion or two or more people or by management override of the control. Misstatements due to error or fraud may occur and not be detected on a timely basis.

Evaluation of Disclosure Controls and Procedures

## Table of Contents

In connection with the preparation of this quarterly report on Form 10-Q for the period ended September 30, 2014, an evaluation was performed under the supervision and with the participation of the Company's management including our Chief Executive Officer ("CEO") and Principal Financial and Accounting Officer ("PFO") to determine the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of September 30, 2014. Based on this evaluation, our management concluded that our disclosure controls and procedures were effective as of September 30, 2014 to provide reasonable assurance that the information required to be disclosed by us in reports or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to management, including the Company's principal executive and financial officers, as appropriate, to allow timely decisions regarding required disclosure.

### Changes in Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). Internal control over financial reporting is a process designed by, or under the supervision of, our principal executive officer and principal financial officer and effected by our Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes policies and procedures that:

- (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the Company's transactions;
- (ii) provide reasonable assurance that transactions are recorded as necessary for the preparation of our financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are made only in accordance with authorizations of our management and directors; and
- (iii) provide reasonable assurance regarding prevention or timely detection of any unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect financial statement misstatements. Also, projections of any evaluation of internal control effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

There were no changes in our internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the quarter ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Table of Contents

### PART II - OTHER INFORMATION

#### ITEM 1 – LEGAL PROCEEDINGS

From time to time, we may become involved in various lawsuits and legal proceedings that arise in the ordinary course of business. Litigation is, however, subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. Other than as described below, we are currently not aware of any legal proceedings or claims that we believe would or could have, individually or in the aggregate, a material adverse effect on us.

On October 17, 2012, Blue Calypso, Inc. filed a complaint against us in the U.S. District Court for the Eastern District of Texas. Blue Calypso's complaint alleges that we infringe on their patents related to peer-to-peer advertising between mobile communication devices and seeks unspecified damages. On July 19, 2013, Blue Calypso's case against us was consolidated, along with patent infringement cases against Yelp, Inc. and Foursquare Labs, Inc., into Blue Calypso, Inc. v. Groupon, Inc. for all pretrial purposes, including discovery and claim construction.

On December 16, 2013, the Patent Trial and Appeal Board's (PTAB) instituted a Covered Business Method Review (CBMR) for three of the five patents Blue Calypso asserts in its case against IZEA. In its decisions granting the CBMRs, the PTAB explained that several of Blue Calypso's asserted patents are likely invalid. In particular, the PTAB found it more likely than not that each of these three patents was invalid based on two independent grounds of anticipation, and one ground of obviousness. Additionally, the PTAB preliminarily found it more likely than not that many of the claims of one of Blue Calypso's patents were invalid due to a lack of written description. On January 17, 2014, the PTAB expanded its review to all five of Blue Calypso's assert patents. The PTAB's final decision regarding the asserted patents is expected by the end of this year. On January 16, 2014, the court granted a joint motion to stay Blue Calypso's patent infringement case until the PTAB's review of Blue Calypso's asserted patents is complete.

At this stage, we do not have an estimate of the likelihood or the amount of any potential exposure to us. We believe that there is no merit to this suit and continue to vigorously defend ourselves against Blue Calypso's allegations.

#### ITEM 1A – RISK FACTORS

In addition to the information set forth under Item 1A of Part I to our Annual Report on Form 10-K for the year ended December 31, 2013, information at the beginning of Management's Discussion and Analysis entitled "Special Note Regarding Forward-Looking Information" and updates noted below, investors should consider that there are numerous and varied risks, known and unknown, that may prevent us from achieving our goals. If any of these risks actually occur, our business, financial condition or results of operation may be materially and adversely affected. In such case, the trading price of our common stock could decline and investors could lose all or part of their investment.

##### Risks Related to our Business and Industry

We have a history of losses, expect future losses and cannot assure you that we will achieve profitability or obtain the financing necessary for future growth.

We have incurred significant net losses and negative cash flow from operations since our inception which has resulted in a total accumulated deficit of \$23,980,220 as of September 30, 2014. Although our revenue has increased since inception, we have not achieved profitability and cannot be certain that we will be able to sustain these growth rates or

realize sufficient revenue to achieve profitability. If we achieve profitability, we may not be able to sustain it.

We are developing a new platform to process all of our existing business transactions and grow our operations, but cannot provide any assurance regarding its commercial success.

We are developing a new platform called the IZEA Exchange (IZEAx) which is currently in public beta. IZEAx is designed to provide a unified ecosystem that enables the creation of multiple types of content through a wide variety of social channels. IZEAx is a brand-new system, engineered from the ground-up to replace all of our current platforms with an integrated offering that is improved and more efficient for the company to operate. Our intention is to focus all of our engineering resources on the IZEAx platform for the foreseeable future. We are spending a significant amount of time and resources on the development of this platform, but we cannot provide any assurances of its short or long-term commercial success or growth. A portion of the proceeds of our 2014 Private Placement is being used for completion of the IZEAx

Table of Contents

platform, which is scheduled for continued updates and enhancements into the foreseeable future. There is no assurance that the amount of money being allocated for the platform will be sufficient to complete it, or that such completion will result in significant revenues or profit for us. If our advertisers and creators do not perceive this platform to be of high value and quality, we may not be able to retain them or acquire new advertisers and creators. Additionally, if existing or future competitors develop or offer products or services that provide significant performance, price, creative or other advantages over this platform, demand for IZEAx may decrease and our business, prospects, results of operations and financial condition could be negatively affected.

Exercise of stock options, warrants and other securities will dilute your percentage of ownership and could cause our stock price to fall.

As of November 11, 2014, we have 57,497,631 shares of common stock issued, outstanding stock options to purchase 12,079,108 shares of common stock at an average price of \$0.46 per share, outstanding warrants to purchase 53,942,749 shares of common stock at an average price of \$0.41 per share, and 1,834,023 shares of vested, yet unissued, shares of restricted common stock. Additionally, we have reserved shares to issue stock options, restricted stock or other awards to purchase or receive up to 8,005,908 shares of common stock under our May 2011 Equity Incentive Plan and 1,500,000 shares of common stock under our 2014 Employee Stock Purchase Plan. In the future, we may grant additional stock options, warrants and convertible securities. The exercise, conversion or exchange of stock options, warrants or convertible securities will dilute the percentage ownership of our other stockholders. Sales of a substantial number of shares of our common stock could cause the price of our common stock to fall and could impair our ability to raise capital by selling additional securities.

There may be substantial sales of our common stock under the prospectus relating to our 2014 Private Placement, which could cause our stock price to drop.

We agreed with the investors in our 2014 Private Placement to file a shelf registration statement with the SEC with respect to the resale of all of the shares of our common stock, as well as shares of common stock issuable upon the exercise of warrants, purchased by investors. We filed a registration statement on Form S-1 on April 7, 2014 and it was declared effective on May 14, 2014. The registration statement included a total of 68,571,456 shares of our common stock (of which 34,285,728 shares are presently outstanding and 34,285,728 shares are issuable upon the exercise of warrants). There are currently no agreements or understandings in place with these selling stockholders to restrict their sale of those shares. Sales of a substantial number of shares of our common stock by the selling stockholders over a short period of time could cause the market price of our common stock to drop and could impair our ability to raise capital in the future by selling additional securities.

Holder of warrants issued in our 2014 Private Placement have anti-dilution adjustment rights that, if triggered, could dilute the ownership interests of our existing common stockholders.

Holder of our warrants to purchase 17,893,375 shares of common stock at an exercise price of \$0.35 per share and warrants to purchase 17,893,375 shares at an exercise price of \$0.50 per share issued in our 2014 Private Placement have anti-dilution adjustment rights that, if triggered, could dilute the interests of our common stockholders. The warrants contain weighted average anti-dilution protection for warrant holders if we sell another equity or equity-linked security at a price per share lower than the respective exercise prices during the five-year term of the warrants. Additionally, the warrants do not contain a negotiated floor for the exercise price. As compared with a full ratchet anti-dilution provision, which resets the exercise price at the lowest price in any subsequent sale of stock, a weighted average anti-dilution provision takes into account both the lower price and the number of shares issued at the lower price. The triggering of these anti-dilution provisions could result in the issuance of a substantial number of additional shares of common stock upon exercise of the warrants, which would dilute the ownership interests of our existing common stockholders.

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

Issuance of Common Stock for Services

Effective January 1, 2014, we entered into a one-year agreement to pay \$7,500 per month and 100,000 shares of restricted stock per quarter to a firm to provide investor relations services. In accordance with the agreement, we issued 100,000 shares of restricted common stock valued at \$30,110 on January 1, 2014 and 100,000 shares of restricted common stock valued at \$52,000 on April 1, 2014. This agreement was canceled in June 2014 and no further amounts are owed. The foregoing issuances of shares were made in reliance upon the exemption from registration provided by Section 4(a)(2) of the Securities Act of 1933, as amended.

Table of Contents

ITEM 3 – DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4 – MINE SAFETY DISCLOSURES

Not applicable

ITEM 5 - OTHER INFORMATION

None

32

---



Table of Contents

EXHIBITS

- 3.1 Articles of Incorporation (Incorporated by reference to the Company's registration statement on Form S-1 filed with the SEC on July 2, 2010).
- 3.2 Certificate of Amendment to the Articles of Incorporation (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on February 15, 2013).
- 3.3 Certificate of Amendment to the Articles of Incorporation (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on May 16, 2011).
- 3.4 Bylaws (Incorporated by reference to the Company's registration statement on Form S-1 filed with the SEC on July 2, 2010).
- 3.5 Certificate of Designation (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on May 27, 2011).
- 3.6 Amendment to Certificate of Designation (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on May 27, 2011).
- 3.7 Certificate of Change of IZEA, Inc., filed with the Nevada Secretary of State on July 30, 2012 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on August 1, 2012).
- 3.8 Certificate of Amendment to Articles of Incorporation filed with the Secretary of State of the State of Nevada on April 17, 2014 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on April 18, 2014).
- 4.1 Form of Warrant to Purchase Common Stock of IZEA, Inc. issued to Investors in the 2013 Private Placement (Incorporated by reference to Form 8-K, filed with the SEC on August 21, 2013).
- 4.2 Form of Warrant to Purchase Common Stock of IZEA, Inc. issued to Investors in the 2014 Private Placement (Incorporated by reference to Form 8-K, filed with the SEC on February 24, 2014).
- 10.1 Agreement between the Company and Mitchel Laskey, dated December 26, 2012 (Incorporated by reference to Form 10-K, filed with the SEC on March 29, 2013).
- 10.2 Amended 2011 Equity Incentive Plan as of February 6, 2013 (Incorporated by reference to Form 10-K, filed with the SEC on March 29, 2013).
- 10.3 Financing Agreement between the Company and Bridge Bank, dated March 1, 2013 (Incorporated by reference to Form 10-K, filed with the SEC on March 29, 2013).
- 10.4 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated April 11, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on April 16, 2013).
- 10.5 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated May 22, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on May 28, 2013).
- 10.6 Loan Extension between IZEA, Inc. and Brian W. Brady dated May 31, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on June 3, 2013).
- 10.7 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated June 7, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on June 21, 2013).
- 10.8 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated June 14, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on June 21, 2013).
- 10.9 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated July 25, 2013 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on July 30, 2013).
- 10.10 Loan Agreement and Promissory Note between IZEA, Inc. and Brian W. Brady dated August 12, 2013 (Incorporated by reference to the Company's Quarterly Report on Form 10-Q filed with the SEC on

August 14, 2013).

- 10.11 Form of Securities Purchase Agreement executed by IZEA, Inc. and Investors in the 2013 Private Placement (Incorporated by reference to Form 8-K, filed with the SEC on August 21, 2013).
- 10.12 Form of Securities Purchase Agreement, dated as of February 12, 2014, by and among IZEA, Inc. and the Investors (Incorporated by reference to Form 8-K, filed with the SEC on February 19, 2014).
- 10.13 Form of Registration Rights Agreement, dated as of February 21, 2014, among IZEA, Inc. and each of the Investors (Incorporated by reference to Form 8-K, filed with the SEC on February 24, 2014).
- 10.14 Amended and Restated 2011 Equity Incentive Plan as of April 16, 2014 (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on April 18, 2014).

33

---

Table of Contents

10.15		2014 Employee Stock Purchase Plan (Incorporated by reference to the Company's current report on Form 8-K filed with the SEC on April 18, 2014).
10.16		Employment Agreement between IZEA, Inc. and LeAnn Hitchcock dated August 25, 2014.
31.1	*	Section 302 Certification of Principal Executive Officer
31.2	*	Section 302 Certification of Principal Financial and Accounting Officer
32.1	**	Section 906 Certification of Principal Executive Officer
32.2	**	Section 906 Certification of Principal Financial and Accounting Officer
		The following materials from IZEA, Inc.'s Quarterly Report on Form 10-Q for the nine months ended September 30, 2014 are formatted in XBRL (eXtensible Business Reporting Language): (i) the
101	***	Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statement of Stockholders' Equity (Deficit), (iv) the Consolidated Statements of Cash Flow, and (iv) Notes to the Consolidated Financial Statements.

\* Filed herewith.

In accordance with Item 601 of Regulation S-K, this Exhibit is hereby furnished to the SEC as an accompanying document and is not deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that Section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933.

In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

Table of Contents

SIGNATURES

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

IZEA, Inc.  
a Nevada corporation

November 13, 2014

By: /s/ Edward H. Murphy  
Edward H. Murphy  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

November 13, 2014

By: /s/ LeAnn C. Hitchcock  
LeAnn C. Hitchcock  
Chief Financial Officer  
(Principal Financial and Accounting Officer)